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Law Companion Ruling

Non-arm's length income – expenditure incurred under a non-arm's length arrangement

This is a draft consolidation outlining proposed changes to Law Companion Ruling LCR 2021/2 *Non-arm's length income – expenditure incurred under a non-arm's length arrangement* to outline the ATO view as to how the amendments to section 295-550 of the *Income Tax Assessment Act 1997*, made under the *Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Act 2024* apply to a small complying super fund (a complying superannuation entity with no more than 6 members including a self-managed super fund) that incurs non-arm's length expenditure (or where expenditure is not incurred) in gaining or producing ordinary or statutory income. The Addendum which makes these changes, when finalised, will be a public ruling for the purposes of the *Taxation Administration Act 1953*.

📌 Relying on this draft Ruling

This publication is a draft for public comment. It represents the Commissioner's preliminary view on how a relevant provision could apply.

If this draft Ruling applies to you and you rely on it reasonably and in good faith, you will not have to pay any interest or penalties in respect of the matters covered if this draft Ruling turns out to be incorrect and you underpay your tax as a result. However, you may still have to pay the correct amount of tax.

Table of Contents	Paragraph
What this draft Ruling is about	1
Date of effect	4
Overview of 2024 amendments to the non-arm's length income provisions	5
<i>Non-arm's length component</i>	6A
<i>Other changes made by the 2024 amendments – for complying superannuation funds</i>	7
Non-arm's length expenditure – requirements of paragraphs 295-550(1)(b) and (c), paragraphs 295-550(5)(b) and (c), and subsections 295-550(8) and (9)	9A
<i>Specific non-arm's length expense – paragraphs 295-550(1)(b) and 295-550(1)(c)</i>	10
<i>General non-arm's length expense – subsections 295-550(8) and (9)</i>	11A
Non-arm's length expenditure – requirements of paragraphs 295-550(5)(b) and (c)	12
Application of non-arm's length expenditure provisions	14
<u>Example 1 – non-arm's length expenditure was incurred to acquire an asset – NALI</u>	22
<u>Example 2 – non-arm's length expenditure incurred has a nexus to all income of the fund – NALI</u>	24
Purchase of an asset under a non-arm's length arrangement	27
<u>Example 3 – purchase less than market value and no in specie contribution – NALI</u>	31

LCR 2021/2DCStatus: **draft only – for comment**

<u>Example 4 – purchase financed through a limited recourse borrowing arrangement on non-arm’s length terms – NALI</u>	34
<u>Example 5 – part purchase and part in specie contribution at market value – not NALI</u>	38
Capacity in which activities are performed – self-managed superannuation funds	40
Whether dealings are on a non-arm’s length basis	49
<u>Example 6 – internal arrangement within an SMSF – trustee provides services to the SMSF</u>	54
<u>Example 7 – SMSF trustee carrying out duties – trustee capacity</u>	55
<u>Example 8 – third party providing services – discounts</u>	58
<u>Example 9 – SMSF trustee carrying out duties – different capacities</u>	61
<u>Example 10 – SMSF trustee carrying out duties – individual capacity</u>	70
<u>Example 11 – SMSF trustee carrying out duties – individual capacity</u>	72
Expenditure relating to a superannuation entity as a beneficiary of a trust	76
<u>Example 12 – SMSF incurs non-arm’s length expenditure in acquiring a fixed entitlement in a unit trust</u>	77
Application of the market value substitution rules	81
<u>Example 13 – market value substitution rules (CGT consequences for the transferor and the fund)</u>	83
Appendix 1 – Compliance approach	88
Appendix 2 – Your comments	95

What this draft Ruling is about

1. This draft Ruling^{A1} clarifies how the amendments to section 295-550 of the *Income Tax Assessment Act 1997* (ITAA 1997)¹ ([2024 amendments](#)) operate in a scheme where the parties do not deal with each other at arm’s length and the trustee of a [small complying superannuation fund \(a complying superannuation entity² with no more than 6 members including a self-managed superannuation fund \(SMSF\)\)](#), incurs non-arm’s length expenditure (or where expenditure is not incurred) in gaining or producing ordinary or statutory income. ~~The amendments apply in relation to income derived in the 2018–19 income year and later income years, regardless of whether the scheme was entered into before 1 July 2018.~~

^{A1} For readability, all further references to 'this Ruling' refer to the Ruling as it will read when finalised. Note that this Ruling will not take effect until finalised.

¹ See [Schedule 7 to the Treasury Laws Amendment \(Support for Small Business and Charities and Other Measures\) Act 2024 \(TLA Act 2024\)](#) ~~Treasury Laws Amendment (2018 Superannuation Measures No. 1) Act 2019 (TLA Act 2019)~~.

² A 'complying superannuation entity' is defined in subsection 995-1(1) of the ITAA 1997 as a complying superannuation fund, a complying approved deposit fund, or a pooled superannuation trust. While acknowledging that it is the trustee of the complying superannuation entity that derives the relevant income and incurs the relevant expenditure, for the purposes of readability, this Ruling refers to how the provisions apply to a complying superannuation fund. However, the provisions apply equally to a trustee of a complying approved deposit fund and a pooled superannuation trust.

³ ~~[Omitted.] Section 4 of Schedule 2 to the TLA Act 2019.~~

LCR 2021/2DC

Status: **draft only – for comment**

1B. The 2024 amendments apply in relation to income derived and a loss, outgoing or expenditure that is incurred (or not incurred but might have expected to be incurred) in the 2018–19 income year and later income years. These amendments supersede amendments made by *Treasury Laws Amendment (2018 Superannuation Measures No. 1) Act 2019*.^{3A}

2. For the purposes of readability, a reference in this Ruling to ‘non-arm’s length expenditure’, ~~as described in paragraphs 10 to 13 of this Ruling~~, includes where no loss, outgoing or expenditure is incurred under the relevant scheme.

3. All legislative references in this Ruling are to the ITAA 1997, unless otherwise indicated.

Date of effect

4. It is proposed that this Ruling, when finalised, will remain effective from 1 July 2018

4A. When changes are made to this Ruling by the subsequent addendum that issues, these will be incorporated into a consolidated version of the Ruling. The addendum will provide details of how that addendum amends the Ruling, including the date of effect of the amendments.

Overview of **2024** amendments to the non-arm’s length income provisions

5. The taxable income of a complying superannuation fund is made up of 2 components – a ‘low tax component’, which is taxed at 15%, and a ‘non-arm’s length component’ (NALC), which is taxed at the top marginal tax rate.

6. ~~The 2024 amendments have modified the calculation of the NALC for an income year for small complying superannuation funds. The non-arm’s length component for an income year is the amount of a complying superannuation fund’s non-arm’s length income (NALI) less any deductions to the extent that they are attributable to that income. To the extent that the ordinary and statutory income of a complying superannuation fund is NALI, the income is not exempt current pension income.~~

Non-arm’s length component

6A. For a superannuation fund, other than a small complying superannuation fund, the NALC for an income year is the amount of that entity’s non-arm’s length income (NALI) less any deductions to the extent that they are attributable to that income.^{5A}

6B. For a small complying superannuation fund, the NALC for an income year is the lesser of (‘lesser of’ calculation) the:

- sum of
 - each amount of NALI (other than NALI as a result of a general expense that is a non-arm’s length expense) less deductions attributable to that NALI, and

^{3A} See paragraphs (1) to (3) of item 5 in Schedule 7 to the TLA Act 2024.

