



# ***PR 2001/147 - Income tax: Willmott Forests Project - 2002 Prospectus***

 This cover sheet is provided for information only. It does not form part of *PR 2001/147 - Income tax: Willmott Forests Project - 2002 Prospectus*

 This document has changed over time. This is a consolidated version of the ruling which was published on *14 November 2001*



# Product Ruling

## Income tax: Willmott Forests Project - 2002 Prospectus

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### Preamble

*The number, subject heading, and the **What this Product Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Withdrawal**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. Product Ruling PR 1999/95 explains Product Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a public ruling and how it is binding on the Commissioner.*

### No guarantee of commercial success

The Australian Taxation Office (ATO) **does not** sanction or guarantee this product as an investment. Further, we give no assurance that the product is commercially viable, that charges are reasonable, appropriate or represent industry norms, or that projected returns will be achieved or are reasonably based.

Potential investors must form their own view about the commercial and financial viability of the product. This will involve a consideration of important issues such as whether projected returns are realistic, the 'track record' of the management, the level of fees in comparison to similar products, how the investment fits an existing portfolio, etc. We recommend a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential investors by confirming that the tax benefits set out below in the **Ruling** part of this document are available, **provided that** the arrangement is carried out in accordance with the information we have been given, and have described below in the **Arrangement** part of this document.

If the arrangement is not carried out as described below, investors lose the protection of this Product Ruling. Potential investors may wish to seek assurances from the promoter that the arrangement will be carried out as described in this Product Ruling.

Potential investors should be aware that the ATO will be undertaking review activities to confirm the arrangement has been implemented as described below and to ensure that the participants in the arrangement include in their income tax returns income derived in those future years.

### Terms of Use of this Product Ruling

This Product Ruling has been given on the basis that the person(s) who applied for the Ruling, and their associates, will abide by strict terms of use. Any failure to comply with the terms of use may lead to the withdrawal of this Ruling.

Participants may wish to refer to the ATO's Internet site at <http://www.ato.gov.au> or contact the ATO directly to confirm the currency of this Product Ruling or any other Product Ruling that the ATO has issued.

## What this Product Ruling is about

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1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax laws' identified below apply to the defined class of persons who take part in the arrangement to which this Ruling refers. In this Ruling this arrangement is sometimes referred to as the Willmott Forests Project - 2002 Prospectus or simply as 'the Project'.

### Tax laws

2. The tax laws dealt with in this Ruling are:
- Section 6-5 of the *Income Tax Assessment Act 1997* ('ITAA 1997');
  - Section 8-1 (ITAA 1997);
  - Section 17-5 (ITAA 1997);
  - Division 27 (ITAA 1997);
  - Division 35 (ITAA 1997);
  - Division 328 (ITAA 1997);
  - Section 82KL of the *Income Tax Assessment Act 1936* ('ITAA 1936');
  - Section 82KZL (ITAA 1936);
  - Section 82KZME (ITAA 1936);
  - Section 82KZMF (ITAA 1936); and
  - Part IVA (ITAA 1936).

### Goods and Services Tax

3. In this Ruling all fees and expenditure referred to include Goods and Services Tax ('GST') where applicable. In order for an entity (referred to in this Ruling as a Grower) to be entitled to claim input tax credits for the GST included in its expenditure, it must be registered or required to be registered for GST and hold a valid tax invoice.

### Changes in the Law

4. The Government is currently evaluating further changes to the tax system in response to the *Ralph Review of Business Taxation* and continuing business tax reform is expected to be implemented over a number of years. Although this Ruling deals with the taxation

legislation enacted at the time it was issued, later amendments may impact on this Ruling. Any such changes will take precedence over the application of this Ruling and, to that extent, this Ruling will be superseded.

5. Taxpayers who are considering participating in the Project are advised to confirm with their taxation adviser that changes in the law have not affected this Product Ruling since it was issued.

### **Note to promoters and advisers**

6. Product Rulings were introduced for the purpose of providing certainty about tax consequences for participants in projects such as this. In keeping with that intention, the Tax Office suggests that promoters and advisers ensure that participants are fully informed of any legislative changes after the Ruling is issued.

### **Class of persons**

7. The class of persons to whom this Ruling applies is the persons who are more specifically identified in the Ruling part of this Product Ruling and who enter into the arrangement specified below on or after the date this Ruling is made. They will have a purpose of staying in the arrangement until it is completed (i.e., being a party to the relevant Agreements until their term expires) and deriving assessable income from this involvement. In this Ruling these persons are referred to as 'Growers'.

8. The class of persons to whom this Ruling applies does not include persons who intend to terminate their involvement in the arrangement prior to its completion, or who otherwise do not intend to derive assessable income from it.

### **Qualifications**

9. The Commissioner rules on the precise arrangement identified in the Ruling. If the arrangement described in the Ruling is materially different from the arrangement that is actually carried out, the Ruling has no binding effect on the Commissioner. The Ruling will be withdrawn or modified.

10. A Product Ruling may only be reproduced in its entirety. Extracts may not be reproduced. As each Product Ruling is copyright, apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to the Manager, Legislative Services, AusInfo, GPO Box 1920, Canberra ACT 2601.

## Date of effect

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11. This Ruling applies prospectively from 14 November 2001, the date this Ruling is made. However, 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 (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

12. If a taxpayer has a more favourable private ruling (which is legally binding), the taxpayer can rely on that private ruling if the income year to which it relates has ended or has commenced but not yet ended. However if the arrangement covered by the private ruling has not commenced, and the income year to which it relates has not yet commenced, this Ruling applies to the taxpayer to the extent of the inconsistency only (see Taxation Determination TD 93/34).

