


CR 2007/87 - Income tax: treatment of payments received under the Lower Murray Darling Catchment Management Authority Rangelands Incentive Strategy - Conservation Reserves and Sustainable Grazing Schemes

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Class Ruling

Income tax: treatment of payments received under the Lower Murray Darling Catchment Management Authority Rangelands Incentive Strategy – Conservation Reserves and Sustainable Grazing Schemes

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ⓘ 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 considered in this Ruling are:

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- subsection 6-5(1) of the ITAA 1997;
- section 8-1 of the ITAA 1997;
- section 15-10 of the ITAA 1997;
- Division 31 of the ITAA 1997;

- Subdivision 40-G of the ITAA 1997;
- section 104-25 of the ITAA 1997;
- paragraph 118-20(1)(a) ITAA 1997, and
- paragraph 118-37(2)(a) 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 landholders who receive a stewardship payment and/or on-ground works payment under the Lower Murray Darling Catchment Management Authority (LMDCA) Rangelands Incentive Strategy – Conservation Reserves and Sustainable Grazing Schemes. This Ruling does not apply to government agencies, non-government organisations or groups whose income is otherwise exempt.

Qualifications

4. 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 12 to 29 of this Ruling.

5. 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

7. This Ruling applies from 1 July 2006 to 30 June 2016. However, the Ruling continues to apply after 30 June 2016 to all entities within the specified class who entered into the specified scheme during the term of the Ruling.

8. 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.

9. 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)).

10. 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.

11. 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

12. 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:

- Class Ruling request from LMDCMA and further information provided by LMDCMA on 12 June 2007 and 7 August 2007;
- Rangelands Incentive Strategy detailed information form;
- Rangelands Incentive Strategy Landholder information sheet – (as modified on 11 April 2007);
- LMDCMA Fact sheet No. 39 – *Establishment of Grazing and Conservation Reserves* (as modified on 13 December 2006);

- LMDCA Fact Sheet No. 36 – *Incentives to establish Sustainable Grazing Schemes* (as modified on 13 December 2006);
- Sample Property Vegetation Plans provided by LMDCA; and
- Catchment Management Authority New South Wales Info Sheet 1 – *How does native vegetation improve farm profitability* DNR 05_047_1a.

13. The Rangelands Incentives Strategy (RIS), delivered by the LMDCA, aims to increase the area actively managed for conservation in the Lower Murray Darling Catchment and improve vegetation conditions across the catchment to achieve vegetation targets specified by the *Lower Murray Darling Catchment Action Plan (2006)* (LMDCA CAP 2006).¹ The establishment of Conservation Reserves and Sustainable Grazing Schemes are key CMA strategies to achieve these targets.

RIS Conservation Reserves Scheme

14. The RIS Conservation Reserves Scheme provides a stewardship payment to eligible landholders who wish to permanently manage an area of their property for conservation according to an agreed Property Vegetation Plan (PVP). Landholders are required to address the following criteria:

- conservation area is managed to maintain and improve ecosystem functions under an approved PVP;
- conservation reserve must be adequately fenced to control entry of domestic stock (as well as feral and native herbivores in some cases);
- the landholder completes a training workshop on biodiversity assessment (fully funded by LMDCA); and
- the landholder undertakes annual monitoring and submits the results to the LMDCA.

15. The RIS Conservation Reserves Scheme also provides funding for the on-ground works necessary to establish a reserve. Works funded include:

- exclusion fencing – up to \$1,500/km for standard fencing and up to \$2,700/km for total exclusion fencing;
- water point management – up to \$1,500 for the removal or decommissioning of each open water point;

¹ LMDCA – Rangelands Incentives Strategy Landholder Information Sheet – updated 11 April 2007.

- control of an earth dam – up to \$2.70/m for total exclusion fencing where an earth dam is used for a water point and is fed exclusively by a rainfall catchment; and
- installation of a goat trap – up to \$300 for installation of trap gates to allow removal of goats.²

RIS Sustainable Grazing Scheme

16. The RIS Sustainable Grazing Scheme provides a stewardship payment to eligible landholders as an incentive for the improvement and maintenance of a minimum of 40% of ground cover across an entire property, through control of total grazing pressure. Landholders are required to address the following criteria:

- the sustainable grazing area is managed to maintain and improve vegetation condition under an approved PVP (this includes implementation of an agreed sustainable grazing plan);
- the landholder completes training workshop on sustainable grazing; and
- the landholder undertakes annual monitoring and submits the results to the LMDCA.