⁴ [Omitted.] Subsection 295-545(2).

⁵ [Omitted.] Paragraphs 295-385(2)(a), 295-390(2)(a) and 295-400(2)(a).

^{5A} Subsection 295-545(2).

LCR 2021/2DC

Status: **draft only – for comment**

– each amount of NALI as a result of a general expense that is a non-arm's length expense^{5B}

- fund's taxable income for the year less assessable contributions plus any deductions to the extent they are attributable to those contributions.^{5C}

6C. The formula outlined in paragraph 6B of this Ruling introduces a cap on the NALC to ensure that assessable contributions (minus related deductions) are not subject to the higher tax rates under the NALI provisions.^{5D}

6D. The amount of NALI as a result of a general expense that is a non-arm's length expense is calculated using the 'twice the difference' approach.^{5E}

Other changes made by the 2024 amendments – for complying superannuation funds

7. For all complying superannuation funds, the low tax component of a complying superannuation fund's taxable income is the amount of the fund's taxable income less its NALC.^{6A} To the extent that the ordinary and statutory income of any complying superannuation fund is NALI, the income is not exempt current pension income.^{6B} ~~The low tax component of a complying superannuation fund's taxable income is the amount of the fund's taxable income remaining after deducting the non-arm's length component from its total taxable income.~~

8. Following the 2024 amendments the NALI provisions continue to apply where a complying superannuation fund~~Prior to the amendments, the NALI provisions apply where a complying superannuation fund:~~

- derived ordinary or statutory income under a scheme where
 - the parties were not dealing with each other at arm's length in relation to the scheme, and
 - the amount of income is more than what might have been expected to have been derived if those parties had been dealing with each other at arm's length in relation to the scheme^{7, or}
- derived ordinary or statutory income if it is
 - a dividend paid to the fund by a private company, or
 - ordinary income or statutory income that is reasonably attributable to such a dividend unless the amount is consistent with an arm's length dealing^{7A}
- derived income as a beneficiary of a trust, other than because of holding a fixed entitlement to the income of the trust^{7B}

^{5B} Paragraph 295-545(2A)(a).

^{5C} Paragraph 295-545(2A)(b).

^{5D} Paragraph 7.24 of the Explanatory Memorandum to the Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Bill 2024 (EM to the TLA Bill 2024).

^{5E} Subsection 295-550(8) or (9).

⁶ [Omitted.] Subsection 295-545(3).

^{6A} Subsection 295-545(3).

^{6B} Paragraphs 295-385(2)(a), 295-390(2)(a) and 295-400(2)(a).

⁷ Paragraph 295-550(1)(a) Subsection 295-550(1), as it previously read.

^{7A} Subsection 295-550(2).

^{7B} Subsection 295-550(4).

LCR 2021/2DC

Status: **draft only – for comment**

- derived income as a beneficiary of a trust through holding a fixed entitlement to the income of the trust where the
 - fund acquired the entitlement under a scheme, or the income was derived under a scheme, the parties to which were not dealing with each other at arm's length, and
 - amount of income is more than what might have been expected to have been derived if those parties had been dealing with each other at arm's length.⁸

8A. From 1 July 2018, the non-arm's length expenditure provisions will apply to small complying superannuation funds. As explained later in this Ruling, these provisions will apply where the small complying superannuation fund incurs a non-arm's length expense that:

- relates to a specific expense in respect of a particular asset or assets of the fund
- is of a general nature that does not relate to a specific expense of the fund.

8B. The non-arm's length expenditure provisions do not apply to expenditure incurred or expected to have been incurred before 1 July 2018.^{8A}

8C. Superannuation funds other than a small complying superannuation fund, including large APRA regulated funds, exempt public sector superannuation funds, pooled superannuation trusts and approved deposit funds, (large APRA funds), are exempt from the NALI rules arising from non-arm's length expenditure for both general and specific expenses. These large APRA funds are still subject to the other NALI rules.^{8B}

9. The 2024 amendments remove ambiguity in the application of the NALI provisions by clarifying their application where a complying superannuation fund incurs a loss, outgoing or expenditure (or does not incur a loss, outgoing or expenditure) in certain circumstances (as outlined in paragraphs 10 to 13 of this Ruling). While retaining these rules, the amendments remove ambiguity in the application of the NALI provisions by clarifying their application where a complying superannuation fund incurs a loss, outgoing or expenditure (or does not incur a loss, outgoing or expenditure) in certain circumstances (as outlined in paragraphs 10 to 13 of this Ruling).

Non-arm's length expenditure – requirements of paragraphs 295-550(1)(b) and (c), paragraphs 295-550(5)(b) and (c), and subsections 295-550(8) and (9)

9A. The amount of ordinary or statutory income of a small complying superannuation fund that is NALI will depend on whether the non-arm's length expenditure is a specific expense or a general expense.

⁸ Paragraph 295-550(5)(a) Subsection 295-550(5), as it previously read.

^{8A} Schedule 7, Item 5, paragraphs (1) to (3) of the TLA Act 2024.

^{8B} Paragraphs 295-550(1)(a), sections (2), (3) and (4) and paragraph 295-550(5)(a).

⁹ [Omitted.] Paragraphs 295-550(1)(a) and (5)(a).

LCR 2021/2DC

Status: **draft only – for comment**

Specific non-arm's length expense – paragraphs 295-550(1)(b) and 295-550(1)(c)

10. An amount of ordinary or statutory income will be NALI of a small complying superannuation fund where:

- there is a scheme in which the parties were not dealing with each other at arm's length, and
- in gaining or producing the income of the fund in relation to any particular asset or assets of the fund, the fund incurs a loss, outgoing or expenditure of an amount, and the fund incurs a loss, outgoing or expenditure of an amount in gaining or producing the income, and
- the amount of the loss, outgoing or expenditure is less than the amount that the fund might have been expected to incur had those parties been dealing with each other at arm's length in relation to the scheme.¹⁰

11. An amount of ordinary or statutory income will also be NALI of a small complying superannuation fund if, in gaining or producing income in relation to any particular asset or assets of the fund, Further to paragraph 10 of this Ruling, the income is also NALI if the fund does not incur a loss, outgoing or expenditure that the fund might have been expected to incur if those parties had been dealing with each other at arm's length in relation to the scheme.¹¹

General non-arm's length expense – subsections 295-550(8) and 295-550(9)

11A. An amount of ordinary or statutory income will be NALI of a small complying superannuation fund where:

- there is a scheme in which the parties were not dealing with each other at arm's length
- in gaining or producing the income of the fund (but not in gaining or producing the income in relation to any particular asset or assets of the fund) the fund incurs a loss, outgoing or expenditure of an amount, and
- the amount of the loss, outgoing or expenditure is less than the amount that the fund might have been expected to incur had those parties been dealing with each other at arm's length in relation to the scheme.^{11A}

11B. An amount of ordinary or statutory income will also be NALI of a small complying superannuation fund if, in gaining or producing the income (but not in gaining or producing the income in relation to any particular asset or assets of the fund) the fund does not incur a loss, outgoing or expenditure that the fund might have been expected to incur if those parties had been dealing with each other at arm's length in relation to the scheme.^{11B}

11C. As a result of the 2024 amendments, NALI that results from a non-arm's length general expense will be calculated according to the 'twice the difference' approach. Where a non-arm's length general expense is incurred, the amount that is NALI is equal to twice the difference of the amount that the entity actually incurred and the amount that the entity might have expected to incur if the parties had been dealing at arm's length. Where no expense was incurred, the amount will be equal to twice the amount that might have been expected if the parties has been dealing at arm's length.

