Super Clarity

SMSF Arm's Length Info Sheet: May 2026

A practical, audit-focused guide for SMSF professionals to identify risk, gather evidence, and report breaches of section 109 SIS while ensuring that the fund continues to meet the sole purpose test (section 62 SIS).

1. Quick Snapshot

- **General Rule:** If the fund did it, the file should show it (always provide contemporaneous evidence supporting arm's length dealings).
- **Section 109 SIS (arm's length):** Investments must be **made** and **maintained** on arm's length terms.
- **Section 62 SIS (sole purpose test):** Look for **current-day benefits**. Non-arm's length issues are often a practical "litmus test" for a s62 problem.

---

2. Key Definitions (plain English)

Term	Meaning
Arm's length	Would you do it on the same terms with a stranger? Focus on the **quality of the dealings** (terms, process, documentation), not just whether parties are related.
Market value	The amount a willing buyer would pay a willing seller, **assuming arm's length dealing** (no sweetheart deals; no fire sale; both parties have commercial market knowledge).
Incidental benefit	A benefit that is inherent/unavoidable, remote, isolated, or insignificant when assessed against proper retirement-purpose activities.

---

3. Section 109 SIS – Arm's Length Investments

- **S109:** Investments of superannuation entity to be made and maintained on arm's length basis (for as long as it is held, including at disposal)
- **SMSF:** must not invest unless the SMSF and other party are dealing with each other at arm's length (includes **related or unrelated** parties)
- **Related parties:** expect an inference that dealings may not be arm's length unless the trustee can demonstrate otherwise (documentation burden increases).

---

4. What Good Evidence Looks Like (s109)

- Independent valuation/appraisal at acquisition; trustee to provide objective, supportable data to confirm market value every year.
- Executed contracts/agreements on commercial terms (e.g., lease agreements and rental valuations for related-party tenants).
- Proof that ongoing terms are commercial: rent reviews, arrears management, enforcement steps, correspondence.
- Minutes/resolutions showing how trustees determined terms and considered potential alternatives.
- Evidence of payments (e.g. bank statements post-EOFY) and follow-up for late or unpaid amounts

---

5. Section 62: Sole Purpose Test

The SPT is met when, viewed objectively and holistically, the SMSF is maintained solely for retirement and permitted death/ancillary purposes. It must not deliver current-day benefits to members/relatives/other parties, especially on non-arm's length terms. Some of the more practical indications are:

Factors that may indicate an SPT breach	Factors that support SPT compliance
• Trustees sought or negotiated for the benefit. • The benefit influenced the investment/decision-making. • Benefit provided at a cost or detriment to the SMSF. • The pattern of events suggests a material, non-permitted benefit.	• Benefit is inherent/unavoidable in permitted activities. • Benefit is remote, isolated, or insignificant (incl. cumulatively). • Benefit provided on arm's length/market terms; no SMSF detriment. • Activities align with trustee covenants and a considered investment strategy.

---

6. Joining the dots: where s109 and s62 intersect

- **Non-arm's length terms** are frequently the factual signal that an SMSF may also be delivering a **current-day benefit** (raising an s62 issue).
- **Rent not collected**, "sweetheart deals", or **non-commercial loans** can commonly create a multi-breach fact pattern (s109 + s62 + s65, and sometimes in-house asset issues).

- **Tax impact:** If an SMSF derives income or capital gains in excess of what would be expected on arm's length terms, the NALI provisions may apply, resulting in those amounts taxed at the top marginal rate of 45%.

---

7. Practical checklist for SMSF professionals

a) Triage questions

- Who is the counterparty (member/relative/Part 8 associate/unrelated)?
- Is there any current-day benefit (use of asset, concessionary terms, unpaid amounts)?
- Are the terms commercial compared to the market? Would this happen with a stranger?
- Does the transaction align with the trust deed, the investment strategy and trustee covenants?

b) Evidence checklist (minimum file expectations)

- Trust deed support + minutes/resolutions for key decisions.
- Independent valuation(s) supporting acquisition/disposal/related leases.
- Signed agreements (lease/loan/contract) with commercial terms.
- Cashflow evidence: bank statements, ledgers, rental schedules, paid arrears.
- Enforcement evidence where payments were missed (letters, notices, repayment plans, legal steps).
- Third-party confirmations where appropriate.

c) Reporting decision

- Where evidence is insufficient, the auditor will document the reasons and may consider reporting that compliance cannot be confirmed (rather than asserting a definitive breach without support).
- Explain to trustees that an ACR is the auditor's opinion/reporting obligation, whereas an ATO review is a separate investigation.
- Encourage early rectification and (where appropriate) voluntary disclosure to the ATO.

Expert Advice.
SMSF Confidence.

Super Clarity is a specialist SMSF risk management firm designed for accountants, auditors and advisers seeking expert guidance.

Ready to simplify SMSF compliance?

Contact Shelley for tailored support, technical education and independent insights

Contact Us

Phone: 0400 281 800
Email: sbanton@superclarity.com.au
LinkedIn: Shelley Banton

Super Clarity