17. The RIS Sustainable Grazing Scheme also provides funding for the necessary on-ground establishment works. Works funded include:

- provision of a tank and trough to replace existing earth dams – up to \$2,600 for the provision of a tank and trough for each earth dam replaced and up to \$2,600 for the provision of a tank and trough for each new stock watering point installed; and
- exclusion fencing – up to \$2,600 for total exclusion fencing including a trap gate to allow removal of goats for each dam fed exclusively by rainfall.

Funding amount

18. Stewardship payments will be made on a dollar/hectare basis and calculated according to an environmental services score which is made up of scores for vegetation significance, site condition and management activities agreed.

19. On-ground works payments are worked out according to the limits specified in paragraphs 15 and 17 of this Ruling.

² The funding for the installation of goat traps only applies to strategic grazing reserves.

20. All stewardship and on-ground works payments are made on a dollar for dollar basis. That is, the landholder is required to provide a contribution that is equal to the amount of contribution that is specified in the PVP or PAMS³ Management Agreement (MA) for the on-ground works completed or stewardship provided. A landholder's labour/time component (at \$30/hr or current approved rate as determined by the LMDCMA from time to time) and use of own machinery (at 80% of a contractor's rate) will be considered as an in-kind contribution to a project.

Eligibility

21. Eligible recipients of on-ground works and stewardship payments include landholders and groups within the NSW Lower Murray Darling Catchment who have natural resource management responsibilities. The vast majority of land in this catchment is Western Land Lease. For the purposes of this Ruling all eligible applicants, including such leaseholders, will be referred to as 'landholders'.

22. Where applicable, the Western Lands Commissioner must endorse the agreements entered into between landholders and the LMDCMA and agree to change the lease conditions of affected leaseholds from grazing to conservation reserves.

Delivery mechanism

23. The primary delivery mechanism for the on-ground works incentives and/or stewardship payments is a PVP or MA. A PVP generally requires detailed mapping and significant field assessment and will be used for the larger property scale projects of \$10,000 or more. MAs will usually only require a simple map and little or no field assessment. They will be used for smaller projects of typically less than \$10,000, such as goat traps or water point control. Both MAs and PVPs are voluntary, legally binding agreements under the *Native Vegetation Act 2003*, between the landholder and the LMDCMA. They are a record of the terms of agreement and include standard conditions, special conditions, agreement objectives, agreement period, activities and milestones, landholder and property details and the payment schedule.⁴

24. The landholder is required to address, in the approved PVP, how the criteria in paragraphs 14 or 16 will be achieved and monitored. Indicators which the landholder may use to measure this include:

- achieving a 40% minimum level of ground cover to reduce wind and water erosion;

³ PVP Administration Management System (PAMS).

⁴ Four versions of these PVPs were provided by the LMDCMA with the class ruling application.

- achieving a target reduction in the number of feral and native herbivores; and
 - achieving an improvement in vegetation condition through the removal of stock from a reserve and preventing feral and native grazing animals from access to water.
25. The following features are common to the PVPs:
- the landholder agrees to:
 - undertake the agreed management actions within the time period specified in the PVP (on-ground works components are to be commenced or completed within the period specified for the management action and management actions are to continue for the term of the agreement);
 - obtain, maintain in force and comply with, all necessary statutory approval, consents and permits required for the carrying out of their obligations under the PVP;
 - allow the LMDCA access to the land for the purpose of auditing and monitoring compliance with the terms of the PVP;
 - notify the LMDCA prior to selling the land to which the PVP applies, and
 - retain receipts, records of all expenditures (including in kind expenditure and contributions) associated with the incentive payments, quotes or other documentations and provide them to LMDCA if requested.
 - the LMDCA agrees to pay the landholder the amount of contribution specified in the PVP in consideration of the landholder performing the obligations set out in the PVP; and

- both parties agree that the LMDCMA may terminate the agreement under the PVP by notice in writing to the landholder in the event that the landholder fails to comply with their obligations under the PVP. If the agreement under the PVP is terminated, the landholder must refund all the incentive payments under the PVP for works that are not completed.⁵

An Incentive Funding PVP can be negotiated to last for any length of time and is transferred to the new owner if the property is sold.⁶

26. The activities may be performed by the landholder themselves using their own labour and equipment at rates specified in the contract or they may utilise the services of a contractor.

