



Australian Government

Australian Taxation Office

Ruling compendium – LCR 2021/2

❗ Relying on this Compendium

This Compendium of comments provides responses to comments received on draft Law Companion Ruling LCR 2021/2DC *Non-arm's length income – expenditure incurred under a non-arm's length arrangement*. It is not a publication that has been approved to allow you to rely on it for any purpose and is not intended to provide you with advice or guidance, nor does it set out the ATO's general administrative practice. Therefore, this Compendium does not provide protection from primary tax, penalties or interest for any taxpayer that purports to rely on any views expressed in it.

Summary of issues raised and responses

All legislative references in this Compendium are to the *Income Tax Assessment Act 1997*, unless otherwise indicated.

Issue number	Issue raised	ATO response
1	General comment While we acknowledge the ATO's efforts to clarify the application of the non-arm's length expenditure (NALE) provisions, significant uncertainties remain, particularly concerning the: • delineation between trustee and individual capacities • nexus between NALE and income • disproportionate impact on a self-managed superannuation fund (SMSF) due to minor compliance breaches.	We have noted this submission.
2	Arm's length and market value The draft update to the Ruling references concepts such as 'arm's length' and 'market value'; however, neither term is defined or fixed. The final update to the Ruling needs to provide solid guidance on how a superannuation fund can establish an appropriate commercial price. The Explanatory Memorandum to the Treasury Law Amendment (2018	The purpose of the update to the Ruling was to provide our view as to how the amendments in <i>Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Act 2024</i> apply in respect of the NALE and non-arm's length component (NALC) provisions. Advice concerning market valuations and the provision of a safe harbour concerning the use of valuations is beyond the scope of this update.

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	Superannuation Measures No. 1) Bill 2019 (EM to the TLA Bill 2019) said the following, at paragraph 2.49: It can be difficult to determine an exact price that is 'non-arm's length'. An 'arm's length' price may be accepted to fall within a range of commercial prices. Industry seeks express acknowledgment in the final update to the Ruling of paragraph 2.49 of the EM to the TLA Bill 2019 and to reflect the process of negotiation. We are concerned that the ATO remains silent on the fact that it is ubiquitously difficult to definitively determine what an arm's length price or value might be. The final update to the Ruling would be improved if this point was acknowledged. The final update to the Ruling should also contain guidance on how small superannuation funds may acceptably determine the lower and upper bounds of appropriate commercial prices and how they may then decide on an appropriate price or value to apply in a particular circumstance. The ATO should provide examples and guidance on some types of assets where an acceptable range of value might apply to show when NALE is not enlivened. The ATO should also consider the introduction of safe harbour provisions which allow some variance in market value, within an acceptable range.	Guidance on market value and general valuation principles to assist SMSF trustees can be located at Guide to valuing SMSF assets and Market valuation for tax purposes.
3	Record-keeping requirements for asset acquisitions We acknowledge that taxpayers are required to retain adequate records to accurately determine their tax liabilities. What evidence would prove that the transaction had been completed on arm's length terms?	The purpose of the update to the Ruling was to provide our view as to how the amendments in <i>Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Act 2024</i> apply in respect of the NALE and NALC provisions. What constitutes acceptable record keeping is beyond the scope of this update. However, our website provides guidance to assist SMSF trustees. Refer to SMSF record-keeping requirements, Guide to valuing SMSF assets and Market valuation for tax purposes.

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4	Internal SMSF arrangements and trustee capacity issues Overall, we consider that the ATO has provided insufficient guidance in the draft update to the Ruling to enable SMSFs to identify whether services provided to it by a trustee constitutes an internal fund arrangement or the provision of services in another capacity. It would be valuable for the final update to the Ruling to provide guidance, as well as examples of services, that could be provided by trustees who work in a trade occupation (for example, builders, joiners or carpenters), and to indicate if certain services are provided in their capacity as trustee. Such people may be employees and may be registered, but not individually licensed. To reduce ambiguity and compliance risk, the ATO needs to provide clearer guidance to trustees on the delineation of roles, where members with relevant skills (for example, advisers, accountants or lawyers) perform fund-related tasks. Trustee capacity – rebuttal of presumption The ATO's position in the draft update to the Ruling (at paragraph 47) is that services are presumed to be provided in a trustee capacity unless evidence indicates otherwise. However, the draft update to the Ruling provides limited guidance on how this presumption can be rebutted, particularly in scenarios where trustees or directors possess professional skills and licences that could benefit their funds but do not meet all of the requirements of section 17B of the <i>Superannuation Industry (Supervision) Act 1993</i> (SISA). Paragraph 42 – non-applicability of NALI rules Paragraph 42 of the draft update to the Ruling uses the statutory restriction in the SISA as the reason for the non-arm's length income (NALI) rules to not apply. The internal	The Ruling articulates a number of factors at paragraph 47 that we consider will be relevant in determining the capacity in which an individual operates. It is necessary to consider these factors on a case-by-case basis depending on the particular facts of each arrangement. Paragraph 47 of the Ruling also confirms that 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 the Ruling, unless there are factors that suggest a contrary conclusion. The update to the Ruling has revised paragraph 42 to confirm that the NALI provisions will not be enlivened where statutory restrictions prevent the trustee from receiving remuneration. The update has also revised paragraph 43 of the Ruling to confirm that where a trustee or a director of a corporate trustee operates in another capacity and can receive remuneration for their service under section 17B of the SISA, arm's length remuneration must be paid for those services to avoid the application of the NALI provisions. Additionally, Example 7A was also added in the update to the Ruling to provide further guidance.