## Withdrawal

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13. This Product Ruling is withdrawn and ceases to have effect after 30 June 2004. The Ruling continues to apply, in respect of the tax law(s) ruled upon, to all persons within the specified class who enter into the arrangement specified below. Thus, the Ruling continues to apply to those persons, even following its withdrawal, who entered into the specified arrangement prior to withdrawal of the Ruling. This is subject to there being no change in the arrangement or in the person's involvement in the arrangement.

## Arrangement

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14. The arrangement that is the subject of this Ruling is specified below. This arrangement incorporates the following documents:

- Application for a Product Ruling received on 17 August 2001;
- Draft Willmott Forests - 2002 Prospectus received on 19 October 2001;
- The Project Constitution lodged with the application for a Product Ruling;
- Compliance Plan for Willmott Forests Limited dated 23 May 2000;
- **Lease Agreement** between Willmott Forests Limited ('WFL') and the Grower;

- **Forestry Management Agreement** between WFL and the Grower;
- **Terms Agreement** between WFL and the Grower;
- Wood Purchase Agreement between Willmott Forests Limited and Austral Softwoods Bombala Pty Ltd dated 31 July 2001;
- Correspondence and attachments from WFL and WFL's Taxation Advisors dated 19 October 2001, 25 October 2001, 31 October 2001, 1 November 2001 and 5 November 2001.

**Note: certain information has been provided on a commercial-in-confidence basis and will not be disclosed or released under Freedom of Information legislation.**

15. The documents highlighted are those Growers enter into or become a party to. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate of a Grower, will be a party to, which are part of the arrangements to which this Ruling applies. The effect of these agreements is summarised as follows.

### Overview

16. This arrangement is called the Willmott Forests Project - 2002 Prospectus.

Location	Bombala region of south-east New South Wales
Type of business each participant is carrying on	Commercial forestry
Tree species	<i>Pinus radiata</i>
Number of Woodlots under cultivation	Unlimited
Minimum number of Woodlots than can be subscribed for	1 Woodlot
Size of each Woodlot	0.5 Hectare
Minimum number of trees per Woodlot	550 seedlings
The term of the investment	25 years
Initial cost to Growers	\$3,850 per Woodlot

Initial cost per hectare	\$7,700
Ongoing Costs to Growers	There are no ongoing payments for maintenance or lease rental. These costs will be covered by a percentage of Gross Timber Proceeds from the thinnings in Years 13 and 18 of the Project and the Clear Fell in Year 25 of the Project (see paragraphs 30 & 31).
Other costs to Growers	Insurance premiums re fire and wind damage after year 10 if a Grower so desires. Growers will also incur harvesting / marketing costs.
Other possible costs	Any other amounts agreed in writing between WFL and Growers.

17. Growers participating in the Project enter into a Lease Agreement and a Forestry Management Agreement. Growers lease a 0.5 hectare area of land called a 'Woodlot' from WFL for 25 years. A Grower must apply for a minimum of 1 Woodlot. There is no minimum or maximum amount that must be raised under the Prospectus. WFL has stated that the land for the Project is already available and WFL will have freehold title to the Project Land prior to allocation to Growers. Information provided in the 2002 Prospectus indicates that the Project Land will be drawn from land within the Bombala region of south-east New South Wales.

### **Lease Agreement**

18. The Lease is granted by WFL ('lessor') to Growers (lessee') under the terms of the Lease Agreement. Growers are granted an interest in land in the form of a lease to use their Woodlot for the purposes of conducting their afforestation business, including the right to harvest timber grown on the Woodlot. The lease is for 25 years and may be extended by 5 years or until such time as the trees have been harvested and the land made good, whichever is the sooner.

19. The lessee shall not use the land jointly with anyone else and retains the right to say when the trees are to be planted. It should be noted however that by virtue of the Forestry Management Agreement, the trees will be planted in the financial year in which a Grower is accepted into the Project (see paragraphs 22 & 23). If the lessee breaches any conditions, the lessor may enter the land to remedy the

breaches at cost to the lessee. If the lessee defaults, the lessor can re-enter the land. Re-entry by the lessor ends the lease but the lessor retains all rights under the general law including the right to sue the lessee for unpaid money or for damages for breaches of the lessee's obligations under the lease.

### **Forestry Management Agreement**

20. A Forestry Management Agreement is entered into between WFL ('the Manager') and each Grower. Growers contract with the Manager to establish and maintain the plantation until maturity. The Manager shall use all reasonable endeavours to complete the following works in accordance with good forestry practices in respect of the leasehold property. WFL may delegate its responsibilities.

#### ***Part 1 – preparation and planting (Services provided in year 1)***

- All planning and monitoring works – i.e., development and adherence to the Plantation Establishment Plan;
- Sample and soil testing;
- Allocation and survey – in field work, setting out firebreaks, access ways and other plantation feature;
- Preparation works – ripping, mounding and/or ploughing;
- Pre-planting weedicide treatments as required;
- Fencing as required;
- Supply and planting *Pinus radiata* seedlings (high quality *Pinus radiata* cuttings or seedling material) at a minimum rate of 550 per Woodlot;
- Fertilising, where required;
- Pest control; and
- External consultants fees and expenses.

#### ***Part 2 – maintenance to clear fell (years 2 – 25)***

Establishment work in years 2 to 4 as follows:

##### *Year 2*

- Supply and replanting of seedlings where required;
- Treatment of re-growth;
- Post-planting weedicide treatments as required;

- Folia analysis of planted stock;
- Construction and maintenance of access road and firebreaks as required; and
- General maintenance inclusive of on going monitoring.

*Year 3* – general maintenance including monitoring; attention to regrowth, access roads and firebreaks, fertilising where required.

*Year 4* – general establishment work and maintenance, including monitoring, attention to regrowth, access roads and firebreaks.

In years 5 to 25 maintenance work involve further fertilising and general maintenance including attention to regrowth, access roads, firebreaks and selective pruning.