Funding application process

27. Landholders who are eligible for funding are required to complete and submit an 'Incentives Application form'. The applicant is then contacted by a PVP Officer to discuss the application, and organise a site visit, if appropriate. The PVP Officer will provide advice and guidance on the minimum standards which the proposal must meet and will discuss funding options and assist in estimating the funding required. An environmental assessment is undertaken to evaluate the environmental benefits of the project. The project is given an environmental services score which is compared with the funding requirement. This determines a project value to assist with ranking against other proposals.

28. If a landholder's proposal is accepted, they will be issued with a draft PVP outlining the management actions and outcomes required, along with a proposed schedule of milestones and payments. Once the landholder accepts the offer, a final agreement is produced and approved. The landholder may then commence works and submit an invoice for the first payment instalment.

Circumstances where funding is not available

29. Funding is not available under these schemes for:

- conservation reserves established under other schemes;
- areas involving compliance issues or which were cleared without authorisation; and
- sites previously established as environmentally significant areas.

⁵ To receive continued funding the landholders need to provide evidence to the LMDCMA of their conservation efforts. Each year the applicant must submit photographs of each vegetation point and record ongoing changes in a diary. LMDCMA staff will also monitor progress on a regular basis.

⁶ See LMDCMA Fact Sheet No. 39.

Ruling

Exempt income

30. Neither a stewardship payment nor on-ground works payment received by a landholder under the RIS Conservation Reserves Scheme or Sustainable Grazing Scheme are exempt income.

Stewardship payment

Section 6-5 – income according to ordinary concepts

31. A stewardship payment received by a landholder under the RIS Conservation Reserves Scheme or Sustainable Grazing Scheme is income according to ordinary concepts and is assessable under section 6-5.

Capital gains tax

32. CGT event C2 under section 104-25 happens to the entitlement to receive the stewardship payment when the entitlement is satisfied.

33. However, any capital gain made as a result of a stewardship payment will under paragraph 118-20(1)(a) be reduced to the extent that the payment is included in assessable income.

On-ground works payment

Section 6-5 – income according to ordinary concepts

34. A payment for eligible on-ground works under the RIS Conservation Reserves Scheme or Sustainable Grazing Scheme is not income according to ordinary concepts and is not assessable under section 6-5.

Section 15-10 – bounty or subsidy

35. If the landholder is carrying on a business on the land, a payment received under the RIS Conservation Reserves Scheme or Sustainable Grazing Scheme for on-ground establishment works is assessable as a bounty or subsidy under section 15-10.

36. If the landholder is not carrying on a business on the land, a payment received under the RIS Conservation Reserves Scheme or Sustainable Grazing Scheme for on-ground establishment works is not assessable income under section 15-10.

Capital gains tax

37. CGT event C2 under section 104-25 happens to the entitlement to receive the on-ground establishment works payment when the entitlement is satisfied.

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

Deductions offsetting assessable income

39. No deduction is available under section 8-1, Division 31 or Subdivision 40-G for the expected reduction in value of the land as a consequence of the establishment of a conservation reserve.

Commissioner of Taxation

19 September 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.*

Exempt income

40. An amount of ordinary or statutory income is 'exempt income' if it is made exempt by a provision of the tax law or another Commonwealth law. Ordinary income is also exempt income to the extent that the ITAA 1997 excludes it (expressly or by implication) from being assessable income. However an amount of statutory income is exempt income only if it is made exempt from income tax by a provision of the ITAA 1997 outside Division 6 or another Commonwealth law. Payments made by the LMDCMA in accordance with an agreement with a landholder are not excluded from being assessable income either expressly or by implication.

Stewardship payment

Section 6-5 – income according to ordinary concepts

41. 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.

