


CR 2007/64 - Income tax: treatment of payments received under the Securing our Fishing Future package: * Fishing Community Assistance to assist recipients to develop an existing business

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Class Ruling

Income tax: treatment of payments
received under the Securing our Fishing
Future package:

- Fishing Community Assistance to assist recipients to develop an existing business

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❶ This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 15-10 of the ITAA 1997;
- Part 3-1 of the ITAA 1997;
- section 104-25 of the ITAA 1997;
- subsection 110-45(3) of the ITAA 1997;

- subsection 110-55(6) of the ITAA 1997;
- paragraph 118-37(2)(a) of the ITAA 1997; and
- Part 3-3 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies is applicants who applied for and received payments to develop an existing business under the Fishing Community Assistance components of the *Securing our Fishing Future* Package (Package). The Ruling does not apply to those exempt entities specified in section 11-5.

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 13 to 28 of this Ruling.

6. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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Date of effect

8. This Ruling applies from 1 July 2006 to 30 June 2010. However, the Ruling continues to apply after this date to all entities within the specified class who entered into the specified scheme during the term of the Ruling, subject to there being no change in the scheme or in the entities involved in the scheme.

9. The Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

10. If this Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

11. If this Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

12. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Scheme

13. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them, form part of and are to be read with the description:

- Application for Class Ruling from the Department of Agriculture, Fisheries and Forestry (DAFF) dated 30 January 2006 and supplementary correspondence from DAFF dated 24 October 2006; and
- DAFF Securing our Fishing Future – Fishing Community Assistance Guidelines.

14. The Package, announced by the Australian Government on 23 November 2005, is a major structural adjustment package for the Australian fishing industry designed to reduce fishing capacity and better position the industry to be profitable and self-adjust in the future.

15. The Fishing Community Assistance component of the Package is to help communities that are vulnerable to the impacts of reductions in fishing activity associated with the Package by providing financial assistance to help stimulate sustainable new economic activity and employment opportunities in these communities.

16. DAFF makes a formal determination of the eligibility for Fishing Community Assistance and the level of assistance that may be granted.

17. There are 4 eligibility tests for Fishing Community Assistance:

- the applicant must be an eligible organisation;
- the applicant must have an Australian Business Number (ABN) or an Australian Company Number (ACN);
- the proposed activity must be an eligible activity type; and
- the proposed activity must be in an eligible activity location.

First eligibility test: eligible organisation

18. An applicant must be one of the following types of organisations:

- private enterprise businesses;
- cooperatives;
- local government bodies;
- community groups or councils;
- non-departmental government agencies; or
- non-profit organisations.

Second eligibility test: ABN or ACN

19. An applicant must have an ABN or an ACN. DAFF will not enter into a funding agreement with an applicant unless the applicant has an ABN or ACN.

Third eligibility test: eligible activity type

20. The applicant's proposed activity must stimulate economic activity or enhance employment opportunities. Appropriate uses of Fishing Community Assistance include:

- adding value to existing resources, products or business;
- establishing or expanding a business in response to demonstrated markets;
- creating sustainable new economic/employment opportunities;
- providing infrastructure that enhances economic opportunities;
- diversifying skill; and
- increasing the uptake of innovation, best practice or new technologies.

This Ruling only deals with Fishing Community Assistance that has been provided to an applicant to develop an existing business.

Fourth eligibility test: eligible activity location

21. The applicant's proposed activity must be located in a community that has been affected by the reduction in fishing activity associated with the Package.

22. Fishing Community Assistance funding may be considered for one or more stages of a multi-stage project including later stages of a project that has already commenced.

23. Fishing Community Assistance will fund projects of generally not more than \$500,000.

24. All applications in a funding round will be assessed and rated on a competitive basis according to:

- whether both the applicant and the proposed activity meet the eligibility requirements; and
- how the proposed activity meets the assessment criteria at clause 7.4 of the Securing our Fishing Future – Fishing Community Assistance Guidelines, compared to all other applications received from eligible applicants.