¹⁰ Paragraph 295-550(1)(b).

¹¹ Paragraph 295-550(1)(c).

^{11A} Subsection 295-550(8).

^{11B} Subsection 295-550(9).

LCR 2021/2DC

Status: **draft only – for comment**

11D. Where a non-arm's length general expense is actually incurred, when calculating the NALC, the amount of NALI using the 'twice the difference' approach is not reduced by the amount actually incurred.^{11C}

Non-arm's length expenditure – requirements of paragraphs 295-550(5)(b) and (c)

12. Other income derived by a small complying superannuation fund as a beneficiary of a trust through holding a fixed entitlement to the income of the trust is NALI of the fund where:

- there is a scheme in which the parties were not dealing with each other at arm's length
- the fund incurs a loss, outgoing or expenditure of an amount in acquiring the entitlement or in gaining or producing the income, and
- the amount of the loss, outgoing or expenditure is less than the amount that the fund might have been expected to incur if those parties had been dealing with each other at arm's length in relation to the scheme.¹²

13. Other income derived by a small complying superannuation fund as a beneficiary of a trust through holding a fixed entitlement the income of the trust is also NALI if the fund does not incur a loss, outgoing or expenditure in acquiring the entitlement or in gaining or producing the income that the fund might have been expected to incur if those parties had been dealing with each other at arm's length in relation to the scheme.¹³ ~~Further to paragraph 12 of this Ruling, the income is also NALI if the fund does not incur a loss, outgoing or expenditure that the fund might have been expected to incur if those parties had been dealing with each other at arm's length in relation to the scheme.~~

13A. A non-arm's length expense incurred in relation to the acquiring the fixed entitlement to the income of a trust or in gaining or producing the income as a beneficiary of such a trust is a specific expense and not a general expense.

Application of non-arm's length expenditure provisions

14. In applying paragraphs 295-550(1)(b) and (c), 295-550(5)(b) and (c), or 295-550(8)(b) and (9)(b) (non-arm's length expenditure provisions), it is necessary to identify the relevant scheme under which the parties to the scheme were not dealing with each other at arm's length. A 'scheme' is defined as '... any arrangement; or ... any scheme, plan, proposal, action, course of action or course of conduct, whether unilateral or otherwise'.¹⁴

15. It is therefore necessary to identify both the steps of the relevant scheme and the parties that deal with each other under those steps of the scheme.

16. Within the identified steps of the scheme, it is then necessary to determine whether the small complying superannuation fund incurs non-arm's length expenditure in: gaining or producing the ordinary or statutory income, or acquiring the fixed entitlement to the income of a trust.

^{11C} Subparagraph 295-545(2A)(a)(ii).

¹² Paragraph 295-550(5)(b).

¹³ Paragraph 295-550(5)(c).

¹⁴ Subsection 995-1(1).

LCR 2021/2DC

 Status: **draft only – for comment**

- gaining or producing the ordinary or statutory income^{14A} and whether it is *in relation* to any particular asset or assets of the fund or not^{14B}, or
- in acquiring the fixed entitlement to the income of a trust or in gaining or producing the income derived as beneficiary of a trust.^{14C}

17. In identifying whether the **small** complying superannuation fund has incurred NALI, there must be a sufficient nexus between the non-arm's length expenditure and the relevant ordinary or statutory income. That is, the expenditure must have been incurred 'in' gaining or producing the relevant income (or acquiring the relevant entitlement). Further, to determine whether the income is *in relation* to any particular asset or assets of the fund or not, there must also be a sufficient nexus between the non-arm's length expenditure and ordinary or statutory income derived in respect of that asset or assets including the disposal of that asset.

17A. While guidance can be obtained from jurisprudence concerning the application of section 8-1 to determine whether there is a sufficient nexus between the non-arm's length expenditure and the relevant income¹⁵, the non-arm's length expenditure does not have to be deductible under section 8-1 for the non-arm's length expenditure provisions to apply. The non-arm's length expenditure may be of a revenue or capital nature¹⁶, or deductible under a specific provision, provided there is a sufficient nexus to the relevant income.

18. Non-arm's length expenditure incurred to acquire an asset (including associated financing costs) will be specific expenditure and will have a sufficient nexus to all ordinary or statutory income derived by the **small** complying superannuation fund in respect of that **particular** asset. This includes any capital gain derived on the disposal of the asset (see Example 1 of this Ruling).¹⁷ There will still be a sufficient nexus between the initial non-arm's length expenditure incurred to acquire an asset (including associated financing costs) and an amount of statutory income, determined by reference to any capital gain derived by the fund on the disposal of that particular asset^{17A} ~~for the capital gain to be NALI~~ even where the trustee subsequently refinances the borrowing arrangement on arm's length terms (see Example 4 of this Ruling).

19. In some instances, the non-arm's length expenditure will have a sufficient nexus to all of the ordinary income, statutory income, or both, derived by the fund rather than to any particular asset or assets of the fund. A general expense is a loss, outgoing or expenditure of an amount that is incurred (including nil expenditure) in gaining or producing income of the fund but not in relation to any particular asset or assets of the fund. For example, a fund may incur expenditure that does not specifically relate to a particular asset or assets owned or acquired amount being derived by the fund but still has a sufficient nexus more

^{14A} Paragraphs 295-550(8) and (9).

^{14B} Subparagraph 295-550(8)(b)(i) and paragraph 295-550(9)(b).

^{14C} Paragraphs 295-550(5)(b) and (c).

¹⁵ See Taxation Ruling TR 93/17 *Income tax: income tax deductions available to superannuation funds*—See paragraph 2.38 of the Explanatory Memorandum to the Treasury Laws Amendment (2018 Superannuation Measures No. 1) Bill 2019 (the EM). See also.

¹⁶ Subsection 295-550(7).

¹⁷ Paragraphs 7.1, 7.2 and 7.40 of the EM to the TLA Bill 2024 refer back to the Treasury Laws Amendment (2018 Superannuation Measures No. 1) Bill 2019 (TLA Bill 2019). As such, see Example 2.1 and paragraph 2.39 of the Explanatory Memorandum to the TLA Bill 2019 (EM to the TLA Bill 2019). See also Example 2.1 and paragraph 2.39 of the EM.