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	nature of the relationship is a more valid reason for the NALI rules not to apply and should be included in the paragraph.	
5	Application of section 17B of the <i>Superannuation Industry (Supervision) Act 1993</i> If section 17B of the SISA applies, an SMSF can avoid the application of section 295-550 by ensuring that a trustee receives arm's length remuneration for services provided. The converse also applies. That is, if section 17B of the SISA does not apply, the trustee cannot be remunerated for the services provided (in their individual capacity), which would, therefore, create potential exposure to section 295-550. We request that the ATO provide sufficient further guidance in relation to the requirements of section 17B of the SISA so that SMSFs are able to identify and manage this issue. A 'safe harbour' compliance approach could be considered to not apply ATO compliance resources to determine whether section 295-550 applies in scenarios where a trustee is prohibited by section 17A of the SISA from being remunerated by an SMSF for services that are general in nature (for example, when the trustee does not carry on business in their own right, such as where the trustee is an employee).	See our response to Issue 4 of this Compendium. Whether section 17A or 17B of the SISA applies is a question of fact to be determined based on the circumstances of each case. Safe harbours relating to the application of section 17B of the SISA have not been included in the update to the Ruling.
6	Trustees of fixed unit trusts Industry request that the final update to the Ruling includes commentary that the trustee of a fixed unit trust also has statutory and fiduciary duties and obligations which the fixed trust's deed and governing rules may empower the trustee to perform, and that the trustee's skills, knowledge and experience can assist the trustee to complete these tasks. Greater clarity is required to determine whether trustees of fixed unit trusts can apply their professional skills in fulfilling their duties without breaching their trustee capacity and tainting distributions to SMSF unit holders.	Whether a distribution from a fixed unit trust to an SMSF is NALI as a result of actions taken by the trustee of the fixed unit trust extends beyond consideration of the NALF rules (which is the focus of this Ruling) and requires proper consideration of all the facts and circumstances relevant to that distribution.

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	Inclusion of an example in the final update to the Ruling, applying Ruling principles at the unit trust level will provide certainty for SMSF trustees and ensure alignment of the ATO's view across different trust structures.	
7	Acquiring units in a unit trust It would be beneficial to many SMSFs for the ATO to provide guidance through an example where an SMSF has invested in a unit trust that continually issued units at a fixed price of \$1 prior to 1 July 2018, despite the net tangible asset value behind the unit trust increasing in value. In certain cases, where the unit trust is 100% owned by the SMSF, the issue of units at \$1 rather than the net tangible asset value may have been due to an oversight. Guidance on the applicability of the NALE provisions in these circumstances would be beneficial.	Paragraph 8B of the Ruling confirms that the NALE provisions do not apply to expenditure incurred or expected to have been incurred before 1 July 2018. However, it is noted that the exclusion does not limit the potential application of other NALI provisions, depending on the facts of each case. In the final update to the Ruling, footnote 8A of paragraph 8B has been added to clarify that the other NALI provisions in section 295-550 can still apply to expenditure incurred or expected to have been incurred before 1 July 2018 where the requirements in those provisions are met.
8	Discount policies There are a number of aspects of paragraph 51 of the draft update to the Ruling that would benefit from further explanation: • Why is 'same discounts' in paragraph 51 plural? Does this mean the same discount has to be provided to employees and partners but the discount provided to each can be different? • Could the ATO confirm its view on discount policies that do not strictly apply to all employees? The overarching principle in this regard appears to be that the policy be 'consistent with normal commercial practices'. On that basis, it seems that a policy that did not apply to all employees may be considered arm's length, provided it can be demonstrated that the policy was formulated on a commercial basis. • The inclusion of the requirement that the trustee must not be able to influence the discount policy creates	In the final update of the Ruling, paragraph 51 of the Ruling has been revised to refer to 'same discount' to address the typographical error. Discount policies are on arm's length terms where they are consistent with normal commercial practices. This will be dependent on the facts and circumstances of each case. Instances where the trustee is able to influence the discount policy or where the discount is not available to all employees, partners, shareholders or office holders, may raise concerns as to whether the discount is consistent with normal commercial practices. In the final update, paragraph 51 of the Ruling has also been revised to reflect the need to focus on normal commercial practices. Revisions have also been made in the final update to the wording of paragraph 60 in Example 8 to ensure consistency with the updated position in paragraph 51.