25. Meeting the eligibility requirements and assessment criteria to a high degree does not guarantee that the application will be successful.

26. Successful applicants will enter into a funding agreement with the Commonwealth. The funding agreement sets out the terms and conditions of the funding, including a schedule of payments linked to agreed milestones, outcomes and timeframes.

27. Fishing Community Assistance will not be paid until a funding agreement has been executed and the DAFF receive a properly rendered tax invoice from the successful applicant for the amount of payment. Subsequent payments will not be made until the DAFF receives:

- an acquittal showing that any previous payments made under the Fishing Community Assistance have been fully expended;
- progress reports as identified in the funding agreement; and
- a properly rendered tax invoice for the amount of the payment.

28. Fishing Community Assistance consists of two rounds. Round one opened on 28 September 2006, and Round two opened on 12 February 2007.

Ruling

Section 6-5 – income according to ordinary concepts

29. A payment received under the Fishing Community Assistance component of the Package to develop an existing business is not income according to ordinary concepts. The receipt is not assessable income under section 6-5.

Section 15-10 – bounty or subsidy

30. A payment received under the Fishing Community Assistance component of the Package to develop an existing business is a bounty or subsidy that is received in relation to carrying on a business. The receipt is assessable income under section 15-10.

Capital gains tax

31. A payment received under the Fishing Community Assistance component of the Package to develop a business is subject to the capital gains tax (CGT) provisions in Parts 3-1 and 3-3.

32. CGT event C2 under section 104-25 happens to the entitlement to receive the Fishing Community Assistance when the entitlement is satisfied.

33. However any capital gain or capital loss made as a result of a payment under the Fishing Community Assistance component of the Package to develop an existing business is disregarded under paragraph 118-37(2)(a).

34. To the extent that an amount paid under the Fishing Community Assistance component of the Package to develop an existing business relates to the acquisition of a new CGT asset, it is a recoupment of the cost of acquiring that asset. However, it is not excluded from the cost base or reduced cost base of the new asset because the amount of the recoupment is assessable income (subsection 110-45(3) and subsection 110-55(6)).

Commissioner of Taxation11 July 2007

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

Section 6-5 – income according to ordinary concepts

35. Subsection 6-5(1) provides that an amount is included in assessable income if it is income according to ordinary concepts (ordinary income). However, as there is no definition of 'ordinary income' in income tax legislation it is necessary to apply principles developed by the courts to the facts of a particular case.

36. Whether or not a particular receipt is ordinary income depends on its character in the hands of the recipient.¹

37. In *G P International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation*² (*G P International Pipecoaters*), the Full High Court stated:

To determine whether a receipt is of an income or of a capital nature, various factors may be relevant. Sometimes the character of receipts will be revealed most clearly by their periodicity, regularity or recurrence; sometimes, by the character of a right or thing disposed of in exchange for the receipt; sometimes, by the scope of the transaction, venture or business in or by reason of which money is received and by the recipient's purpose in engaging in the transaction, venture or business.

38. In considering whether a grant under the *Industrial Research and Development Grants Act 1967* was income according to ordinary concepts, Mahoney J in *Reckitt & Colman Pty Ltd v. FC of T*³ (*Reckitt & Colman*), said that the Court must examine the nature of the payment itself and the relationship of it to the activities, actual or potential of the recipient. A payment which is seen as provided for a purpose which is not part of the recipient's trade will not be income in nature (*Reckitt & Colman*). An example of a payment that was held not to be income in nature because it had nothing to do with the recipient's trade is provided in the following passage from the judgment of Hill J in *First Provincial Building Society Ltd v. Federal Commissioner of Taxation*⁴ (*First Provincial*):

In *Seaham Harbour Dock Co v. Crook* (*HM Inspector of Taxes*) (1931) 16 TC 333 (*Seaham Harbour Dock Co*), the House of Lords held that a grant made to a dock company by way of financial assistance in the extension of its dock did not constitute the 'annual profits or gains' of the taxpayer liable to tax under Case I of Schedule D of the *Income Tax Act 1918* (UK). The payment to the taxpayer there considered was made under legislation permitting assistance to be given in carrying out approved schemes of useful work to relieve unemployment. Their Lordships were unanimous that no tax was payable as the payment in question had nothing to do with the trade of the taxpayer.