^{17A} See Taxation Determination TD 2024/5 *Income tax: how the non-arm's length income and capital gains tax provisions interact to determine the amount of statutory income that is non-arm's length income.*

LCR 2021/2DC

Status: **draft only – for comment**

generally to [thea#](#) income derived by the fund to be deductible under section 8-1, such as¹⁸:

- actuarial costs – except those incurred in complying with, or managing, the fund’s income tax affairs and obligations (for example, Subdivision 295-F) which are ordinarily deductible under section 25-5
- accountancy fees – except those incurred in complying with, or managing, the fund’s income tax affairs and obligations (for example, Subdivision 295-F) which are ordinarily deductible under section 25-5
- audit fees
- costs of complying with a ‘regulatory provision’ as defined in section 38A of the *Superannuation Industry (Supervision) Act 1993* (SISA) (unless the cost is a capital expense)
- trustee fees and premiums under an indemnity insurance policy
- costs in connection with the calculation and payment of benefits to members (but not the cost of the benefit itself); for example, interest on money borrowed to secure temporary finance for payment of benefits and medical costs in assessing invalidity benefit claims
- investment adviser fees and costs in providing pre-retirement services to members, and
- other administrative costs incurred in managing the fund.

20. [Where the fund incurs non-arm’s length general expenditure of the nature outlined in paragraph 19 of this Ruling, the amount of income that is NALI is calculated using the ‘twice the difference’ approach as follows \(see Example 2 of this Ruling\)](#)~~Where the fund incurs non-arm’s length expenditure of the nature outlined in paragraph 19 of this Ruling, the nexus between the expenditure and all the income derived by the fund is sufficient for all the income to be NALI under paragraphs 295-550(1)(b) and (c) (see Example 2 of this Ruling):~~

- [where an amount of non-arm’s length general expense is incurred – the amount that might have been expected to be incurred if the parties had been dealing at arm’s length, minus the amount actually incurred, with the resulting number multiplied by 2^{18A}, or](#)
- [where no amount of non-arm’s length general expense is incurred – twice the amount that might have been expected to be incurred if the parties had been dealing at arm’s length.^{18B}](#)

20A. [Where a non-arm’s length general expense is actually incurred, when calculating the NALC, the amount of NALI using the ‘twice the difference’ approach is not reduced by the amount actually incurred.^{18C} This is because the ‘twice the difference’ approach already takes into account the amount actually incurred by subtracting it from the amount that might have been expected to be incurred if the parties had been at arm’s length, before multiplying the result by 2 to arrive at the amount of NALI.^{18D}](#)

¹⁸ See paragraph 4 of TR 93/17. See also *Commissioner of Taxation (Cth) v Green* [1950] HCA 20.

^{18A} [Subsection 295-550\(8\).](#)

^{18B} [Subsection 295-550\(9\).](#)

^{18C} [Subparagraph 295-545\(2A\)\(a\)\(ii\).](#)

^{18D} [Paragraph 7.23 of the EM to the TLA Bill 2024.](#)

Status: **draft only – for comment**

21. Where a [small](#) complying superannuation fund incurs non-arm's length expenditure ~~of a recurrent nature~~ (that does not relate to the acquisition of ~~any particular~~ asset¹⁹) under a scheme that only has a nexus with the fund deriving ordinary or statutory income during a particular income year, and subsequently ceases to incur that non-arm's length expenditure in a later income year, income derived by the fund in that later income year is not NALI (see Example 2 of this Ruling). Interest expenses incurred under a limited recourse borrowing arrangement (LRBA) is an example of ~~recurrent~~ expenditure that is incurred in relation to an acquisition of an asset.

Example 1 – non-arm's length expenditure was incurred to acquire an asset – NALI

22. During the ~~2022-23~~~~2019-20~~ income year, Armin holds commercial property with a market value of \$800,000. During the income year, he sells the commercial property to himself acting as trustee of his SMSF for \$200,000. The SMSF leases the property to a third party.

23. For the purposes of subsection 295-550(1), the scheme involves the SMSF acquiring the commercial property from Armin for an amount that is less than its market value. There is a sufficient nexus between the non-arm's length expenditure incurred in acquiring that property and the rental income the SMSF derives from leasing the property for the rental income to be NALI. ~~Further, there will be a sufficient nexus between the non-arm's length expenditure and an amount of statutory income, determined by reference to any capital gain derived by the fund on the disposal of that particular property. The non-arm's length expenditure incurred by the SMSF in acquiring the property is a specific expense. The SMSF's NALC is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling. Further, there will be a sufficient nexus between the non-arm's length expenditure and any capital gain derived on the disposal of the property for the capital gain to be NALI.~~

Example 2 – non-arm's length expenditure incurred has a nexus to all income of the fund – NALI

24. For the 2020–21 income year, Mikasa as trustee of her SMSF engages an accounting firm, where she is a partner, to provide accounting services for the SMSF. The accounting services include services other than those relating to complying with, or managing, the SMSF's income tax affairs and obligations. The accounting firm does not charge the SMSF for those services as a result of non-arm's length dealings between the parties (and not as part of any discount policy referred to in paragraph 51 of this Ruling).

25. For the purposes of subsection 295-550(1), the scheme involves the SMSF acquiring the accounting services under a non-arm's length arrangement. The non-arm's length expenditure (being the nil amount incurred for the services) has a sufficient nexus with all of the ordinary and statutory income derived by the SMSF for the 2020–21 income year. ~~The non-arm's length expenditure incurred by the SMSF in acquiring the accounting services (nil amount) is a general expense. As such, for the 2020–21 income year, the amount of NALI as a result of the general expense will be twice the difference between the amount of the expense that might have been expected to be incurred had the parties been dealing at arm's length and the amount the entity incurred. The SMSF's NALC is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling. As such, all of the SMSF's income for the 2020–21 income year is NALI.~~

¹⁹ See paragraph 18 of this Ruling concerning non-arm's length expenditure incurred to acquire an asset.

LCR 2021/2DC

Status: **draft only – for comment**

26. *Subsection 295-550(1) would cease to apply if the arrangement changes for the 2021–22 income year so that the SMSF incurs expenditure for the accounting services provided by the accounting firm of an amount that would have been expected to be incurred where the parties were acting at arm's length. In this situation, none of the SMSF's income for the 2021–22 income year is NALI.*

Purchase of an asset under a non-arm's length arrangement

27. Where a [small](#) complying superannuation fund purchases an asset at less than market value under a scheme where the parties were not dealing at arm's length, the fund incurs non-arm's length expenditure for the purposes of applying the non-arm's length expenditure provisions. In applying those provisions, it does not matter whether the amount of the loss, outgoing or expenditure is revenue or capital in nature.²⁰

28. In situations where the terms of a contract between the [small](#) complying superannuation fund and the seller of the asset make it clear that the asset is being purchased by the fund, the difference between the consideration paid (if any) by the fund and the market value of the asset purchased under the contract cannot represent the value of an in specie contribution made by the other party. This is because there is no other asset being transferred to the superannuation fund that can be regarded as being an in specie contribution. The difference between the consideration (if any) paid by the fund and the market value is not an asset being transferred to the superannuation fund.

29. An in specie contribution can be made in conjunction with a complying superannuation fund purchasing part of an asset where a contract makes it clear the fund is only acquiring part of the asset. In such situations, the fund:

- purchases the interest in the asset specified under the contract, and
- receives the in specie contribution of the remaining interest in the asset.