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	uncertainty, especially given that the word 'influence' is not defined. We consider it inappropriate for there to be a blanket exclusion of an SMSF to obtain an arm's length discount merely because the fund's trustee is in the position to influence the discount policy. We consider that the sentence regarding the trustee's influence on the discount policy should be removed or revised from paragraph 51 and Example 8 in the final update of the Ruling. Small businesses, particularly those where an SMSF trustee or director is a sole director of the business may find it challenging to demonstrate that they cannot influence a discount policy. If retained, specify permissible levels of trustee input without triggering the NALE provisions through examples. We recommend the ATO clarifies whether the mere decision to implement a discount policy is sufficient to demonstrate influence, noting that this would effectively preclude any trustee from implementing a discount policy where they own and operate a small business as a sole proprietor.	
9	Paragraph 18 and footnote 17 Paragraph 18 of the draft update to the Ruling says that (emphasis added): 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). There <i>will</i> 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 the asset ... Paragraph 18 refers readers to footnote 17, which says:	We consider that paragraph 18 of the Ruling reflects the better view of the application of the provisions. This is consistent with paragraph 7.40 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), for the NALE amendments being the subject of the Ruling, which states (emphasis added): Where a specific expense is incurred as a result of a scheme in which the parties are not dealing with each other at arm's length and the entity is a small APRA-regulated fund or SMSF, the amount of income that is non-arm's length income is the same as the treatment prior to these amendments. <i>All of the ordinary or statutory income that results from the scheme is non-arm's length income.</i> Accordingly, we maintain the view as expressed in the Ruling.

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	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 ... However, paragraph 2.41 of the EM to the TLA Bill 2019 states (emphasis added): In some circumstances, non-arm's length capital expenditure can result in a superannuation entity earning non-arm's length income. Where a fund acquires an asset for less than market value through non-arm's length dealings, the revenue generated by that asset <i>may be</i> non-arm's length income, as well as any statutory income (that is, net capital gains) resulting from the disposal of that asset. We are concerned about the use of the word 'will' in paragraph 18 as there will be circumstances where an asset purchased for less than market value may not lead to any resultant capital gains being taxed as NALI as acknowledged in the EM to the TLA Bill 2019.	
10	Employee stock ownership plans Paragraph 51 of the draft update to the Ruling, requiring 'all' members of a specific group, such as employees, officers or partners, does not reflect typical arm's length commercial practices, is not supported by law, and sets an unrealistic standard. For example, an employee stock ownership plan (ESOP) only mandates a certain participation level, like an offer to at least 75% of permanent employees as per Division 83A. Referring to an ESOP arrangement where a member obtains a discount, it would be helpful if the ATO could clarify in the final update to the Ruling whether this discount would trigger NALF, or if there are grounds where that discount would not give rise to NALF.	Discount policies are on arm's length terms where they are consistent with normal commercial practices. This will be dependent on the facts and circumstances of each case. Instances where the trustee is able to influence the discount policy or where the discount is not available to all employees, partners, shareholders or office holders, may raise concerns as to whether the discount is consistent with normal commercial practices. In the final update to the Ruling, paragraph 51 of the Ruling has been revised to reflect the need to focus on normal commercial practices It will be necessary to consider the specific facts and circumstances of the arrangement to determine how the guidance in paragraph 51 may apply.

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11	Employee share schemes Industry asks the ATO for guidance on how the NALI provisions could potentially apply to employee share schemes. We are aware of published edited private advice (authorisation number 1052314103521) published on the ATO's website on 16 December 2024. If any of the facts changed, would section 295-550 apply? For example, many employee share schemes are only offered to a particular class of employee, such as senior managers and executives. Alternatively, participation in the employee share scheme may be offered to greater than say, 75% of permanent employees who have completed at least 3 years of service (for example, as required by section 83A-105). It is recommended that a specific example be included in the final update to the Ruling that also addresses the application of the SISA, particularly restrictions under section 66. We also recommend provision of real-world examples with genuine employee share scheme structures in the final update to the Ruling.	Employee share schemes are highly fact-specific and variable. However, we consider that the Ruling contains sufficient guidance (including paragraph 51, as revised in the final update to the Ruling) to apply the relevant principles, and examples, to assist trustees to comply with the NALI provisions. The application of section 66 of the SISA is beyond the scope of the update to the Ruling. The application of section 66 will be dependent on the facts and circumstances of each case.
12	Provision of trustee guarantees We would argue that personal guarantees provided by superannuation fund trustees should not lead to the NALI provisions applying because third-party arrangements by lenders or others (such as builders) would demand a superannuation fund's trustees provide a personal guarantee. We believe the final update to the Ruling should discuss and provide an example about this issue.	It would be necessary to consider the specific facts and circumstances of the arrangement to determine how the NALI provisions may apply.
13	Example 1 Example 1 of the Ruling is no longer necessary as the topic is discussed in greater detail in Taxation Determination TD 2024/5 <i>Income tax: how the non-arm's length income and</i>	We consider that Example 1 of the Ruling demonstrates specific expenditure and the calculation of the NALC. It has therefore been retained in the final update to the Ruling.