42. Whether or not a particular receipt is ordinary income depends on its character in the hands of the recipient.⁷ In *GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation*⁸ (the *Pipecoaters* case), 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.

⁷ *Scott v. Federal Commissioner of Taxation* (1966) 117 CLR 514 (the *Scott* case), *Hayes v. Federal Commissioner of Taxation* (1956) 96 CLR 47 (the *Hayes* case), *Federal Coke Co Pty Ltd v. Federal Commissioner of Taxation* (1977) 7 ATR 519; 77 ATC 4255.

⁸ (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1.

43. The landholder receives the amount of contribution specified in the PVP in consideration of the landholder performing the obligations set out in that agreement. One of those obligations is the undertaking of agreed management actions within the specified time period set out in the PVP. The agreed management actions always include annual monitoring and can include the reduction in grazing pressure from stock, feral and native herbivores. This can take the form of a de-stocking of a property which can be a total exclusion from the reserved area for the duration of the agreement, or an exclusion from the area for a specified period of the year for the duration of the agreement, in order to achieve specific ground cover targets.

44. A payment is not for the imposition of some restriction or fetter where an examination of the arrangement under which the payment was made shows that the restriction is not what the payment received by the taxpayer was for and is only incidental to the arrangement and a consequence of it (*MIM Holdings Ltd v. Commissioner of Taxation* 97 ATC 4420; (1997) 36 ATR 108) (the *MIM* case).

45. In the *MIM* case, the Full Federal Court found that a payment to a taxpayer under a 'Reservation Agreement' to ensure that the taxpayer's subsidiary would keep a defined part of its generating capacity available to supply the requisite electricity was not a payment for the imposition of some restriction or fetter. Northrop, Hill and Cooper JJ concluded that the payment was for ensuring that the taxpayer's subsidiary would supply the requisite electricity, and relying on *Hayes v. FCT* (1956) 96 CLR 47 (the *Hayes* case) and *Reuter v. FC of T* 111 ALR 716; 93 ATC 4037 said that 'amounts paid in consideration of the performance of services will almost always be income'.

46. The question of whether an amount is a product of the taxpayer's services (that is, paid in consideration of the performance of the taxpayer's services) has been considered in a number of High Court decisions. The following guidance is afforded by those decisions:

- the whole of the circumstances must be considered;⁹
- a generally decisive consideration is whether the receipt is the product in a real sense of any employment of, or services rendered by the recipient, or of any business, or any revenue production activity carried on by the recipient; and¹⁰

⁹ *The Squatting Investment Company Ltd v. FC of T* (1953) 86 CLR 570 (the *Squatting* case) at CLR 627.

¹⁰ The *Squatting* case at CLR 633; the *Hayes* case at CLR 56-57; the *Scott* case at CLR 527-528.

- other considerations that are relevant, but not decisive include:
 - the motive of the donor (payer) in paying the amount;¹¹
 - the regularity and periodicity of the payment¹² however a payment in a lump sum does not require a conclusion that the payment is capital;¹³ and
 - the recipient's expectation that an amount will be received.¹⁴

47. Although a PVP or MA may provide for a payment to be payable upon the de-stocking of a property (which may be an achievement of a milestone in the PVP), the payment is not considered in isolation as the de-stocking of a property is but one of a number of management actions covered by the PVP or MA and the payment merely forms part of the overall payment plan. The objective of the PVP or MA is to achieve the outcomes or targets that are directed towards achieving the LMDCA CAP 2006 vegetation targets. It follows that a stewardship payment under the RIS – Conservation Reserves Scheme or Sustainable Grazing Scheme is not a payment for the imposition of some restriction or fetter.

48. The PVP or MA is a legally binding agreement under the *Native Vegetation Act 2003* between the landholder and the LMDCA that specifies the rights and obligations of both the landholder and the LMDCA and includes a schedule of milestones to which the landholder needs to adhere to receive payment. Under the agreement between the landholder and the LMDCA the landholder agrees to provide services¹⁵ to the LMDCA over the specified period for consideration. The stewardship payment is the product, in a real sense, of the services rendered by the landholder.

49. Other considerations such as the landholder's expectation to receive the payment in return for undertaking activities as set out in the contract and the motive of the LMDCA (to give the landholder an incentive for carrying out the work) also support the conclusion that the stewardship payment is the product of the services rendered by the landholder.