[29A.](#) The [small](#) complying superannuation fund will not have incurred non-arm's length expenditure for the purposes of subsections 295-550(1) or (5) where that part of the asset acquired under the contract is purchased at market value. However, if the fund pays less than market value for the part of the asset purchased under the contract, then the non-arm's length expenditure provisions apply for the reasons outlined in paragraph 27 of this Ruling. This would be the case even if the in specie contribution relating to the other part of the asset is recorded at market value in the fund's accounts and is allocated to the member's superannuation interest.

30. [The non-arm's length expenditure incurred by the fund in acquiring the property is a specific expense.](#) A consequence of the non-arm's length expenditure provisions applying to the purchase of either all, or a part, of the asset is that all of the income derived from that asset will be NALI, including any capital gains from the disposal of the asset.

Example 3 – purchase less than market value and no in specie contribution – NALI

31. *During the 2018–19 income year, Russell (as trustee of his SMSF) purchases listed shares from a related entity for \$500,000. The market value of the shares at the time of purchase is \$900,000. The terms of the agreement specify the purchase price as*

²⁰ Subsection 295-550(7).

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\$500,000, rather than \$900,000. Accordingly, the arrangement does not involve an in specie contribution being made to the SMSF.

32. The non-arm's length dealing between Russell's SMSF and his related entity amounts to a scheme, which has resulted in his SMSF incurring capital expenditure that was less than would otherwise be expected if those parties were dealing with each other at arm's length in relation to the scheme. The capital expenditure was incurred in gaining or producing the dividend income. The non-arm's length expenditure incurred by the SMSF in purchasing the listed shares is a specific expense. Any dividend income derived by the SMSF from the shares will be NALI. The SMSF's NALC is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling.

33. The non-arm's length expenditure incurred in acquiring the shares also results in an amount of statutory income, determined by reference to any capital gain being derived by the fund on the disposal of those particular shares (such as a disposal of the shares) being NALI. Refer to Example 13 of this Ruling for an explanation of how this operates in conjunction with the market value substitution rule. ~~The non-arm's length expenditure incurred in acquiring the shares will also result in any capital gain that might arise from a subsequent CGT event happening in relation to the shares (such as a disposal of the shares) being NALI. Refer to Example 13 of this Ruling for an explanation of how this operates in conjunction with the market value substitution rule.~~

Example 4 – purchase financed through a limited recourse borrowing arrangement on non-arm's length terms – NALI

34. During the 2018–19 income year, Kellie (as trustee of her SMSF) enters into a non-commercial LRBA with herself in her individual capacity to purchase a commercial property valued at \$2 million. Her SMSF borrows 100% of the purchase price and the terms of the loan include interest being charged at a rate of 1.5% per annum and repayments only being made on an annual basis over a 25-year period. Kellie's SMSF receives a commercial rate of rent from the property of \$12,000 per month.

35. If Kellie's SMSF had entered into an LRBA on arm's length terms, it would be expected that repayments of principal and interest would occur on a monthly basis and interest would be charged on the LRBA at a commercial rate. The loan-to-market value ratio would have also not exceeded commercial levels.

36. For the purposes of subsection 295-550(1), the scheme involves the SMSF entering into the LRBA with Kellie, complying with the terms of the LRBA, purchasing the commercial property, and deriving the rental income. The terms of the LRBA constitute a non-arm's length dealing between the SMSF and Kellie, which resulted in the SMSF incurring expenditure in gaining or producing rental income that was less than would otherwise be expected if those parties were dealing with each other at arm's length in relation to the scheme. The non-arm's length expenditure incurred by the SMSF in purchasing the commercial property is a specific expense. The rental income derived from the commercial property by the SMSF for all income years is therefore NALI, regardless of whether the LRBA is subsequently refinanced on arm's length terms. The SMSF's NALC is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling.

37. The non-arm's length expenditure incurred under the LRBA will also result in an amount of statutory income, determined by reference to any capital gain derived by the fund on the disposal of that particular property (such as disposal of the property) being NALI. This will be the case regardless of whether the LRBA is subsequently refinanced on

LCR 2021/2DC

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~~[arm's length terms.](#)^{20A}*The non-arm's length expenditure incurred under the LRBA will also result in any capital gain that might arise from a subsequent CGT event happening in relation to the property (such as disposal of the property) being NALI. This will be the case regardless of whether the LRBA is subsequently refinanced on arm's length terms.*~~

Example 5 – part purchase and part in specie contribution at market value – not NALI

38. During the ~~2023-24~~~~2018-19~~ income year, Nadia owns commercial premises that she leases to a third party which use the premises to carry on a business. The commercial premises have a market value of \$500,000. Nadia would like to transfer it to her SMSF, but her SMSF only has \$400,000 in cash. Nadia's SMSF purchases 50% of the commercial premises under a contract from Nadia for \$250,000. Nadia makes an in specie non-concessional contribution of the remaining 50% interest in the commercial premises (valued at \$250,000). The acceptance of the in specie contribution by Nadia as trustee of the SMSF is recorded by her in writing and the market value of the in specie contribution is reported in the SMSF's accounts. The SMSF reports the non-concessional contribution to the ATO.

39. Nadia's SMSF continues to lease the commercial premises to the third party at a commercial rate of rent. As the commercial premises were acquired by the SMSF at market value and a commercial rate of rent was charged, the rental income derived by the SMSF is not considered to be NALI. Any capital gain that might arise from the disposal of the factory will also not be NALI.

Capacity in which activities are performed – self-managed superannuation funds

40. In the context of SMSFs, it may be necessary for an individual to ascertain whether they are performing an activity as a trustee of the superannuation fund or whether they are acting in a different capacity. An SMSF is a superannuation fund that satisfies the conditions set out in sections 17A and 17B of the SISA.²¹ The statutory scheme requires a member of a SMSF to be either a trustee of the fund or a director of a body corporate that is a trustee of the fund.²² The SISA also prevents a trustee, or a director of a body corporate that is a trustee, of an SMSF from receiving remuneration for any duties or services performed by the trustee or director in relation to the SMSF.²³

41. However, subsections 17B(1) and (2) of the SISA provides exceptions to paragraphs 17A(1)(f) and (g) and paragraphs 17A(2)(c) and (d) of the SISA, such that a trustee or director of a corporate trustee can receive remuneration for duties or services performed by them if they:

- perform the duties or services other than in their capacity as trustee or director of a body corporate that is a trustee
- are appropriately qualified, and hold all necessary licences, to perform the duties or services

^{20A} [This is subject to paragraph 17A of Practical Compliance Guideline PCG 2016/5 Income tax – arm's length terms for Limited Recourse Borrowing Arrangements established by self-managed superannuation funds.](#)

²¹ See section 10 of the SISA.

²² See paragraphs 17A(1)(b) to (d), and 17A(2)(a) and (b) of the SISA.

²³ See paragraphs 17A(1)(f) and (g), and 17A(2)(c) and (d) of the SISA.

LCR 2021/2DC

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- perform the duties or services in the ordinary course of a business, carried on by them, of performing similar duties or services for the public, and
- receive remuneration that is no more favourable to them than that which it is reasonable to expect would apply if they were dealing with the relevant other party at arm's length in the same circumstances.

42. Given the statutory restrictions that prevent a trustee or director of a corporate trustee from receiving remuneration, paragraphs 295-550(1)(b) and (c) [or subsections 295-550\(8\) and \(9\)](#) will not be enlivened due to the trustee or director not charging for the services performed in relation to the fund when acting in a trustee capacity.²⁴ For example, the non-arm's length expenditure provision will not apply where a trustee, acting in that capacity, performs bookkeeping or accounting services for the fund for no remuneration.