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	<i>capital gains tax provisions interact to determine the amount of statutory income that is non-arm's length income.</i> If the ATO wishes to retain Example 1, then it should discuss the market [value] substitution rule and refer to TD 2024/5.	The purpose of the example is not to work through the calculation of the amount of statutory income by reference to the capital gain that is included in the taxpayer's assessable income. It is therefore not necessary for the example to discuss the market value substitution rule or the views set out in TD 2024/5.
14	Example 2 We note that in the draft update to the Ruling, Example 2 has been updated to take into account the changes made by the Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Bill 2023 (EM to the TLA Bill 2023). It should be further updated to: - discuss the issue of establishing an appropriate arm's length value (as per <i>BPFN and Commissioner of Taxation</i> [2023] AATA 2330 (<i>BPFN</i>)) - acknowledge that the EM to the TLA Bill 2023 states, at paragraph 7.32 (emphasis added): ... Provided that the amount charged for any such services <i>is not less than</i> that which would be expected to be charged between parties dealing at arm's length, the dealings are not subject to the non-arm's length income rules. In such cases, the trustee of an SMSF may also be prevented from charging any more than the arm's length price because of the regulatory requirements in the SIS Act (see section 17B of the SIS Act, which permits a trustee to charge up to an arm's length amount for duties or services performed other than in the capacity as trustee).	We consider that Example 2 and the Ruling contains sufficient guidance outlining the principles to be applied to assist trustees to comply with the NALI provisions. Guidance on market value and general valuation principles to assist SMSF trustees can be located at Guide to valuing SMSF assets and Market valuation for tax purposes.
15	Example 3 We believe the matters discussed in Example 3 of the draft update to the Ruling are covered in TD 2024/5 and Taxation Ruling TR 2010/1 <i>Income tax: superannuation contributions</i>. If the ATO wishes to retain Example 3, it should be updated to discuss the market substitution rule in greater detail (and not include this subject as a separate subject and its own	We consider that Example 3 of the Ruling demonstrates the type of expenditure that is a specific expense and, as a result, the need to use the 'lesser of' calculation to determine the superannuation fund's NALC. It has therefore been retained. The purpose of the example is not to work through the calculation of the amount of statutory income by reference to the capital gain that is included in the taxpayer's assessable income. It is therefore not necessary for the

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	stand-alone example) and also refer to TD 2024/5 and TR 2010/1.	example to discuss the market value substitution rule or the views set out in TD 2024/5. However, in the final update to the Ruling, this example has been further revised to remove any reference to 'capital' expenditure. Whether an expense is a general or specific expense for NALI purposes does not rely on a determination of the expense being capital or revenue in nature. This is supported by subsection 295-550(7), which states that 'paragraphs (1)(b) and (c) and (5)(b) and (c) apply to a loss, outgoing or expenditure whether or not it is of capital or of a capital nature'.
16	Example 4 We are disappointed Example 4 of the draft update to the Ruling does not discuss Practical Compliance Guideline PCG 2016/5 <i>Income tax – arm's length terms for Limited Recourse Borrowing Arrangements established by self-managed superannuation funds</i> as well as Taxation Determination TD 2016/16 <i>Income tax: will the ordinary or statutory income of a self-managed superannuation fund be non-arm's length income under subsection 295-550(1) of the Income Tax Assessment Act 1997 (ITAA 1997) when the parties to a scheme have entered into a limited recourse borrowing arrangement on terms which are not at arm's length?</i>. Reference should be made to a limited recourse borrowing arrangement (LRBA) set on arm's length terms but then accidentally falling outside the rules, where the mistake is promptly corrected. For example, an LRBA may be structured and maintained at arm's length but miss an interest and principal repayment in a particular year, which is rectified as soon as the issue is identified. In ordinary commercial lending arrangements, a catch-up payment would be permitted. In this scenario, due to the nature of the NALE, we do not consider that there is sufficient nexus to the future capital gain derived by the fund on the disposal of the asset acquired under the LRBA.	We consider that paragraph 37, as revised in the final update to the Ruling reflects the better view of the application of the provisions. PCG 2016/5 and TD 2016/16 are not referenced in the Ruling. Practical compliance guidelines set out practical administration approaches to assist taxpayers in complying with relevant tax laws and are not rulings. Provided you follow the guidelines in good faith, we will administer the law in accordance with the approach in the guideline. As Example 4 of the Ruling provides guidance as to the application of the NALE provisions, a reference to TD 2016/16 is not relevant as that Determination provides guidance as to the application of paragraph 295-550(1)(a).

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	Further guidance is necessary to assist trustees to determine market-based lending terms when a third-party lender is only able to provide indicative terms, not binding contractual terms.	
17	Example 5 In the final update to the Ruling, Example 5 should provide guidance on establishing an appropriate arm's length value.	We consider that Example 5 and the Ruling contains sufficient guidance outlining the principles to be applied to assist trustees to comply with the NALI provisions. Guidance on market value and general valuation principles to assist SMSF trustees can be located at Guide to valuing SMSF assets and Market valuation for tax purposes .
18	Example 6 In the final update to the Ruling, Example 6 should be expanded to discuss the alternative that Leonie uses her employer's tax agent portal to lodge the SMSFs annual return. The example should also clarify whether the ATO's conclusion would be different if Leonie used the equipment or assets of her employer or lodged the SMSF's return under her employer's tax agent registration (or both). The treatment of expenses ordinarily deductible under section 25-5 should also be considered here. Example 6 focuses on the capacity in which the service is undertaken, ignoring the absence of a required nexus to the fund's income. This example is misleading and should be amended to acknowledge that section 295-550 does not apply in such cases, making the question of capacity irrelevant. Example 6, which assumes no use of professional equipment or licences, does not reflect common scenarios where trustees may use such resources incidentally for fund purposes.	See our response to Issue 4 of this Compendium. In the final update to the Ruling, we have added footnote 18A to paragraph 19 of the Ruling, to reference the interaction of the NALI provision with section 25-5. Example 6 (at paragraph 54) has also been clarified to state that the accounting services include services other than those relating to complying with, or managing, the SMSF's income tax affairs and obligations, which are ordinarily deductible under section 25-5.

