


TD 2006/D15 - Income tax: what amounts are included in 'establishment expenditure' for the purposes of working out the decline in value of a horticultural plant under section 40-545 of the Income Tax Assessment Act 1997 ?

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This document has been finalised by TD 2006/46.



Draft Taxation Determination

Income tax: what amounts are included in ‘establishment expenditure’ for the purposes of working out the decline in value of a horticultural plant under section 40-545 of the *Income Tax Assessment Act 1997*?

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

This publication is a draft for public comment. It represents the Commissioner’s preliminary view about the way in which a relevant taxation 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. You can rely on this publication (excluding appendixes) to provide you with protection from interest and penalties in the way explained below. If a statement turns out to be incorrect and you underpay your tax as a result, you will not have to pay a penalty. Nor will you have to pay interest on the underpayment provided you reasonably relied on the publication in good faith. However, even if you don’t have to pay a penalty or interest, you will have to pay the correct amount of tax provided the time limits under the law allow it.

Ruling

1. Only capital expenditure that is attributable to the establishment of a horticultural plant is establishment expenditure.
2. Capital expenditure includes expenses incurred in establishing or extending a plantation up to the stage of planting horticultural plants in their long-term growing medium. The cost of maintaining an established plantation is revenue in nature. Therefore, the cost of maintenance does not form part of establishment expenditure.
3. Establishment expenditure includes:
 - the cost of purchasing plants or seeds;
 - any costs incurred in preparing to plant;
 - the cost of planting the plants or seeds;
 - the costs of pots and potting mixtures (for potted plants);
 - the costs incurred in grafting trees; and

TD 2006/D15

- the cost of establishing plants used for associated purposes, such as for companion planting (if those plants are not horticultural plants in their own right).

Costs incurred in preparing to plant includes the part of the cost of ploughing, top dressing, fertilising, top soil enhancement, soil analysis tests, forming up planting rows and planting site surveys that is attributable to the establishment of a horticultural plant.

4. Establishment expenditure also includes the cost of maintaining plants until they are ready to be planted, because the dominant purpose of the expenditure is to preserve and improve the plants until they are ready to be used, by planting or establishing them in their long-term growing medium.

5. The cost of merely replacing a plant in an established orchard or plantation because of premature death or disease is not capital in nature and does not form part of establishment expenditure. Such costs are revenue in nature and would be deductible under section 8-1 of the ITAA 1997.

6. The cost of purchasing land to be used for growing a horticultural plant is not establishment expenditure, as the cost is attributable to the land rather than to the establishment of the plant.

7. The costs of draining swamp or low-lying land and of clearing land are specifically excluded from establishment expenditure under subsection 40-555(3) of the *Income Tax Assessment Act 1997* (ITAA 1997).

Date of effect

8. When the final Determination is issued, it is proposed to apply both before and after its date of issue. However, the Determination will 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 Determination.

Commissioner of Taxation

12 April 2006

Appendix 1 – Explanation

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

Explanation

9. The term 'establishment expenditure' is defined in section 40-545 of the ITAA 1997 as amounts of capital expenditure incurred that are attributable to the establishment of the horticultural plant. The amount of establishment expenditure is used in subsection 40-545(2) of the ITAA 1997 to work out the decline in value of a horticultural plant for an income year.

10. 'Establishment' is not defined for the purposes of section 40-545 of the ITAA 1997. However, in *The Macquarie Dictionary* (revised third edition, 2001) 'establish' in this context means:

- to set up on a firm or permanent basis; institute; found; and
- to settle or install in a position, business, etc.

11. In general terms, to establish a horticultural plant would be to plant it in its long-term growing medium.

12. Paragraph 5.24 of the Revised Explanatory Memorandum to the New Business Tax System (Capital Allowances) Bill 2001 makes it clear that the cost of establishing a horticultural plant extends beyond the cost of planting. Paragraphs 5.24 and 5.25 provide a number of examples of the costs of establishing horticultural plants (refer to paragraph 3 of this Ruling).

13. Establishment expenditure includes only capital expenditure. Costs incurred in acquiring plants and planting them to establish or extend a plantation are capital in nature. As Pincus J, with whom the other members of the Full Federal Court agreed, said in *FC of T v. Osborne* 90 ATC 4889 at 4895; (1990) 21 ATR 888 at 895:

It appears to be consistent with the trend of these authorities to hold that, in general, costs incurred in establishing a plantation of fruit or nut trees, at least up to the stage of getting seedlings in the ground, are capital expenses.

14. In some cases, a business will buy plants from a nursery under a contract where the purchased plants are held and maintained by the nursery until an agreed delivery date. The total cost charged by the nursery for the plants can include the cost of maintaining the plants until the delivery date. The maintenance costs could cover such services as potting, pruning, staking, weeding, spraying, watering and other horticultural services necessary to keep the plants alive and growing at an acceptable rate. As the maintenance cost relates to maintaining the plants prior to planting, the cost is capital in nature.

Appendix 2 – Your comments

Your comments

15. We invite you to comment on this draft Taxation Determination. Please forward your comments to the contact officer by the due date. (Note: The Tax Office prepares a compendium of comments for the consideration of the relevant Rulings Panel. The Tax Office may use a sanitised version (names and identifying information removed) of the compendium in providing its responses to persons providing comments. Please advise if you do not want your comments included in a sanitised compendium.)

Due date: 12 May 2006

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References

Previous draft:

Not previously issued as a draft

Subject references:

- establishment expenditure
- horticultural plant

Legislative references:

- ITAA 1997 8-1
- ITAA 1997 40-545
- ITAA 1997 40-545(2)
- ITAA 1997 40-555(3)

Case references:

- FC of T v. Osborne 90 ATC 4889; (1990) 21 ATR 888

Other references:

- The Macquarie Dictionary (revised third edition, 2001)
- Revised Explanatory Memorandum to the New Business Tax System (Capital Allowances) Bill 2001

ATO references

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