¹ *Scott v. FCT* (1966) 117 CLR 514, *Hayes v. FCT* (1956) 96 CLR 47 and *Federal Coke Co Pty Ltd v. FCT* (1977) 7 ATR 519; 77 ATC 4255.

² (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1.

³ (1974) 74 ATC 4185; 4 ATR 501.

⁴ (1995) 56 FCR 320; 95 ATC 4145; (1995) 30 ATR 207.

Hill J noted that *Seaham Harbour Dock Co* was cited by the High Court in its judgment in *G P International Pipecoaters*, among other cases, as authority for the proposition that a gift or subsidy to 'replenish or augment the payee's capital' was not income in ordinary concepts because it could not fairly be said to be 'a product or incident of the payee's income-producing activity'.

39. Fishing Community Assistance considered in this Ruling is available to develop an existing business of eligible applicants whose proposed activity stimulates economic activity or enhances employment opportunities in communities vulnerable to the reduction in fishing activity under the Package. Like the grant in *Seaham Harbour Dock Co*, the Fishing Community Assistance is not a product or incident of any contract or agreement to supply goods or services in the applicant's trade. Rather, the Fishing Community Assistance is paid for the purpose of assisting the applicant with development costs. The nature of the Fishing Community Assistance and its relationship to the applicant's business activities show that the Fishing Community Assistance is capital in nature.

40. Fishing Community Assistance paid to a successful applicant is not income according to ordinary concepts and is not included in the taxpayer's assessable income under subsection 6-5(1).

Section 15-10 – bounty or subsidy

41. Section 15-10 provides that an amount is included in assessable income if it is:

- a bounty or subsidy;
- received in relation to carrying on a business; and
- not assessable as ordinary income under section 6-5.

Bounty or subsidy received in relation to carrying on a business

42. The terms 'bounty' and 'subsidy' are not defined in income tax legislation. The word 'subsidy', as noted by Windeyer J in *Placer Development Ltd v. Commonwealth of Australia*,⁵ derives from the Latin 'subsidium' meaning 'an aid or help'. The Macquarie Dictionary,⁶ defines subsidy as including 'a grant or contribution of money'. The ordinary meaning adopted by case law is 'aid provided by the Crown (government) to foster or further some undertaking or industry'.

⁵ (1969) 121 CLR 353.

⁶ 2001, rev, 3rd edn.

43. Following the decisions in *The Squatting Investment Co Ltd v. Federal Commissioner of Taxation*,⁷ *Reckitt & Colman Pty Ltd v. FC of T*,⁸ and *First Provincial*, it is now well accepted that a 'bounty' or 'subsidy' includes a financial grant made by a government. Fishing Community Assistance is a bounty or subsidy.

44. A bounty or subsidy will be 'in relation to' carrying on a business when there is a real connection between the payment and the business. The term 'in relation to' includes within its scope payments that have a direct or indirect connection to the business. As stated by Hill J in *First Provincial*:

The words 'in relation to' are words of wide import. They are capable of referring to any relationship between the two subject matters, in the present case the receipt of the bounty or subsidy, on the one hand, and the carrying on of the business, on the other ... the degree of connection will be 'a matter of judgment on the facts of each case'. ... What is necessary, at the least, in the present context is that there be a real connection ... the relationship need not be direct, it may also be indirect.⁹

45. A bounty or subsidy must be related to 'carrying on' the business not merely for commencing or ceasing a business. As stated by Hill J in *First Provincial*:

the relationship must be to the 'carrying on' of the business. These words may perhaps be understood in opposition to a relationship with the actual business itself. They would make it clear, for example that a bounty received, merely in relation to the commencement of a business or the cessation of the business, would not be caught. The expression 'carrying on of a business' looks, in my opinion, to the activities of that business which are directed towards the gaining or producing of assessable income, rather than merely to the business itself.¹⁰

46. A government payment to industry received by an entity to assist with the costs of developing an existing business is received in relation to 'carrying on' a business.¹¹

47. Fishing Community Assistance paid to a successful applicant to develop an existing business is a bounty or subsidy received in relation to the carrying on of a business for the purposes of section 15-10. Accordingly, the receipt is assessable income under section 15-10.