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19	Example 7 In the final update to the Ruling, Example 7 should be expanded to discuss the situation where Levi performed tasks at his business premises – or anywhere else that is not his principal place of residence – especially as, based on the wording of this example, he is likely to be an employee of the business.	See our response to Issue 4 of this Compendium.
20	Example 8 In Example 8 of the draft update to the Ruling, we do not consider that Sasha's employer would be a third party. We accept, however, that based on the facts she cannot influence the discount rate offered by her employer. In the final update to the Ruling, Example 8 should be expanded to include the additional situation where Sasha has a degree of influence on the discount rate and what process should be followed to establish an arm's length price should also be discussed as per <i>BPFN</i>.	We disagree and consider Sasha's employer to be another party, separate to Sasha and Sasha's fund. In the final update to the Ruling, paragraph 51 has been revised to reflect the need to focus on normal commercial practices. Updates have also been made to paragraph 60 to ensure consistency with the updated position in paragraph 51. We consider that these updates and the Ruling contains sufficient guidance outlining the principles to be applied to assist trustees to comply with the NALI provisions. The final update has also clarified paragraph 59 to indicate that section 25-5 does not apply in the circumstances of the Example. Guidance on market value and general valuation principles to assist SMSF trustees can be located at Guide to valuing SMSF assets and Market valuation for tax purposes.
21	Example 9 Issues that we have with Example 9 of the draft update to the Ruling include: What would be the NALI outcome if Trang had the skills, knowledge and experience to complete all tasks in renovating the bathroom and kitchen in the second apartment such as tiling or waterproofing, but did not hold formal trade qualifications for those tasks? We consider the correct interpretation in this case is that, in part, Trang has provided professional services (the specific plumbing work) and, in part, trustee services (those not requiring her plumbing trade skills, knowledge or experience). Trang will need a	We consider that Example 9 accurately sets out our view in determining whether an individual is performing an activity as a trustee of the superannuation fund or whether they are acting in a different capacity. We also consider that it accurately reflects our view on how the NALF rules apply in the facts and circumstances outlined. We consider that in the scenario contemplated in the Example, there is a sufficient nexus between the NALF incurred by the SMSF in acquiring the plumbing services for the second SMSF rental property and the rental income derived, as well as with any future amount of statutory income, determined by reference to any capital gain derived by the fund on the disposal of the second SMSF rental property. See TR 2010/1 for further guidance on the interaction of the contribution and NALI provisions.

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	reasonable and acceptable method of determining an arm's length price for her professional services. • In relation to the first dot point, what if Trang completed all tasks during normal business hours (and only performed this work when third-party clients had not asked her to complete work for them on a particular half or full day) and also used her employee's time and energy to complete these tasks as otherwise that person would not have been employed gainfully? • It would be open to Trang to value her work on the apartment's bathroom and kitchen as an in specie contribution on the arm's length determined increase in market value of the apartment as per paragraphs 29 to 32B of draft Taxation Ruling TR 2010/1DC2 <i>Income tax: superannuation contributions</i>. This point should be acknowledged in the final update to the Ruling. Trang will need a reasonable and acceptable method of determining an arm's length market value both before the renovations commence and once they are completed. • The EM to the TLA Bill 2023 says, at paragraph 7.40: Where a specific expense is incurred as a result of a scheme in which the parties are not dealing with each other at arm's length and the entity is a small APRA-regulated fund or SMSF, the amount of income that is non-arm's length income is the same as the treatment prior to these amendments. All of the ordinary or statutory income that results from the scheme is non-arm's length income. We would argue that further guidance is required to determine the ordinary and statutory income from the scheme in this case. • It is well accepted that, over time, kitchens and bathrooms in residential premises must be replaced	The updates made to Example 9 were made to reflect our view as to how the amendments in <i>Treasury Laws Amendment (Support for Small Business and Charities and Other Measures) Act 2024</i> apply in respect of general and specific expenditure and that the SMSF's NALC is calculated using the 'lesser of' calculation. Guidance on market value and general valuation principles to assist SMSF trustees can be located at Guide to valuing SMSF assets and Market valuation for tax purposes. However, in Example 9, we note that Trang does not charge the SMSF for the work undertaken in respect of the second SMSF rental property. Our view on what constitutes a sufficient nexus for the purpose of applying the NALC provisions is explained at paragraphs 17A to 21 of the Ruling.

