PCG 2020/5 - Applying the non-arm's length income provisions to 'non arm's length expenditure' - ATO compliance approach for complying superannuation entities

Applying the non-arm's length income provisions to 'non arm's length expenditure' – ATO compliance approach for complying superannuation entities

Relying on this Guideline
This Practical Compliance Guideline sets out a practical administration approach to assist taxpayers in complying with relevant tax laws. Provided you follow this Guideline in good faith, the Commissioner will administer the law in accordance with this approach.

Table of Contents | **Paragraph**

What this Guideline is about

1. This Guideline provides a transitional compliance approach for a complying superannuation entity concerning the application of the amendments to section 295-550 of the *Income Tax Assessment Act 1997*[1] where a superannuation entity incurs certain non-arm's length expenditure (or where expenditure is not incurred) in gaining or producing ordinary or statutory income. A complying superannuation entity refers to a complying superannuation fund, a complying approved deposit fund or a pooled superannuation trust. For the purposes of readability, a reference in this Guideline to a 'complying superannuation fund' applies equally to a complying approved deposit fund and a pooled superannuation trust.

Date of effect

2. This Guideline applies both before and after its issue in respect of the 2018–19, 2019–20, 2020–21, 2021–22 and 2022–23 income years.

[1] See the *Treasury Laws Amendment (2018 Superannuation Measures No. 1) Act 2019*.

Background

3. This Guideline should be read in conjunction with Law Companion Ruling LCR 2021/2 *Non-arm's length income – expenditure incurred under a non-arm's length arrangement*.

4. Section 295-550 of the *Income Tax Assessment Act 1997* sets out rules as to when a complying superannuation fund will derive non-arm's length income (NALI). The amendments to section 295-550[2] result in a complying superannuation fund deriving NALI in circumstances where the entity incurs 'non-arm's length expenditure' as described in paragraphs 10 to 13 of LCR 2021/2.[3] 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.[4]

5. The ATO has previously issued draft Law Companion Ruling LCR 2018/D10 *Non-arm's length income – expenditure incurred under a non-arm's length arrangement* when the amendments were originally introduced. LCR 2018/D10 was withdrawn following the lapsing of Treasury Laws Amendment (2018 Superannuation Measures No. 1) Bill 2018 when the 45th Parliament was prorogued and the House of Representatives was dissolved on 11 April 2019.

6. As a result of consultation feedback received on LCR 2018/D10, the ATO provided clarification on particular issues in draft Law Companion Ruling LCR 2019/D3 *Non-arm's length income – expenditure incurred under a non-arm's length arrangement* and then in LCR 2021/2. One of these issues concerned when non-arm's length expenditure will have a sufficient nexus with income derived by the complying superannuation fund for the NALI provisions to apply. In particular, the Commissioner has set out the view that certain non-arm's length expenditure incurred by a complying superannuation fund may have a sufficient nexus to all ordinary and/or statutory income derived by the fund for that income to be NALI (for example, fees for accounting services).[5] This can be contrasted to non-arm's length expenditure that has a more direct nexus to particular ordinary or statutory income derived by the fund (for example, expenditure relating to the acquisition of an income-producing asset).

7. The ATO recognises that trustees of complying superannuation funds may not have realised that the amendments will apply 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 fund in an income year, noting that it was not explicitly stated in LCR 2018/D10. It is also recognised that the amendments apply in relation to the 2018–19 and later income years which may result in all income derived by a fund during the 2018–19, 2019–20, 2020–21, 2021–22 and 2022–23 income years being classified as NALI where it has incurred non-arm's length expenditure of a general nature.

8. As there are some unresolved concerns raised by industry, the ATO considers it is appropriate to extend the transitional compliance approach to the income years outlined in paragraphs 9 and 10 of this Guideline. The ATO has also updated the compliance approach set out in paragraphs 88 to 94 of LCR 2021/2 to reflect this change.

The ATO's transitional compliance approach

9. The ATO will not allocate compliance resources to determine whether the NALI provisions apply to a complying superannuation fund for the 2018–19, 2019–20, 2020–21, 2021–22 and 2022–23 income years where the fund

[2] See the *Treasury Laws Amendment (2018 Superannuation Measures No. 1) Act 2019*.
[3] Further references in this Guideline to 'non-arm's length expenditure' has the same meaning as described in LCR 2021/2.
[4] See section 4 of Schedule 2 to the *Treasury Laws Amendment (2018 Superannuation Measures No. 1) Act 2019*.
[5] See Example 2 of LCR 2021/2.

incurred non-arm's length expenditure (as described in paragraphs 10 to 13 of LCR 2021/2) of a general nature that has a sufficient nexus to all ordinary and/or statutory income derived by the fund in those respective income years (for example, non-arm's length expenditure on accounting services). This transitional compliance approach only applies to general expenditure that is incurred on or before 30 June 2023.

10. This transitional compliance approach does not apply where the fund incurred non-arm's length expenditure that directly related to the fund deriving particular ordinary or statutory income.

Commissioner of Taxation
1 June 2020

Amendment history

Date of amendment	Part	Comment
10 June 2022	Paragraphs 2, 3, 4, 6, 7 to 9 Various	Amendments made to extend the compliance approach in this Guideline to the 2022–23 financial year References to LCR 2019/D3 updated with references to LCR 2021/2.
9 April 2021	Paragraphs 2, 7 and 10	Amendments made to extend the compliance approach in this Guideline to the 2021–22 financial year.

References

Previous draft:
Previously released in draft format as PCG 2019/D6

ATOlaw topics	Superannuation ~~ Funds ~~ Taxable income ~~ Non-arm's-length components
Legislative references	ITAA 1997 295-550 Treasury Laws Amendment (2018 Superannuation Measures No. 1) Act 2019
Related Rulings/Determinations	LCR 2018/D10W LCR 2019/D3 LCR 2021/2
Other references	Treasury Laws Amendment (2018 Superannuation Measures No. 1) Bill 2018
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