21. The Manager will arrange and pay for public liability insurance for the term of the Project and for insurance against damage caused by events including fire, lightning, hail, aircraft or other aerial devices and/or articles dropped there from, windstorm (including cyclone), removal of debris and snow cover until Year 10 subject to the conditions under the Insurance Policy. After Year 10 the decision to further insure against these risks will be the Grower's responsibility.

22. It is contemplated by WFL that during the year ended 30 June 2002, WFL will determine a date based on appropriate silvicultural practices ('**first determined date**') whereby a Grower's application that is accepted on or before the first determined date, will have Part 1 Services fully completed by 30 June 2002. Any Applications received after the first determined date but on or before 30 June 2002 will be accepted on 1 July 2002.

23. It is contemplated by WFL that during the year ended 30 June 2003, WFL will also determine a date based on appropriate silvicultural practices ('**second determined date**') whereby Part 1 Services under the Forestry Management Agreement will commence to be provided and fully completed in the year ending 30 June 2003, where a Grower's application is accepted between 1 July 2002 and on or before the second determined date.

## **Harvesting and Marketing**

24. Harvesting of the trees and marketing of timber are the Grower's decision. The Grower may engage the Manager to arrange for these services to be carried out at the appropriate time or make other arrangements to harvest and market the timber. The Manager's fees and expenses for doing so will be 1% of Gross Timber Proceeds. Harvesting is anticipated to be undertaken in years 13 (1<sup>st</sup> thinning), 18 (2<sup>nd</sup> thinning) and 25 (Clear fell).

25. The Manager has entered into a Wood Purchase Agreement with Austral Softwoods Bombala Pty Ltd ('Austral') for the purchase of both sawlogs and pulp marketed or sold through the Manager from plantings made by it on behalf of Growers pursuant to the 2002 prospectus. The Wood Purchase Agreement allows for Austral to have first rights to the supply of sawlogs and pulp from harvesting (when marketed by the Manager) at a price to be set once notification of timber volumes is provided to Austral in accordance with the Wood Purchase Agreement. If such a price is below other independently sourced prices, Austral can match that price or the Manager (as agent for those Growers who appoint the Manager to market their timber) will be free to deal with any other suitable purchaser at the higher price.

26. Proceeds received by the Manager are to be distributed firstly to the Manager to cover any outstanding annual fees and to reimburse the company for any out of pocket expenses, the remainder is to be distributed to the Growers.

### **Constitution**

27. The Constitution sets out the terms and conditions under which WFL agrees to act for the Growers and to manage the Project. Within 30 days of lodgement of an Application, WFL is required to advise whether the Application has been accepted or rejected. Where the application is accepted, the Manager has two months to place the Grower on the register and provide the Grower with a copy of the Forestry Management Agreement and Lease Agreement. At the conclusion of the Project the Manager has 180 days to sell all of the assets and pass on the net proceeds, after covering costs, to the Growers. Growers are bound by the Constitution by virtue of their acceptance into the Project.

### **Project Fees**

28. The total fee for Part 1 services under the Forestry Management Agreement is \$3,850 per Woodlot and this fee is payable according to the following payment options.

- Cash - \$3,850 payable on application;
- 1 year term – deposit of \$350 payable on application with balance of \$3,500 payable in 12 equal monthly instalments of \$291.67 interest free;
- 2 year term – deposit of \$350 payable on application with balance of \$3,500 payable in 24 equal monthly instalments of \$159.90 inclusive of interest at 9%; or

- 5 year term – deposit of \$700 payable on application with balance of \$3,150 payable in 60 equal monthly instalments of \$65.39 inclusive of interest at 9%.

29. Payments for one, two or five year term monthly instalments will commence on 30 June 2002 or the last business day of the second month after the application is accepted whichever is the later. The last instalment will be adjusted to include any amount of the balance outstanding as at the due date of the last instalment. The monthly instalments can be paid by direct debit from the Grower's credit card account or other nominated account.

30. For Part 2 services, a maintenance fee of 7% of the Gross Timber Proceeds is required to be paid by each Grower as and when timber is thinned or clear felled and sold.

31. Under the Lease Agreement, lease rentals of 2% of the Gross Timber Proceeds are required to be paid by Growers pursuant to the lease agreement as and when timber is thinned or clear felled and sold.

## **2002 Application Form ('Application') and Terms Agreement**

32. Upon signing the Application, a Grower acknowledges that the full fee of any application monies is immediately due and payable. However, a Grower can apply to have the application money paid by instalments. Payment options available are one, two or five year terms and are as set-out in section 2 of the Application and shown in paragraph 28 above.

33. A Grower who elects to pay the application monies on terms is required to execute the Terms Agreement.

34. Under the Terms Agreement, a Grower declares that the terms for payment of Monies Owing have been extended pursuant to the Application and that this agreement is supplementary to the Application. The Terms Agreement details the terms of payments due under the Application. Monies Owing will be the balance of the Part 1 fee, interest and all other Monies actually or contingently owing under the Application.

35. The Terms Agreement contemplates that payment on terms will be on a full recourse basis in that if a Grower defaults, WFL will pursue the Monies Owing to the full extent permitted by law. WFL has stated that WFL will not release Growers from any liability or commitment to honour their obligations under any of the agreements.

36. Application monies paid on application will be deposited into a trust account known as the Willmott Forests Limited Project – Application Account and will only be released and paid to WFL once the Application is accepted.

**Finance**

37. Growers who do not pay the fees for Part 1 services under the Forestry Management Agreement by instalment (see paragraph 28 above) can fund their investment in the Project themselves, or borrow from an independent lender.

38. This Ruling does not apply if the finance arrangement entered into by the Grower includes or has any of the following features:

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL or the funding arrangements transform the Project into a 'scheme' to which Part IVA may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project are involved or become involved in the provision of finance to Growers for the Project.