43. However, when the trustee or director of a corporate trustee operates in another capacity and either does not receive remuneration for those services or receives remuneration in accordance with the exceptions in section 17B of the SISA, paragraphs 295-550(1)(b) or (c) [or subsections 295-550\(8\) or \(9\)](#) may apply where the fund incurs non-arm's length expenditure.

44. A trustee or director of a corporate trustee of a SMSF will be required to perform particular actions in order to satisfy obligations imposed on them, including:

- any conditions imposed by statute (for example, the SISA and the *Corporations Act 2001*)
- any fiduciary conditions imposed under the law, and
- any duties or obligations imposed under the trust deed of the SMSF.

45. The trust deed of the SMSF may also provide the trustee or director of the corporate trustee the power to perform certain actions.

46. An individual's business, profession, life experiences or employment may result in the individual having skills and knowledge that can assist the individual perform their duties in their capacity as trustee, or as a director of a corporate trustee, of a SMSF. Utilising such skills and knowledge of itself does not indicate that the individual is not acting in their capacity as trustee or as a director of a corporate trustee. For example, a financial adviser who is a trustee of a SMSF can utilise their skills and knowledge in deciding the investment strategy of the SMSF in their capacity as trustee.

47. In the context of applying paragraphs 295-550(1)(b) and (c) [or subsection 295-550\(8\) or \(9\)](#), it is appropriate to presume that an individual is acting in their capacity as a trustee, or director of a corporate trustee, where the actions are consistent with a duty, obligation or power referred to in paragraph 44 of this Ruling, unless there are factors that suggest a contrary conclusion. [Factors to be considered when determining whether an individual is performing their activities in their individual capacity and not in their capacity as a trustee, or a director of a corporate trustee, include:](#) ~~Factors that indicate that the individual is performing their activities in their individual capacity and not in their capacity as a trustee, or a director of a corporate trustee, include:~~

- The individual charges the complying SMSF for performing the services. However, there can be circumstances where the individual can be acting in their individual capacity even though they do not charge the SMSF for performing the services.

²⁴ [See paragraphs 7.28 to 7.32 of the EM to the TLA Bill 2024. See paragraphs 2.31 to 2.35 of the EM.](#)

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- The individual uses the equipment and other assets of their business, or equipment and other assets used in their profession or employment in a material manner. However, minor, infrequent or irregular use of equipment or assets will not, of itself, indicate the individual is acting in their individual capacity. For example, in the absence of any other factor indicating otherwise, minor, infrequent or irregular use of a business computer at the office by an individual would not, of itself, indicate the individual is acting in their individual capacity.
- The individual performs the activities pursuant to a licence or qualification relating to their business, or their profession or employment. That is, the activity can only be performed due to the individual or business holding the relevant licence or qualification.
- The activity is covered by an insurance policy relating to their business, or their profession or employment (for example, indemnity insurance).

48. It is necessary to carefully weigh up all the relevant facts, circumstances and factors in deciding whether the individual is acting in a capacity other than as trustee, or as a director of a corporate trustee, of an SMSF.

Whether dealings are on a non-arm's length basis

49. Where a trustee, or a director of a corporate trustee, of a [small](#) complying superannuation fund performs services other than in these capacities (for example, in their individual capacity) to a [small](#) complying superannuation fund for remuneration, the non-arm's length expenditure provisions will apply where the remuneration is incurred by the fund in gaining or producing ordinary or statutory income and the remuneration is non-arm's length expenditure. The non-arm's length expenditure provisions will also apply in these situations where no remuneration is provided. For example, the non-arm's length expenditure provisions will apply where a trustee (being an accountant by profession) contracts the bookkeeping or accounting services to their accounting firm, which charges non-arm's length rates.

50. If arm's length charges are paid, the non-arm's length expenditure provisions will not apply. We would expect the trustee (or a director of a corporate trustee) of a [small](#) complying superannuation fund and the service provider to have a sound basis, such as the application of commercial pricing policies, for arriving at the amount to be charged.

51. A [small](#) complying superannuation fund might enter into arrangements that result in it receiving discounted prices. Such arrangements will still be on arm's length terms where they are consistent with normal commercial practices, such as an individual acting in their capacity as trustee (or a director of a corporate trustee) being entitled to a discount under a discount policy where the same discounts are provided to all employees, partners, shareholders or office holders. [Further, the trustee \(or director of a corporate trustee\) of the fund should also not be able to influence the discount policy.](#)

52. Further, services provided to a [small](#) complying superannuation fund on a pro bono basis will also still be on arm's length terms where the trustee (or director of a corporate trustee) of the fund is not able to influence the service provider's decision to supply the services on a pro bono basis.

53. [Pricing based on a cost-recovery basis, other than an arrangement covered in paragraph 51 of this Ruling, will not be consistent with an arm's length dealing. Similarly, although pricing based on a cost-recovery basis will not generally be consistent with an arm's length dealing, there may be limited circumstances where a party operating on a](#)

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~~simple cost recovery basis for particular services is commercially justifiable because of the economies of scale it achieves within its business by providing other services. For example, this may occur with respect to services provided to a large Australian Prudential Regulation Authority (APRA) fund either by the trustee acting in a separate capacity or by a related third party. In this context, a trustee of a large APRA fund that charges the fund on a cost recovery basis will not result in the non-arm's length expenditure provisions applying.~~

Example 6 – internal arrangement within an SMSF – trustee provides services to the SMSF

54. *Leonie is a trustee of an SMSF of which she is the sole member. She is a chartered accountant and registered tax agent who is employed in an accounting and tax agent business. Leonie (in her capacity as trustee) prepares the accounts and annual return for the SMSF. She does not use the equipment or assets of her employer, nor does she lodge the annual return using her tax agent registration. As she performs these duties or services as trustee of the SMSF, she does not charge the SMSF for this work.²⁶ The non-arm's length expenditure provisions do not apply as the duties or services performed by Leonie are in her capacity as trustee rather than under an arrangement in which parties are dealing with one another on a non-arm's length basis.*

Example 7 – SMSF trustee carrying out duties – trustee capacity

55. *Levi is the trustee of his SMSF of which he is the sole member. He is also a financial adviser and director of Levi and Co Financial Services Pty Ltd. Levi operates the business of Levi and Co Financial Services Pty Ltd from a commercial office and on regular occasions from his home. At home, Levi uses the computer and office equipment supplied by and paid for by the business.*

56. *When at home, but not while working or billing clients, Levi undertakes the bookwork and occasionally makes online investments for his SMSF using the computer and office equipment supplied by the business.*

57. *Levi performs these activities as trustee of his SMSF and does not charge the SMSF for this work. Levi's use of the computer and office equipment at home is minor and incidental in nature and will not, of itself, indicate that he is undertaking these services in any capacity other than as trustee for his SMSF.*

Example 8 – third party providing services – discounts

58. *Sasha is the trustee of her SMSF of which she is the sole member. She is also an employee of Eren & Co Accountants.*

59. *Sasha engages Eren & Co Accountants to provide accounting services to her SMSF. Sasha is entitled to a staff discount rate that is available to all staff of Eren & Co Accountants. Sasha is charged the discounted rate for these services.*

60. *As the discount is available to all staff of Eren & Co Accountants and is not able to be influenced by Sasha, the discounted rate has been provided on an arm's length basis. Accordingly, the non-arm's length expenditure provisions will not apply.*

²⁵ [\[Omitted.\] See paragraph 2.50 of the EM.](#)

²⁶ In accordance with paragraph 17A(1)(f) of the SISA.