¹¹ The *Hayes* case at CLR 55.

¹² *FC of T v. Dixon* (1952) 86 CLR 540 (the *Dixon* case) at CLR 568.

¹³ The *MIM* case at ATC 4430, applying the *Pipecoaters* case.

¹⁴ The *Dixon* case; the *Squatting* case. This principle was also applied in *FC of T v. Blake* (1984) 15 ATR 1006; 84 ATC 4661.

¹⁵ The services are in the form of management actions such as de-stocking a property, collecting, monitoring and reporting data, implementing a grazing plan, maintaining the exclusion zone, applying ecological fire management strategies, and retaining regrowth, dead timber and rocks.

50. The principle that an amount paid in consideration of the performance of services is income applies even though the services are provided in an isolated transaction that is not part of a continuing business or profession of rendering services (*Brent v. FCT* (1971) 125 CLR 418; (1971) 2 ATR 563; (1971) 45 ALJR 557). Accordingly, a stewardship payment received under a PVP or MA is ordinary income and is assessable under section 6-5.

Capital gains tax

51. CGT event C2 under section 104-25 happens when the entitlement to receive the stewardship payment is satisfied, that is, when the payment is made to the applicant.

52. However, any capital gain as a result of a payment of a stewardship payment is reduced in accordance with paragraph 118-20(1)(a).

53. Paragraph 118-20(1)(a) provides that any capital gain is reduced if, a provision of the Act outside Part 3-1 includes an amount (for any income year) in the assessable income because of the event. In this case the payment will be included in assessable income (see paragraph 50 of this Ruling). Consequently, any capital gain resulting from CGT event C2 happening in relation to the stewardship payment will be reduced to zero in accordance with paragraph 118-20(2)(a).

On-ground works payments

Section 6-5 – income according to ordinary concepts

54. Although the on-ground works payments are payable under the same PVP or MA as the stewardship payments, they are not payments for the performance of services but rather payments to be applied towards the costs of on-ground establishment works such as fencing, the decommissioning of water access points, or the installation of goat traps. These costs are capital in nature. A subsidy that is intended to assist a recipient with capital costs is a receipt of a capital nature (the *Pipecoaters* case). Accordingly, a payment for on-ground establishment works is not income according to ordinary concepts and is not assessable under section 6-5.

Section 15-10 – bounty or subsidy

55. 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.

56. 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* (1969) 121 CLR 353, derives from the Latin 'subsidiū' meaning 'an aid or help'. The Macquarie Dictionary, 2001, rev. 3rd edn, 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', which includes the payment of a financial grant.

57. A subsidy will be 'in relation to' carrying on a business when there is a real connection between the subsidy and the business. The term 'in relation to' includes within its scope subsidies that have a direct or indirect connection to the business. As stated by Hill J in the *First Provincial Building Society v. FCT* (1995) 56 FLR 320; 95 ATC 4145; (1995) 30 ATR 207 (the *First Provincial* case) when considering the former paragraph 26(g) of the *Income Tax Assessment Act 1936*:

The words 'in relation to' are words of wide import. They are capable of referring to any relationship between 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.

58. The expression 'carrying on of the business' looks to the activities of the business which are directed towards the gaining or producing of assessable income rather than merely to the business itself. In *First Provincial*, the Full Federal Court held that although the receipt lacked the necessary connection with the taxpayer's business activities to constitute ordinary income, it was received in relation to the carrying on of the taxpayer's business because the payment assisted the taxpayer to continue to carry on the taxpayer's business activities as a building society. The RIS Conservation Reserves and Sustainable Grazing Schemes seek to increase the area of native vegetation reserved and improve the condition of native vegetation communities on properties in the catchment. The establishment of Conservation Reserves and Sustainable Grazing Programs are key strategies to achieve this target. The relationship between the management of native vegetation and farming activities is described in the CMA New South Wales Info Sheet 1 – *How does native vegetation improve farm profitability*. It explains how '[f]arms with good vegetation can improve economic outcomes for farmers by improving land value, increasing productivity, and reducing operating costs'.¹⁶ Accordingly, where a landholder is carrying on a business on the land, the receipt of funding for on-ground works necessary to establish a Conservation Reserve or Sustainable Grazing Program is a bounty or subsidy received in relation to carrying on a business and is assessable under section 15-10.