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	due to normal wear and tear, improvements in equipment and changing consumer tastes. The ATO typically allows depreciation at 2.5% per year over 40 years commencing when construction has been completed. The declining value of the work performed needs to be discussed in this example as this will feed into the SMSF's capital gains tax (CGT) calculations and will also feed into the capital gain made in relation to the 'scheme'. • Renovating the bathroom and kitchen, Trang is merely acting like any prudent owner would, by using her skills, knowledge and experience to keep the costs of completing these renovation tasks as low as possible. Acting prudently is a statutory prudential requirement and a common trustee obligation. There appears to be an assumption in the draft update to the Ruling that by renovating the kitchen and bathroom of the second apartment, Trang has improved that property. • We are of the view that Example 9 of the draft update to the Ruling is impractical. If Levi, as illustrated in Example 7 of the draft Ruling, is allowed to make occasional contributions to his SMSF portfolio as a trustee without the application of NALI provisions, it raises a question regarding why Trang, in Example 9, is restricted from conducting a bathroom renovation on a fund asset in her capacity as a trustee. Given that Trang is unlikely to engage in such renovations regularly, the associated costs would be incorporated into the asset's cost base. If her labour is to be considered, the market value of the service provided should be treated as a cost base adjustment.	
22	Example 10 In the final update to the Ruling, this example should be expanded to include the situation where Jean is a retired	As we consider that the proposed expansion may have limited application in practice, we have not expanded Example 10 of the Ruling. We otherwise refer to our response to Issue 4 of this Compendium.

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	electrician, however, retains his licence, but is no longer providing services to the general public.	
23	Examples 11 and 12 We have no comment about these examples.	We have noted this submission.
24	Example 13 We believe the matters discussed in this example are covered in TD 2024/5 and TR 2010/1. If the ATO wishes to retain Example 13, it should be updated to discuss the market substitution rule in greater detail (and not include this subject as a separate subject and its own standalone example) and also refer to TD 2024/5 and TR 2010/1.	We consider that Example 13 of the Ruling demonstrates the application of the CGT market value substitution rule in section 112-20 in circumstances where the parties did not deal with each other at arm's length, as well as the calculation of the NALC. The example has therefore been retained. Guidance on market value general valuation principles to assist SMSF trustees can be located at Guide to valuing SMSF assets and Market valuation for tax purposes .
25	Deductibility of expenses – additional clarity Greater clarity is needed around the deductibility of expenses under section 25-5. It is unclear how this applies in many cases, including for superannuation funds that have no accumulation assets (that is, only have pension assets) because, like all other superannuation funds, these funds still have ordinary or statutory income.	In the final update to the Ruling, we have added footnote 18A to paragraph 19 of the Ruling to reference the interaction of the NALI provision with section 25-5.
26	Proposed additional examples We recommend that additional examples are included in the final update to the Ruling to: - clarify the distinction between actions taken in an individual capacity versus those undertaken as a trustee, particularly in scenarios where a trustee, director or member of an SMSF is also involved in an entity in which the SMSF invests, such as a private company or unit trust - understand whether a minor utilisation of a professional qualification or licence could lead to NALC – for example, if an accountant prepares accounts during their personal time with minimal use of business	See our response to Issues 4 and 6 of this Compendium. In the final update to the Ruling, we have included an additional example (Example 7A) to assist in determining the capacity in which an individual is acting.

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	resources and the SMSF does not incur any fee, it would be helpful to confirm that if the lodgment is made through their firm's tax agent registration, it would not give rise to NALE - clarify if, where an SMSF experiences reduced income, whether it is classified as NALE – for example, when income derived from a related party lease is not indexed - outline where an expense paid on behalf of a fund constitutes NALE – for example, fees paid by a member relating to documents setting up an SMSF and the corporate trustee.	
27	De minimis threshold We recognise that the setting of a <i>de minimis</i> threshold for NALI is generally a policy decision. However, the Commissioner may exercise his remedial powers to establish such a threshold, and in our view, it is important to have such a safe harbour in place. It is recommended that safe harbour provisions introduce materiality thresholds to guide trustees on acceptable incidental use of professional licences and resources, reducing uncertainty and compliance burdens.	The Commissioner's remedial power under Subdivision 370-A of Schedule 1 to the <i>Taxation Administration Act 1953</i> is beyond the scope of these updates. Safe harbours have not been included in the update to the Ruling.
28	The distinction between contributions and NALI or NALE The draft Ruling lacks a clear delineation between contributions and NALE. Historically, the ATO has regarded payments made on behalf of a fund, including a discount on an ESOP, as contributions. In practice, expenses incurred on behalf of a fund often go unrecognised until a later financial year when they are reported in the financial statements as sundry creditors. There is a genuine concern that SMSF auditors and the ATO may consider such amounts as invoking NALE.	It is necessary to consider the particular facts and circumstances of an arrangement to determine whether a small complying superannuation fund has incurred less expenditure, or no expenditure, under a scheme than it might have been expected to have incurred in gaining or producing ordinary or statutory income if the parties to the scheme had been dealing with each other at arm's length. We consider that paragraphs 27 to 39 and 51 of the Ruling contain sufficient guidance on contributions and discounts respectively to assist trustees. Updates to TR 2010/1 clarify our position concerning the interaction of the NALI rules when a member of a superannuation fund makes a contribution to the fund.