**Ruling**

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**Application of this Ruling**

39. This Ruling applies to Growers who are accepted to participate in the Project on or before the first determined date and who have executed a Forestry Management Agreement, a Lease Agreement and if applicable, a Terms Agreement on or before the first determined date.

40. This Ruling also applies to Growers who are accepted to participate in the Project between 1 July 2002 and on or before the

second determined date and who have executed a Forestry Management Agreement, a Lease Agreement and if applicable, a Terms Agreement between 1 July 2002 and on or before the second determined date.

41. The Grower's participation in the Project must constitute the carrying on of a business of primary production.

42. A Grower is not eligible to claim any tax deductions until the Grower's application to enter the Project is accepted and the Project has commenced.

## **The Simplified Tax System ('STS') - Division 328**

43. For a Grower participating in the Project, the recognition of income and the timing of tax deductions is different depending on whether the Grower is an 'STS taxpayer'. To be an 'STS taxpayer' a Grower:

- must be eligible to be an 'STS taxpayer'; and
- must have elected to be an 'STS taxpayer'.

## **Qualification**

44. This Product Ruling assumes that a Grower who is an 'STS taxpayer' is so for the income year in which their participation in the Project commences. A Grower may become an 'STS taxpayer' at a later point in time. Also, a Grower who is an 'STS taxpayer' may choose to stop being an 'STS taxpayer', or may cease to be eligible to be an 'STS taxpayer', during the term of the Project. These are contingencies relating to the circumstances of individual Growers that cannot be accommodated in this Ruling. Such Growers can ask for a private ruling on how the taxation legislation applies to them.

## **Tax outcomes for Growers who are not 'STS taxpayers'**

### **Assessable Income - Section 6-5**

45. That part of the Gross Timber Proceeds from the Project attributable to the Grower's produce, less any GST payable on those proceeds (section 17-5), will be assessable income of the Grower under section 6-5.

46. The Grower recognises ordinary income from carrying on the business of afforestation at the time that income is derived.

**Section 8-1: Deduction for Management fee and interest on terms payment**

47. A Grower who is not an 'STS taxpayer' and who is accepted into the Project on or before the first determined date may claim tax deductions for the following revenue expenses.

<b>Fee Type</b>	<b>ITAA 1997 Section</b>	<b>Year 1 30/6/2002</b>	<b>Year 2 30/6/2003</b>	<b>Year 3 30/6/2004</b>
Management fee	8-1	\$3,850 – see Note (i)	nil	nil
Interest on terms payment	8-1	As incurred – see Note (ii) below	As incurred – see Note (ii) below	As incurred – see Note (ii) below

**Notes:**

- (i) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (e.g. input tax credits): Division 27. See example at paragraph 121;
- (ii) Growers should read the discussion of the prepayment rules in paragraphs 91 to 104 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant agreement or is at the Grower's choice.

48. A Grower who is not an 'STS taxpayer' and who is accepted into the Project between 1 July 2002 and on or before the second determined date may claim tax deductions for the following revenue expenses.

<b>Fee Type</b>	<b>ITAA 1997 Section</b>	<b>Year 1 30/6/2002</b>	<b>Year 2 30/6/2003</b>	<b>Year 3 30/6/2004</b>
Management fee	8-1	nil	\$3,850 – see Notes (iii) & (iv)	nil
Interest on terms payment	8-1	nil	As incurred – see Note (v) below	As incurred – see Note (v) below

**Notes:**

- (iii) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be

adjusted as relevant for GST (e.g. input tax credits):  
Division 27. See example at paragraph 121;

- (iv) The Management fee shown in the Forestry Management Agreement is deductible in full in the year that they are incurred. However, if a Grower chooses to prepay fees for the doing of a thing (e.g., the provision of management services or the leasing of land) that will not be wholly done in the income year the fees are incurred, the prepayment rules of the ITAA 1936 may apply to apportion those fees. In such cases, the tax deduction for the prepaid fee must be determined using the formula shown in paragraph 97 unless the expenditure is 'excluded expenditure'. 'Excluded expenditure' is an 'exception' to the prepayment rules and is deductible in full in the year in which it is incurred. For the purpose of this Ruling 'excluded expenditure' refers to an amount of expenditure of less than \$1,000;
- (v) Growers should read the discussion of the prepayment rules in paragraphs 91 to 104 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant agreement or is at the Grower's choice.

## **Section 8-1: Deductibility of interest on loans**

49. The deductibility or otherwise of interest arising from any loan agreements entered into by a Grower is outside the scope of this Ruling. However Growers should read the discussion of the prepayment rules in paragraphs 89 to 104 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant loan agreement or is at the Grower's choice.

## **Tax outcomes for Growers who are 'STS taxpayers'**

### **Assessable Income - Section 6-5**

50. That part of the Gross Timber Proceeds from the Project attributable to the Grower's produce, less any GST payable on those proceeds (section 17-5), will be assessable income of the Grower under section 6-5.

51. The Grower recognises ordinary income from carrying on the business of afforestation at the time the income is received (paragraph 328-105(1)(a)).

### **Section 8-1 and section 328-105**

52. A Grower who is an 'STS taxpayer' and who is accepted into the Project on or before the first determined date may claim tax deductions for the following revenue expenses.