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Example 9 – SMSF trustee carrying out duties – different capacities

61. Trang is the trustee of her SMSF of which she is the sole member. She is also a plumber by trade and runs her own business as a sole trader in which she also employs an apprentice, Novee.

62. Trang's SMSF has 2 investment properties which are leased for a commercial rate of rent.

63. After finishing work for the day, Trang stops by one of the SMSF's investment properties to connect a stand-alone water filter provided (and to be taken away at lease end) by the tenant. She uses some of her tools of trade to complete the installation.

64. Trang performs this activity as trustee of her SMSF and does not charge the SMSF for this work. Trang's use of the tools of her trade in respect of this property is minor, infrequent or irregular in nature and will not, of itself, indicate that she is undertaking these services in any other capacity other than as trustee for her SMSF. Accordingly, the non-arm's length expenditure provisions will not apply.

65. In respect of the second SMSF rental property, Trang undertakes a complete renovation of the bathroom and kitchen. She schedules time in her work calendar to undertake the work and uses the tools of her trade to undertake all plumbing work on the renovations. She also engages Novee in all works.

66. Trang does not charge the SMSF for the work undertaken in respect of the second SMSF rental property.

67. In this instance, Trang's use of the tools of her trade will not be considered minor, infrequent or irregular in nature. Considering all her activities, she will be considered to be undertaking these services in her individual capacity, rather than as trustee for her SMSF.

68. For the purposes of subsection 295-550(1), the scheme involves the SMSF obtaining the services from Trang and deriving the rental income. Trang not charging the SMSF for the services provided constitutes a non-arm's length dealing between the SMSF and Trang, which resulted in the SMSF incurring expenditure (being the nil amount incurred) in gaining or producing rental income that was less than would otherwise be expected if those parties were dealing with each other at arm's length in relation to the scheme. The non-arm's length expenditure incurred by the SMSF in acquiring the plumbing services for the second SMSF rental property is a specific expense. The SMSF's non-arm's length component is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling.

69. As such, there is sufficient nexus between the non-arm's length expenditure and the rental income derived from the second SMSF rental property. The rental income will therefore be NALI. The non-arm's length expenditure will also result in an amount of statutory income, determined by reference to any capital gain derived by the fund on the disposal of the second SMSF rental property, being NALI. ~~The non-arm's length expenditure will also result in any capital gain that might arise from the subsequent disposal of the second SMSF rental property, being NALI.~~

Example 10 – SMSF trustee carrying out duties – individual capacity

70. Jean is the trustee of his SMSF of which he is the sole member. He is also a licensed electrician by trade, operating an electrician business as a sole trader. The SMSF owns a residential property which it leases for a commercial rate of rent.

Status: **draft only – for comment**

71. Jean undertakes electrical work on the rental property done in his capacity as a licensed electrician, with work done covered under his businesses professional indemnity insurance and utilising its equipment and tools of trade. ~~Jean undertakes electrical work on the rental property that can only be done by a licensed electrician.~~ In that instance, the work done by Jean is not as trustee of his SMSF but in his individual capacity. Jean charges the SMSF the commercial rate for the work undertaken on the rental property. Accordingly, the non-arm's length expenditure provisions will not apply.

Example 11 – SMSF trustee carrying out duties – individual capacity

72. Sharon is a director of the corporate trustee of an SMSF of which she is the sole member. She is a licensed real estate agent and is the director of Ringo Real Estate Pty Ltd which conducts a real estate business, including property management services for rental properties. The SMSF holds a residential property which it leases for a commercial rate of rent. Sharon provides property management services to the SMSF as a licensed real estate agent. She utilises the equipment and assets of Ringo Real Estate Pty Ltd (including the business' website) in performing these services. Her actions are covered by the applicable insurance policies in respect of Ringo Real Estate Pty Ltd. Accordingly, Sharon provides property management services in her individual capacity to the SMSF with respect to the residential property. Ringo Real Estate Pty Ltd does not have a discount policy referred to in paragraph 51 of this Ruling. She charges the SMSF 50% of the price for her services that Ringo Real Estate Pty Ltd would otherwise charge a party.

73. For the purposes of subsection 295-550(1), the scheme involves the SMSF obtaining the services from Sharon and deriving the rental income. The price charged to the SMSF constitutes a non-arm's length dealing between the SMSF, Ringo Real Estate Pty Ltd and Sharon, which resulted in the SMSF incurring expenditure in gaining or producing rental income that was less than would otherwise be expected if those parties were dealing with each other at arm's length in relation to the scheme. The non-arm's length expenditure incurred by the SMSF in acquiring the property management services with respect to the residential property is a specific expense. The SMSF's NALC is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling.

74. As such, there is sufficient nexus between the non-arm's length expenditure and the rental income derived from the residential property. The rental income will therefore be NALI for each income year the non-arm's length dealing remains in place.

75. Due to the nature of the non-arm's length expenditure, there will not be a sufficient nexus between the non-arm's length expenditure and an amount of statutory income, determined by reference to any capital gain derived by the fund on the disposal of that particular residential property. ~~Due to the nature of the non-arm's length expenditure, there will not be a sufficient nexus between the non-arm's length expenditure and any future capital gain made by the SMSF on the disposal of the residential property.~~

Expenditure relating to a superannuation entity as a beneficiary of a trust

76. As explained in paragraphs 12 to 13A of this Ruling, the non-arm's length expenditure provisions apply to expenditure incurred (or that might have been expected to have been incurred) by a small complying superannuation fund as a beneficiary of a trust. Examples of expenditure to which paragraphs 295-550(5)(b) and (c) may apply include:

- a small complying superannuation fund incurs non-arm's length expenditure in acquiring the interest in the trust, or

LCR 2021/2DC

Status: **draft only – for comment**

- the fund enters into an LRBA on non-arm's length terms in order to obtain funds to acquire the fixed entitlement.

Example 12 – SMSF incurs non-arm's length expenditure in acquiring a fixed entitlement in a unit trust

77. During the ~~2018-19~~~~2016-17~~ income year, Scott (as trustee of his SMSF) enters into a non-commercial LRBA with himself in his individual capacity to purchase units, valued at \$50,000, in a stock exchange-listed unit trust. The SMSF borrows 100% of the purchase price and the terms of the loan include no interest being charged and repayments of principal not being required until the end of the 25-year term of the loan. The units provide the SMSF with a fixed entitlement to the income of the unit trust. The unit trust distributes \$8,000 to the SMSF at the end of the ~~2020-21~~~~2018-19~~ income year.

78. If Scott's SMSF had entered into an LRBA on arm's length terms, it would be expected that repayments of principal and interest would occur monthly and interest would be charged under the LRBA at a commercial rate. It could have also used its own cash assets to fund part of the purchase to reduce the loan to market value ratio to commercial levels.