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	Accordingly, further guidance from the ATO is necessary to clarify the treatment of the expenses incurred on behalf of the fund and guidance added to the final update to the Ruling must be consistent. We also request further clarification as invariably, in practice, an expense paid on behalf of a fund is not detected until a subsequent financial year and reported in the financial statements as a sundry creditor. However, there is fear that SMSF auditors and ATO officers might consider these amounts as invoking NALE. There is no clear guidance or divide in the draft update to the Ruling between what is considered a contribution and what is considered NALE.	
29	Date of effect Paragraph 8B of the draft update to the Ruling states that: The non-arm's length expenditure provisions do not apply to expenditure incurred or expected to have been incurred before 1 July 2018. This necessitates clarification regarding the Ruling's applicability to that prior period. The final update to the Ruling should explicitly address the circumstances of non-arm's length acquisitions that occurred before 1 July 2018 but were subsequently sold on an arm's length basis after this date. For example, if an asset valued at \$20,000 is acquired for \$10,000 (50% of its market value) before 1 July 2018, it is important to clarify whether the NALE provisions would apply to the subsequent sale of that asset, provided that all related transactions were conducted at arm's length.	See our response to Issue 7 of this Compendium.
30	Rectification The final update to the Ruling should address whether non-arm's length transactions can be rectified, specifically if subsequent payments or reimbursements of expenses can effectively 'untaint' the income. For example, where an asset is purchased at less than its market value, recording an	We do not consider that subsequent payments or reimbursements of expenses, as outlined in the comment, would impact the treatment of ordinary or statutory income under section 295-550 where a small complying superannuation fund has incurred NALE as described in the Ruling. It is necessary to consider the NALE incurred by the fund under the identified scheme.

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	in specie contribution for the balance would be a practical and efficient solution to resolve such issues. If such rectification is not permissible, an explanation should be provided. Although we recognise that delayed payments may contravene other provisions of the SISA, such as those related to arm's length dealings or separation of assets, it is our view that rectification could resolve issues pertaining to NALI and NALE.	The Ruling addresses how the NALI rules interact with the making of in specie contributions – we consider that there is sufficient guidance in the Ruling and examples in respect of in specie contributions. See paragraphs 27 to 30 and Examples 3 and 5 of the Ruling. See also TR 2010/1 for further guidance.
31	Meaning of key terms Further clarity is required on several factors, including the difference between: • general and specific expenses • capital and revenue expenses • pre-acquisition and post-acquisition expenses relating to an asset, and • general expenses and those tax-deductible under section 25-5. Given the potential for various combinations of these expenses, guidance and additional examples from the ATO in the final update to the Ruling would be beneficial in navigating these complexities.	We consider that there is sufficient guidance in the Ruling to address the difference between general and specific expenses. See paragraphs 8A, 9 to 11D, 18 and 19 (and examples 1 to 4, 9 and 11 to 12) of the Ruling. It is noted that this is consistent with the guidance provided in the EM to the TLA Bill 2024. Whether an expense is capital or revenue in nature is not determinative in ascertaining whether an expense is a general or specific expense for NALI purposes – see subsection 295-550(7) which states that ‘paragraphs (1)(b) and (c) and (5)(b) and (c) apply to a loss, outgoing or expenditure whether or not it is of capital or of a capital nature.’ Further, paragraph 17A of the Ruling confirms that the main issue is whether there is a sufficient nexus between the expenditure and income, regardless of whether the expense is capital or revenue in nature. In the final update to the Ruling, Example 3 has been revised to avoid any confusion. Footnote 18A has also been added to paragraph 19 of the Ruling to provide additional content concerning the application of section 25-5.
32	Part acquisition and part contribution When a trustee of an SMSF acquires an asset using both cash and in specie member contributions, several commercial issues arise. As specified in paragraph 29 of the draft update to the Ruling, an in specie contribution can occur simultaneously with an SMSF purchasing a portion of an asset, as long as	Stamp duty consequences with respect to particular arrangements are beyond the scope of this Ruling.

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	the contract specifies that the SMSF is acquiring only a portion of the asset. For stamp duty assessments, the entire market value of the property is considered, leading to questions about stamp duty liability when the SMSF is only a partial legal owner.	
33	Cost recovery – paragraph 53 The elaboration on cost recovery in paragraph 53 of the draft update to the Ruling is, in our view, very broad and should be removed. Cost recovery is used in various industries, including architecture, building and construction, and various trades. We consider that the inclusion of this paragraph is inappropriate, and it is unnecessary to connect it explicitly to paragraph 51 of the Ruling, which can apply without express reference.	We maintain the view as expressed in paragraph 53 of the draft update to the Ruling. However, the final update to the Ruling has revised the paragraph to clarify that pricing based on cost-recovery basis when applying ordinary commercial pricing policies is not consistent with an arm's length dealing.
34	Practical compliance guideline We consider a practical compliance guideline would provide helpful guidance on how ATO compliance resources will be allocated.	A compliance approach has not been included in the update to the Ruling.
35	NALE and nexus to income of the fund We consider the ATO view of what a 'sufficient nexus' is, is too broad and lacks the necessary precision with incurring a particular expense to the related ordinary or statutory income that flows from such an expense that becomes tainted. We therefore request the ATO to reconsider its 'nexus' theory following passage of the 2024 amendments. General expenses have now been dealt with by the 2024 amendments and therefore the ATO should revise its view, as a specific expense can taint an asset forever in a fund if there is a sufficient nexus (for example, see the Trang example in Example 9 of the draft update to the Ruling where the second rental property is tainted while owned by her fund).	See our response to Issue 9 of this Compendium. We do not consider that the 2024 amendments impact our views, outlined in paragraphs 17 to 19 of the Ruling, concerning identifying whether there is a sufficient nexus between the NALE and the relevant ordinary or statutory income. In the final update to the Ruling, footnote 18A has been added to paragraph 19 of the Ruling, which recognises that expenditure deductible under section 25-5, which would not also satisfy the requirements of section 8-1, does not have a sufficient nexus to ordinary or statutory income and accordingly, the NALI provisions will not apply to this expenditure.