<b>Fee Type</b>	<b>ITAA 1997 Section</b>	<b>Year 1 30/6/2002</b>	<b>Year 2 30/6/2003</b>	<b>Year 3 30/6/2004</b>
Management fee	8-1 & 328-105	See Notes (vi) &(vii) below		
Interest on terms payment	8-1 & 328-105	As incurred and paid – see Note (viii) below	As incurred and paid – see Note (viii) below	As incurred and paid – see Note (viii) below

### **Notes:**

- (vi) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (e.g., input tax credits): Division 27. See example at paragraph 121;
- (vii) If a Grower who is an 'STS taxpayer' chooses to pay the Management fee by the cash option, the Management fee of \$3,850 will be fully paid in the year in which it is incurred. Therefore, the Management fee of \$3,850 is deductible in full when it is incurred;  
  
If a Grower who is an 'STS taxpayer' chooses to pay the Management fee by the terms option, then the Management fee of \$3,850 will not be fully paid in the year in which it is incurred. The Management fee is only deductible to the extent to which it has been paid, or has been paid for the Grower. Any amount or part of an amount of the Management fee which is not paid in the year in which it is incurred, will be deductible in the year in which it is actually paid;
- (viii) Growers should read the discussion of the prepayment rules in paragraphs 91 to 104 (below) as those rules may be applicable if interest is prepaid. Subject to the

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‘excluded expenditure’ exception, the prepayment rules apply whether the prepayment is required under the relevant agreement or is at the Grower’s choice.

53. A Grower who is an ‘STS taxpayer’ and who is accepted into the Project between 1 July 2002 and on or before the second determined date may claim tax deductions for the following revenue expenses:

<b>Fee Type</b>	<b>ITAA 1997 Section</b>	<b>Year 1 30/6/2002</b>	<b>Year 2 30/6/2003</b>	<b>Year 3 30/6/2004</b>
Management fee	8-1 & 328-105	nil	See Notes (ix) & (x) below	
Interest on terms payment	8-1 & 328-105	nil	As incurred and paid – see Note (xi) below	As incurred and paid – see Note (xi) below

**Notes:**

- (ix) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (e.g., input tax credits): Division 27. See example at paragraph 121;
- (x) If a Grower who is an ‘STS taxpayer’ chooses to pay the Management fee by the cash option, the Management fee of \$3,850 will be fully paid in the year in which it is incurred. Therefore, the Management fee of \$3,850 is deductible in full when it is incurred;  
  
If a Grower who is an ‘STS taxpayer’ chooses to pay the Management fee by the terms option, then the Management fee of \$3,850 will not be fully paid in the year in which it is incurred. The Management fee is only deductible to the extent to which it has been paid, or has been paid for the Grower. Any amount or part of an amount of the Management fee which is not paid in the year in which it is incurred, will be deductible in the year in which it is actually paid;
- (xi) Growers should read the discussion of the prepayment rules in paragraphs 91 to 104 (below) as those rules may be applicable if interest is prepaid. Subject to the ‘excluded expenditure’ exception, the prepayment rules apply whether the prepayment is required under the relevant agreement or is at the Grower’s choice.

**Section 8-1: Deductibility of interest on loans**

54. The deductibility or otherwise of interest arising from any loan agreements entered into by a Grower is outside the scope of this Ruling. However Growers should read the discussion of the prepayment rules in paragraphs 89 to 104 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant loan agreement or is at the Grower's choice.

**Tax outcomes that apply to all Growers****Division 35 – Deferral of losses from non-commercial business activities****Section 35-55 – Commissioner's discretion**

55. For a Grower who is an individual and who enters the Project during the year ended 30 June 2002 the rule in section 35-10 may apply to the business activity comprised by their involvement in this Project. Under paragraph 35-55(1)(b) the Commissioner will decide for the income years ending 30 June 2002 to 30 June 2014 that the rule in section 35-10 does not apply to this activity provided that the Project is carried out in the manner described in this Ruling.

56. For a Grower who is an individual and who enters the Project during the year ended 30 June 2003 the rule in section 35-10 may apply to the business activity comprised by their involvement in this Project. Under paragraph 35-55(1)(b) the Commissioner will decide for the income years ending 30 June 2003 to 30 June 2015 that the rule in section 35-10 does not apply to this activity provided that the Project is carried out in the manner described in this Ruling.

57. This exercise of the discretion in subsection 35-55(1) will not be required where, for any year in question:

- a Grower's business activity satisfies one of the objective tests in sections 35-30, 35-35, 35-40 or 35-45; or
- the 'Exception' in subsection 35-10(4) applies (see paragraph 108 in the Explanations part of this ruling, below).

58. Where either the Grower's business activity satisfies one of the objective tests, the discretion in subsection 35-55(1) is exercised, or the Exception in subsection 35-10(4) applies, section 35-10 will not apply. This means that a Grower will not be required to defer any

excess of deductions attributable to their business activity in excess of any assessable income from that activity, i.e., any 'loss' from that activity, to a later year. Instead, this 'loss' can be offset against other assessable income for the year in which it arises.

59. Growers are reminded of the important statement made on Page 1 of this Product Ruling. Therefore, Growers should not see the Commissioner's decision to exercise the discretion in paragraph 35-55(1)(b) as an indication that the Tax Office sanctions or guarantees the Project or the product to be commercially viable. An assessment of the Project or the product from this perspective has not been made.

## **Sections 82KZME – 82KZMF, 82KL, and Part IVA**

60. For a Grower who participates in the Project and incurs expenditure as required by the Forestry Management Agreement the following provisions of the ITAA 1936 have application as indicated:

- expenditure by a Grower does not fall within the scope of sections 82KZME-82KZMF (but see paragraphs 91 to 104);
- section 82KL does not apply to deny the deductions otherwise allowable; and
- the relevant provisions in Part IVA will not be applied to cancel a tax benefit obtained under a tax law dealt with in this Ruling.

## **Explanations**

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### **Is the Grower carrying on a business?**

61. For the amounts set out in paragraph 28 above to constitute allowable deductions the Grower's afforestation activities as a participant in the Willmott Forests Project - 2002 Prospectus must amount to the carrying on of a business of primary production.