79. For the purposes of subsection 295-550(5), the scheme involves the SMSF entering into the LRBA with Scott, complying with the terms of the LRBA, purchasing the units in the unit trust, and deriving income from those units. The terms of the LRBA constitute a non-arm's length dealing between the SMSF and Scott, which result in the SMSF incurring expenditure in gaining or producing income that was less than would otherwise be expected if those parties were dealing with each other at arm's length in relation to the scheme. The non-arm's length expenditure incurred by the SMSF in entering into the non-commercial LRBA to purchase the units in the unit trust is a specific expense. The \$8,000 distribution derived from the units in the unit trust in the ~~2020-21~~~~2018-19~~ income year, and any distribution derived in future years, is therefore NALI. The SMSF's NALC is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling.

80. The non-arm's length expenditure under the LRBA will also result in an amount of statutory income, determined by reference to any capital gain derived by the fund on the disposal of those particular units being NALI. ~~The non-arm's length expenditure under the LRBA will also result in any capital gain that might arise from a subsequent CGT event happening in relation to the units (such as a disposal of the units) being NALI.~~

Application of the market value substitution rules

81. Where a superannuation fund acquires a CGT asset at less than its market value, the market value substitution rules in section 112-20 may apply to modify the cost base or reduced cost base of the asset. The superannuation fund, when determining the cost base of its CGT asset, is treated as having acquired the asset at market value.²⁷ This affects the amount of any capital gain that may arise from a later CGT event, but does not affect the

²⁷ Assuming that none of the exceptions in subsection 112-20(3) apply.

LCR 2021/2DC

Status: **draft only – for comment**

application of the non-arm's length expenditure provisions in determining whether the asset was acquired by the fund at market value.²⁸

82. Any capital gain that the fund makes from a subsequent CGT event happening in relation to the asset (such as a disposal of the CGT asset) will be NALI.

Example 13 – market value substitution rules (CGT consequences for the transferor and the fund)

83. Continuing on from Example 3 of this Ruling, 2 years later Russell's SMSF sells the shares it acquired for \$500,000 for \$1 million.

84. When calculating the capital gain for the SMSF on disposal of the shares, the cost base of the shares will be modified by the market value substitution rule in section 112-20²⁹ as the parties did not deal with each other at arm's length in relation to the acquisition.

85. This means that the cost base for the shares will be their market value at the time of acquisition by Russell's SMSF, which was \$900,000. The SMSF has therefore realised a capital gain of \$100,000 (\$1 million sale proceeds less deemed cost base of \$900,000).

86. The \$100,000 capital gain derived by the SMSF is subject to the NALI provisions. This is because the amount of expenditure incurred by the SMSF in acquiring the asset was less than what the SMSF might have been expected to incur if the parties were dealing with each other at arm's length. [The SMSF's NALC is calculated using the 'lesser of' calculation referred to in paragraph 6B of this Ruling.](#)

87. It should also be noted that the market value substitution rules in paragraph 116-30(2)(b) would have applied in relation to the capital proceeds received by the related entity at the time Russell's SMSF acquired the shares as the parties were not dealing with each other at arm's length. The rules have the effect of replacing the capital proceeds from the disposal with the market value of the shares at the time the disposal took place.

Commissioner of Taxation

27 November 2024

²⁸ Paragraph 7.2 of the EM to the TLA Bill 2024 refers back to the [Treasury Laws Amendment \(2018 Superannuation Measures No. 1\) Act 2019](#). As such, see paragraphs 2.46 to 2.48 of the [Explanatory Memorandum to the TLA Bill 2019 \(EM to the TLA Bill 2019\)](#). See paragraphs 2.46 to 2.48 of the EM.

²⁹ Assuming that none of the exceptions in subsection 112-20(3) apply.

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Appendix 1 – Compliance approach

On finalising this draft Ruling, we intend to remove the previous compliance approach set out in this Appendix 1 – Compliance approach. This is because the 2024 amendments have:

- excluded large APRA funds from the operation of the non-arm's length expenditure rules, and
- limited the tax impact for a small complying fund of a finding that general fund expenses are non-arm's length by the application of the 'twice the difference' in subsections 295-550(8) and (9).

88. ~~[Omitted.]As stated in paragraph 19 of this Ruling, in some instances the non-arm's length expenditure will have a sufficient nexus to all of the ordinary and/or statutory income derived by the complying superannuation fund. Where the fund incurs non-arm's length expenditure of this nature, the nexus between the expenditure and all the income derived by the fund is sufficient for all the income to be NALI under paragraphs 295-550(1)(b) and (c).~~

89. ~~[Omitted.]It is the Commissioner's view that to avoid the application of the NALI provisions, parties to these arrangements must deal at arm's length and that arm's length expenditure amounts be incurred by the complying superannuation fund (subject to any discount policy referred to in paragraph 51 of this Ruling).~~

90. ~~[Omitted.]It is particularly important for trustees of large APRA-regulated superannuation funds to have appropriate internal controls and processes in place to enable trustees to demonstrate that they have made reasonable attempts to determine arm's length expenditure amounts when making acquisitions from related parties. Appropriate internal controls and processes will be dependent on several factors including the size and nature of the arrangement. Having appropriate controls and processes should form part of the fund's tax risk management and governance framework.~~

91. ~~[Omitted.]Nevertheless, the Commissioner is alive to concerns that a finding that general fund expenses are non-arm's length is likely to have a very significant tax impact on the complying superannuation fund, even where the relevant expenses are immaterial.~~

92. ~~[Omitted.]For this reason, from 1 July 2023, where the ATO applies any compliance resources for such general fund expenses, they will only be directed:~~

- ~~for an SMSF — toward ascertaining whether the parties have made a reasonable attempt to determine an arm's length expenditure amount for services provided to the fund, other than services provided by an individual either acting in the capacity as trustee of the SMSF or as a director of a body corporate that is a trustee of the fund, and~~
- ~~for a large APRA-regulated superannuation fund — toward reviewing supporting documentation that evidences that appropriate internal controls and processes are in place and that reasonable steps were taken to determine an arm's length expenditure amount.~~

93. ~~[Omitted.]Provided this is the case, the ATO will not allocate compliance resources to determine whether those expenses are in fact arm's length expenses.~~

94. ~~[Omitted.]This compliance approach does not impact the compliance approach set out in Practical Compliance Guideline PCG 2020/5 *Applying the non-arm's length income*~~

LCR 2021/2DC

Status: **draft for comment**

~~provisions to 'non arm's length expenditure'—ATO compliance approach for complying superannuation entities. PGG 2020/5 sets out a compliance approach with respect to non arm's length expenditure of a general nature that has a sufficient nexus to all ordinary and/or statutory income derived by the complying superannuation fund that is incurred on or before 30 June 2023.~~

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Appendix 2 – Your comments

95. You are invited to comment on this draft Ruling including the proposed date of effect. Please forward your comments to the contact officer by the due date.

96. A compendium of comments is prepared when finalising this Ruling, and an edited version (names and identifying information removed) is published to the Legal database on ato.gov.au. Please advise if you do not want your comments included in the edited version of the compendium.

Due date: 24 January 2025
Contact officer: Bonita Tsang
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