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	In this regard, we ask that in the final update to the Ruling, the ATO outline any case law and authority (apart from ATO materials) that it can provide for advisers and taxpayers to better understand the nexus needed and when a specific or general expense will have the requisite nexus to ordinary and statutory income. In the final update to the Ruling, the ATO should consider a complementary paragraph to paragraph 19, listing common expenses where no sufficient nexus to the fund's income exists.	
36	Financial advice and NALE The draft update to the Ruling oversimplifies the interaction of the NALE provisions with the operation of the <i>Corporations Act 2001</i> and financial services law. For example, there are nuances with licensed advisers providing personal financial advice to themselves or their SMSF and charging a fee, as these laws require the adviser and client to be distinct parties. We recommend explicit guidance on the treatment of financial advice fees to align the final update with existing legal frameworks and ensure it provides workable and realistic compliance pathways for SMSF trustees who are also licensed advisers.	Issues as to the application of the <i>Corporations Act 2001</i>, or other laws dealing with the provision of financial advice, are beyond the scope of this update.
37	Specific NALE – revenue or capital We welcome the ATO taking on board industry's previous comments to remove reference to expenses of a 'recurrent nature'. However, we do not believe edits to paragraph 21 of the Ruling in the draft update are sufficient to provide the clarity industry needs to understand when NALI could apply to any future capital gain on disposal of an asset. When read in conjunction with edits made to Example 9 in the draft update (Trang's example), we believe the rationale for the change aligns with the concept of revenue versus	The words 'recurrent expenditure' were previously used in the Ruling to describe NALE that does not relate to the acquisition of any particular asset and that only has a nexus with the fund deriving ordinary or statutory income during a particular income year. It was used to highlight a scenario where that NALE did not have a nexus with ordinary or statutory income derived in a later income year. This description was removed based on feedback from industry that it caused confusion. The removal of 'recurrent expenditure' has no impact on the substantive content and our position in respect of identifying whether a non-arm's length expense has a sufficient nexus with an amount of ordinary or statutory

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	capital expenses. If this is correct, this should be explicitly outlined in the final update to the Ruling. We recommend that: • The ATO should explicitly clarify the rationale for the removal of the term ‘recurrent expense’ in paragraph 21 of the Ruling, particularly as it relates to tainting future capital gains. • NALE that merely maintains or repairs an asset to ensure its continued functioning should only result in NALI for the income year in which it was incurred, assuming exceptions for trustee capacity do not apply.	income being derived by a small complying superannuation fund. See paragraphs 17 to 20 of the Ruling. We consider that there is sufficient guidance in the Ruling to address the difference between general and specific expenses. Whether an expense is capital or revenue in nature is not determinative in ascertaining whether an expense is a general or specific expense for NALI purposes. See our response to Issue 31 of this Compendium. A distinction between maintenance and repairs is not relevant in determining whether an expense is a non-arm’s length expense.
38	NALE and capital gains tax – scope and proportionality of penalties The ATO view that specific NALE of a capital nature can taint all income and any future capital gain linked to the asset permanently, irrespective of how minor the expense is, is a disproportionate outcome. The Commissioner should consider the exercise of their general powers of administration, in accordance with Law Administration Practice Statement PS LA 2009/4 <i>Decisions made by the Commissioner in the general administration of the taxation laws</i>, to mitigate the disproportionate CGT outcomes for capital improvements under the NALI or NALE provisions.	The Commissioner’s general administration of the taxation laws, as outlined in PS LA 2009/4, is beyond the scope of this update. We consider that the positions set out in the Ruling on this issue are consistent with policy intent as referenced in the Ruling.
39	Private advice Two instances of edited private advice (Authorisation numbers 1052132378413 and 1052155666298) highlight several areas where the ATO’s approach in the final update to the Ruling needs refinement: • The threshold test that needs to be applied by trustees in their circumstances needs to be clearly stated and supported with a clear explanation, noting that the	See our response to Issue 4 of this Compendium. The edited private advice referred to will be reviewed.

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	issue of materiality likewise is not clearly stated or discussed. Both pieces of edited private advice recognise that minor, infrequent, or irregular use of business equipment (for example, tax agent software or computers) does not, of itself, indicate that an individual is acting in their professional capacity rather than in their capacity as a trustee. This practical position should be explicitly addressed in the final update to the Ruling to provide certainty to trustees. In the advice with authorisation number 1052155666298, the ATO concluded that the trustee's use of their tax agent registration number, while incidental and for cost efficiencies, did not constitute NALE. This contrasts with the rigid approach implied in the draft update to the Ruling. The edited private advice emphasises the importance of trustees documenting their intention and capacity when providing services to the fund. This practice could be formally incorporated into the final update to the Ruling as a compliance safeguard, allowing trustees to demonstrate that their actions are within the scope of their trustee duties. The ATO should ensure the final update to the Ruling provides comprehensive examples reflecting practical realities, such as those outlined in the referenced private advice. The details in private rulings should be consistent and reflected in the final update to the Ruling.	