62. Where there is a business, or a future business, the Gross Timber Proceeds from the sale of the wood produce from the Woodlots comprising the Project will constitute gross assessable income in their own right. The generation of 'business income' from such a business, or future business, provides the backdrop against which to judge whether the outgoings in question have the requisite connection with the operations that more directly gain or produce this income.

63. For schemes such as that of the Willmott Forests Project - 2002 Prospectus, Taxation Ruling TR 2000/8 sets out in paragraph 89 the circumstances in which the Grower's activities can constitute the carrying on of a business. As Taxation Ruling TR 2000/8 sets out, these circumstances have been established in court decisions such as *FCT v. Lau* 84 ATC 4929.

64. Generally, a Grower will be carrying on a business of afforestation, and hence primary production, if:

- the Grower has an identifiable interest (by lease or by licence) in the land on which the Grower's trees are established;
- the Grower has a right to harvest and sell the wood produce from those trees;
- the afforestation activities are carried out on the Grower's behalf;
- the afforestation activities of the Grower are typical of those associated with a afforestation business; and
- the weight and influence of general indicators point to the carrying on of a business.

65. In this Project, each Grower enters into a Forestry Management Agreement and a Lease Agreement.

66. Under the Lease Agreement, each individual Grower will have rights over a specific and identifiable area of land. The Lease Agreement provides the Grower with an ongoing interest in the specific trees on the leased area for the term of the Project. Under the Lease, the Grower must use the land in question for the purpose of carrying out afforestation activities, and for no other purpose. The Lease allows the Manager to come onto the land to carry out its obligations under the Forestry Management Agreement.

67. Under the Forestry Management Agreement the Manager is engaged by the Grower to establish and maintain a Woodlot on the Grower's identifiable area of land during the term of the Project. The Manager has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the Woodlot on the Grower's behalf.

68. The Manager can also be engaged to harvest and sell, on the Grower's behalf, the wood produce grown on the Grower's Woodlot.

69. The general indicators of a business, as used by the Courts, are described in Taxation Ruling TR 97/11. Positive findings can be made from the Project's description for all the indicators.

70. The activities that will be regularly carried out during the term of the Project demonstrate a significant commercial purpose. Based

on reasonable projections, a Grower in the Project will derive assessable income from the sale of the wood produce that will return a before-tax profit, i.e., a profit in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

71. The pooling of wood produce from trees grown on the Grower's Woodlot with the wood produce of other Growers is consistent with general afforestation practices. Each Grower's proportionate share of the sale proceeds of the pooled wood products will reflect the proportion of the trees contributed from their Woodlot.

72. The Manager's services are also consistent with general silvicultural practices. They are of the type ordinarily found in afforestation ventures that would commonly be said to be businesses. While the size of a Woodlot is relatively small, it is of a size and scale to allow it to be commercially viable (see Taxation Ruling IT 360).

73. The Grower's degree of control over the Manager as evidenced by the Forestry Management Agreement, and supplemented by the Corporations Act, is sufficient. During the term of the Project, the Manager will provide the Grower with regular progress reports on the Grower's Woodlot and the activities carried out on the Grower's behalf. Growers are able to terminate arrangements with the Manager in certain instances, such as cases of default or neglect.

74. The afforestation activities, and hence the fees associated with their procurement, are consistent with an intention to commence regular activities that have an 'air of permanence' about them. For the purposes of this Ruling, the Grower's afforestation activities in the Willmott Forests Project - 2002 Prospectus will constitute the carrying on of a business.

### **The Simplified Tax System - Division 328**

75. Subdivision 328-F sets out the eligibility requirements that a Grower must satisfy in order to enter the STS and Subdivision 328-G sets out the rules for entering and leaving the STS.

76. The question of whether a Grower is eligible to be an 'STS taxpayer' is outside the scope of this Product Ruling. Therefore, any Grower who relies on those parts of this Ruling that refer to the STS will be assumed to have correctly determined whether or not they are eligible to be an 'STS taxpayer'.

### **Section 8-1: Deductibility of the initial management fee**

77. Consideration of whether the initial management fee is deductible under section 8-1 begins with the first limb of the section. This view proceeds on the following basis:

- the outgoing in question must have a sufficient connection with the operations or activities that directly gain or produce the taxpayer's assessable income;
- the outgoings are not deductible under the second limb if they are incurred when the business has not commenced; and
- where all that happens in a year of income is that a taxpayer is contractually committed to a venture that may not turn out to be a business, there can be doubt about whether the relevant business has commenced, and hence, whether the second limb applies. However, that does not preclude the application of the first limb in determining whether the outgoing in question has a sufficient connection with activities to produce assessable income.

78. The management fee associated with the afforestation activities will relate to the gaining of income from the Grower's business of afforestation (see above), and hence have a sufficient connection to the operations by which income (from the harvesting and sale of wood produce) is to be gained from this business. It will thus be deductible under the first limb of section 8-1. Further, no 'non-income producing' purpose in incurring the fee is identifiable from the arrangement. The fee appears to be reasonable. There is no capital component of the management fee. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

*Possible application of prepayment provisions*

79. Under the Forestry Management Agreement the management fee is not for things to be done beyond 30 June in the year in which the relevant amounts are incurred. In these circumstances, the prepayment provisions in sections 82KZME and 82KZMF have no application to these fees.

80. However, where a Grower **chooses** to prepay these fees for a period beyond the income year in which the expenditure is incurred, the prepayment provisions (see paragraphs 91 to 104) will apply to determine the amount and timing of the deductions regardless of whether the Grower is an 'STS taxpayer' or not. These provisions apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes 'STS taxpayers' from the operation of section 82KZMF. This is subject to the 'excluded expenditure' exception. For the purpose of this Ruling 'excluded expenditure' refers to an amount of expenditure of less than \$1,000.