⁷ (1953) 86 CLR 570; 10 ATD 126; (1953) 5 AITR 496.

⁸ (1974) 74 ATC 4185; 4 ATR 501.

⁹ (1995) 56 FCR 320 at 333.

¹⁰ (1995) 56 FCR 320 at 332.

¹¹ See *Plant v. Commissioner of Taxation* [2004] AATA 1296, where it was held that a capital payment that assisted in the creation of a bigger and more efficient workshop was received in relation to the carrying on of the business.

Capital gains tax

48. CGT event C2 under section 104-25 happens when the entitlement to receive the Fishing Community Assistance to develop an existing business is satisfied, that is, when the assistance is paid by way of a reimbursement directly to the applicant or payment of expenses on the applicant's behalf.

49. However, any capital gain or capital loss made as a result of a payment of Fishing Community Assistance is disregarded under paragraph 118-37(2)(a).

50. Paragraph 118-37(2)(a) provides a CGT exemption by disregarding a capital gain or capital loss that results from receipt of a payment as reimbursement or payment of expenses under a scheme established under legislation by an Australian government agency. The Fishing Community Assistance is paid under such a scheme.

Payment relates to acquisition of new CGT asset

51. A payment of Fishing Community Assistance to develop an existing business where the payment is a recoupment of the entity's expenditure to acquire a new CGT asset does not reduce the cost base (or reduced cost base) of the asset acquired. This is because, although the expenditure is recouped, the Fishing Community Assistance to develop an existing business is assessable income under section 15-10 (subsection 110-45(3) and subsection 110-55(6)).

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Subject references:

- bounties & subsidies
- capital gains tax
- capital receipts
- government grants income
- income

Legislative references:

- TAA 1953
- TAA 1953 Sch 1 357-75(1)
- ITAA 1997 6-5
- ITAA 1997 6-5(1)
- ITAA 1997 11-5
- ITAA 1997 15-10
- ITAA 1997 Pt 3-1
- ITAA 1997 104-25
- ITAA 1997 110-45(3)
- ITAA 1997 110-55(6)
- ITAA 1997 118-37(2)(a)
- ITAA 1997 Pt 3-3
- Copyright Act 1968
- Industrial Research and Development Grants Act 1967
- Income Tax Act 1918 (UK)

Case references:

- Federal Coke Co Pty Ltd v. Federal Commissioner of Taxation (1977) 7 ATR 519; 77 ATC 4255
- First Provincial Building Society Ltd v. Federal Commissioner of Taxation (1995) 56 FCR 320; 95 ATC 4145; (1995) 30 ATR 207

- G P International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1
- Hayes v. Federal Commissioner of Taxation (1956) 96 CLR 47
- Placer Development Ltd v. Commonwealth of Australia (1969) 121 CLR 353
- Plant v. Commissioner of Taxation [2004] AATA 1296
- Reckitt & Colman Pty Ltd v. Federal Commissioner of Taxation (1974) 4 ATR 501; 74 ATC 4185
- Scott v. Federal Commissioner of Taxation (1966) 117 CLR 514
- Seaham Harbour Dock Co v. Crook (HM Inspector of Taxes) (1931) 16 TC 333
- The Squatting Investment Co Ltd v. Federal Commissioner of Taxation (1953) 86 CLR 570; 10 ATD 126; (1953) 5 AITR 496

Other references:

- Macquarie Dictionary, 2001, rev. 3rd edn, The Macquarie Library Pty Ltd, NSW
- Department of Agriculture, Fisheries and Forestry Securing our Fishing Future – Fishing Community Assistance Guidelines
<www.daff.gov.au/fishingfuture>

ATO references

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