¹⁶ See CMA New South Wales Info Sheet 1 – How does native vegetation improve farm profitability DNR 05_047_1a.

59. Where the landholder is not carrying on a business, the payment for on-ground establishment works does not constitute a bounty or subsidy received in relation to carrying on a business and is not assessable under section 15-10.

Capital gains tax

60. CGT event C2 under section 104-25 happens when the entitlement to receive the on-ground works payment is satisfied, that is, when the payment is made by way of reimbursement directly to the applicant or payment of expenses on the applicant's behalf.

61. However, any capital gain or capital loss made as a result of a payment of an on-ground works payment is disregarded under paragraph 118-37(2)(a).

62. 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 on-ground works payment is paid under such a scheme.

Deductions offsetting assessable income

General deductions – section 8-1

63. Section 8-1 allows a deduction for losses or outgoings to the extent that they are incurred in gaining or producing assessable income, or are necessarily incurred in carrying on a business for the purpose of gaining or producing assessable income. No deduction is available under section 8-1 where there is no actual loss or outgoing. No loss is incurred by a landholder where a PVP or MA requires a change to the purpose of the lease from grazing to conservation with the Western Lands Commission. In these circumstances, there is not a disposal of the land but rather a different income producing utilisation of the land.

64. A landholder may be able to deduct some of the expenses incurred in the course of producing the assessable income as represented by the stewardship payments. However a deduction is not available under section 8-1 where the losses or outgoings are of a capital, private or domestic nature, or are incurred in gaining or producing exempt income, or another provision prevents the taxpayer from deducting them.

Division 31

65. Division 31 creates a special scheme that enables taxpayers to access a deduction for the reduction in land value associated with entering into a conservation arrangement. Division 31 sets out the specific requirements that are needed to be met in order for a deduction to be claimed. One of the conditions is that the landholder must not receive any money, property or other material benefit for entering into the covenant.¹⁷ Failure to meet these requirements means that a deduction for the reduction in land value must be sought under the general provisions in section 8-1.

66. Landholders receiving money in the form of stewardship payments and on-ground works payment under the RIS Conservation Reserves or Sustainable Grazing Schemes are unable to meet the requirements of Division 31 and are not able to access a deduction for any reduction in the value in land under Division 31. There are further differences between the LMDCA agreements and the conservation covenants covered by Division 31 which prevent this specific deduction being available to LMDCA landholders.

Landcare deductions – Subdivision 40-G

67. Certain capital expenditure on landcare operations may qualify for outright deduction in the year the expenditure is incurred under Subdivision 40-G. The deduction applies to:

- taxpayers carrying on a primary production business on land in Australia;
- taxpayers carrying on a business (other than mining or quarrying) for a taxable purpose from the use of rural land in Australia; and
- rural land irrigation water providers whose main business is supplying water to primary producers and businesses using rural land.

68. It is not necessary for a primary producer to own the land on which the primary production business is being carried on in order to claim a deduction under this subdivision. A lessee is therefore entitled to deduct appropriate expenditure under this provision.

69. Deductions may be available under Subdivision 40-G for expenditure incurred by the landholder on actions such as the eradication of flora or fauna pests, prevention of land degradation, erection of fences, construction of levee banks and construction of drainage and other similar works. The deduction is also available for expenditure incurred in the capital repair of these facilities and the extension of landcare operations.

¹⁷ Paragraph 31-5(2)(b)

70. No deduction is available for any reduction in value of land as a consequence of the establishment of a conservation reserve. A reduction in value of land is not an expenditure and Subdivision 40-G has no application in these circumstances.

Appendix 2 – Detailed contents list

71. The following is a detailed contents list for this Ruling:

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Previous draft:

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Subject references:

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- grant
- landcare operation
- ordinary income
- subsidy

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NO: 2007/15895
 ISSN: 1445-2014
 ATOLaw topic: Income Tax ~~ Assessable income ~~ government payments
 Income Tax ~~ Capital Gains Tax ~~ CGT events C1 to C3 - end of a CGT asset