## *Timing of deductions*

81. In the absence of any application of the prepayment provisions, the timing of deduction for the management fee will depend upon whether a Grower is an 'STS taxpayer' or is not an 'STS taxpayer'.
82. If the Grower is not an 'STS taxpayer', the management fee is deductible in the year in which it is incurred.
83. If the Grower is an 'STS taxpayer' the management fee is deductible in the income year in which it is paid, or is paid for the Grower (paragraph 328-105(1)(b)). If any amount that is properly incurred in an income year remains unpaid at the end of that income year, the unpaid amount is deductible in the income year in which it is actually paid or is paid for the Grower.

## **Section 8-1: Deductibility of interest on terms payment**

84. Some Growers may choose to pay the management fee through one of the terms options. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of management fee.
85. The interest incurred for the year ended 30 June 2002 and in subsequent years of income will be in respect of the management fee being paid in instalments. Such interest will have a sufficient connection with the gaining of assessable income to be deductible under section 8-1.
86. As with the management fee, in the absence of any application of the prepayment provisions (see paragraphs 91 to 104), the timing of deductions for interest will again depend upon whether a Grower is an 'STS taxpayer' or is not an 'STS taxpayer'.
87. If the Grower is not an 'STS taxpayer', interest is deductible in the year in which it is incurred.
88. If the Grower is an 'STS taxpayer' interest is not deductible until it has been both incurred and paid, or is paid for the Grower. If interest that is properly incurred in an income year remains unpaid at the end of that income year, the unpaid amount is deductible in the income year in which it is actually paid, or is paid for the Grower.

## **Section 8-1: Deductibility of interest on loans**

89. The deductibility of interest incurred by Growers who finance their participation in the Project through a loan facility with a bank or other financier is outside the scope of this Ruling. Product Rulings

only deal with arrangements where all details and documentation have been provided to, and examined by the Tax Office.

90. While the terms of any finance agreement entered into between relevant Growers and such financiers are subject to commercial negotiation, those agreements may require interest to be prepaid. Alternatively, a Grower may choose to prepay such interest. Unless such prepaid interest is ‘excluded expenditure’ any tax deduction that is allowable will be subject to the prepayment provisions of the ITAA 1936 (see paragraphs 91 to 104).

### **Prepayment provisions - sections 82KZL to 82KZMF**

91. The prepayment provisions contained in Subdivision H of Division 3 of Part III of the ITAA 1936 affect the timing of deductions for certain prepaid expenditure. These provisions apply to certain expenditure incurred under an agreement in return for the doing of a thing under the agreement (e.g., the performance of management services or the leasing of land) that will not be wholly done within the same year of income as the year in which the expenditure is incurred. If expenditure is incurred to cover the provision of services to be provided within the same year, then it is not expenditure to which the prepayment rules apply.

92. For this Project only section 82KZL (an interpretive provision) and sections 82KZME and 82KZMF are relevant. Where the requirements of sections 82KZME and 82KZMF are met, taxpayers determine deductions for prepaid expenditure under section 82KZMF using the formula in subsection 82KZMF(1). These provisions also apply to ‘STS taxpayers’ because there is no specific exclusion contained in section 82KZME that excludes ‘STS taxpayers’ from the operation of section 82KZMF.

#### *Sections 82KZME and 82KZMF*

93. Where the requirements of subsections 82KZME(2) and (3) are met, the formula in subsection 82KZMF(1) (see below) will apply to apportion expenditure that is otherwise deductible under section 8-1 of the ITAA 1997. The requirements of subsection 82KZME(2) will be met if expenditure is incurred by a taxpayer in return for the doing of a thing that is not to be wholly done within the year the expenditure is made. The year in which such expenditure is incurred is called the ‘expenditure year’ (subsection 82KZME(1)).

94. The requirements of subsection 82KZME(3) will be met where the agreement (or arrangement) has the following characteristics:

- the taxpayer’s allowable deductions under the agreement for the ‘expenditure year’ exceed any

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assessable income attributable to the agreement for that year; and

- the taxpayer does not have effective day to day control over the operation of the agreement. That is, the significant aspects of the arrangement are managed by someone other than the taxpayer; and
- either:
  - a) there is more than one participant in the agreement in the same capacity as the taxpayer; or
  - b) the person who promotes, arranges or manages the agreement (or an associate of that person) promotes similar agreements for other taxpayers.

95. For the purpose of these provisions, the agreement includes all activities that relate to the agreement (subsection 82KZME(4)). This has particular relevance for a Grower in this Project who, in order to participate in the Project may borrow funds from a financier. Although undertaken with an unrelated party, that financing would be an element of the arrangement. The funds borrowed and the interest deduction are directly related to the activities under the arrangement. If a Grower prepays interest under such financing arrangements, the deductions allowable will be subject to apportionment under section 82KZMF.

96. There are a number of exceptions to these rules, but for Growers participating in this Project, only the 'excluded expenditure' exception in subsection 82KZME(7) is relevant. 'Excluded expenditure' is defined in subsection 82KZL(1). However, for the purposes of Growers in this Project, 'excluded expenditure' is prepaid expenditure incurred under the arrangement that is less than \$1,000. Such expenditure is immediately deductible.

97. Where the requirements of section 82KZME are met, section 82KZMF applies to apportion relevant prepaid expenditure. Section 82KZMF uses the formula below, to apportion prepaid expenditure and allow a deduction over the period that the benefits are provided.

$$\text{Expenditure} \times \frac{\text{Number of days of eligible service}}{\text{Total number of days of eligible service period}}$$

98. In the formula 'eligible service period' (defined in subsection 82KZL(1)) means, the period during which the thing under the agreement is to be done. The eligible service period begins on the day on which the thing under the agreement commences to be done or on the day on which the expenditure is incurred, whichever is the later,

and ends on the last day on which the thing under the agreement ceases to be done, up to a maximum of 10 years.

*Application of the prepayment provisions to this Project*

99. In this Project:

- for subscribers to the Project on or before the first determined date, an initial fee for plantation, preparation & establishment of \$3,850 per Woodlot; and
- for subscribers after 30 June 2002 but on or before the second determined date, an initial fee for plantation, preparation & establishment of \$3,850,

will be incurred on execution of the Forestry Management Agreement. The fee for plantation, preparation & establishment is charged for providing management services to a Grower by 30 June of the year of execution of the Agreements.

100. The fee for plantation, preparation & establishment is expressly stated to be for a number of specified services. No explicit conclusion can be drawn from the description of the arrangement that the initial fee for plantation, preparation & establishment has been inflated to result in reduced fees being payable for management fees in subsequent years.

101. There is also no evidence that might suggest the management services covered by the fee could not be provided within the relevant expenditure year. Thus, for the purposes of this Ruling, it can be accepted that no part of the initial fee for plantation, preparation & establishment, is for the Manager doing 'things' that are not to be wholly done within the expenditure year. Under the Terms Agreement to be executed between Growers and WFL interest is payable monthly in arrears.

102. On this basis, provided a Grower incurs expenditure as required under the Project agreements, as set out in paragraph 28, then the basic precondition in subsection 82KZME(2) is not satisfied and, in these circumstances, section 82KZMF will have no application.

*Growers who **choose** to pay fees for a period in excess of that required by the Project's agreements*

103. Although not required under either the Forestry Management Agreement or the Terms Agreement, a Grower participating in the Project may **choose** to prepay fees/interest for a period beyond the 'expenditure year'. Similarly, Growers who borrow funds may either choose, or be required to prepay interest. Where this occurs, contrary

to the conclusion reached in paragraph 102 above, section 82KZMF will apply to apportion the expenditure and allow a deduction over the period in which the prepaid benefits are provided.

104. For these Growers, the amount and timing of deductions for any relevant prepaid management fee or prepaid interest will depend upon when the respective amounts are incurred and what the 'eligible service period' is in relation to these amounts.

## **Division 35 - Deferral of Losses from non-commercial business activities**

105. Under the rule in subsection 35-10(2) a deduction for a loss incurred by an individual from certain business activities will not be allowable in an income year unless:

- the 'Exception' in subsection 35-10(4) applies;
- one of four objective tests in sections 35-30, 35-35, 35-40 or 35-45 is met; or
- if one of the objective tests is not satisfied, the Commissioner exercises the discretion in section 35-55.

106. Generally, a loss in this context is, for the income year in question, the excess of an individual taxpayer's allowable deductions attributable to the business activity over that taxpayer's assessable income from the business activity.

107. Under the loss deferral rule in subsection 35-10(2) the relevant loss is not able to be taken into account in the calculation of taxable income in the year that loss arose. Instead, in a later year it may be offset against any income from the same or similar business activity, or, if one of the objective tests is passed, or the Commissioner's discretion exercised, against other income.

108. For the purposes of applying the objective tests, subsection 35-10(3) allows taxpayers to group business activities 'of a similar kind'. Under subsection 35-10(4), there is an 'exception' to the general rule in subsection 35-10(2) where the loss is from a primary production business activity and the individual taxpayer has other assessable income for the income year from sources not related to that activity, of less than \$40,000 (excluding any net capital gain). As both subsections relate to the individual circumstances of Growers who participate in the Project they are beyond the scope of this Product Ruling and are not considered further.

109. In broad terms, the objective tests require:

- at least \$20,000 of assessable income in that year from the business activity (section 35-30);

- the business activity results in a taxation profit in 3 of the past 5 income years (including the current year) (section 35-35);
- at least \$500,000 of real property is used on a continuing basis in carrying on the business activity in that year (section 35-40); or
- at least \$100,000 of certain other assets are used on a continuing basis in carrying on the business activity in that year (section 35-45).

110. A Grower who participates in the Project will be carrying on a business activity that is subject to these provisions. Information provided with the application for this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot in the Project is unlikely to pass one of the objective tests until the income year ended 30 June 2027, for a Grower who enters the Project during the year ended 30 June 2002, or until the income year ended 30 June 2028, for a Grower who enters the Project during the year ended 30 June 2003. Growers who acquire more than one interest in the Project may however, find that their activity meets one of the tests in an earlier income year.

111. Therefore, prior to these respective times, unless the Commissioner exercises an arm of the discretion under paragraphs 35-55(1)(a) or (b), the rule in subsection 35-10(2) will apply to defer to a future income year any loss that arises from the Grower's participation in the Project.

112. The first arm of the discretion in paragraph 35-55(1)(a) relates to 'special circumstances' applicable to the business activity, and has no relevance for the purposes of this Product Ruling. However, the second arm of the discretion in paragraph 35-55(1)(b) may be exercised by the Commissioner where:

- (i) the business activity has started to be carried on;
- (ii) because of its nature, it has not satisfied one of the objective tests; and
- (iii) there is an objective expectation that the business activity of an individual taxpayer will either pass one of the objective tests or produce a taxation profit within a period that is commercially viable for the industry concerned.

113. For a Grower who is an individual and who enters the Project during the year ended 30 June 2002, information provided with this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot in the Project is expected to be carrying on a business activity that will produce a taxation profit for the year

ended 30 June 2015. The Commissioner will decide for such a Grower that it would be reasonable to exercise the second arm of the discretion until the year ended 30 June 2014. Subsection 35-55(2) prevents the Commissioner exercising the discretion beyond this year.

114. For a Grower who is an individual and who enters the Project during the year ended 30 June 2003 information provided with this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot in the Project is expected to be carrying on a business activity that will produce a taxation profit for the year ended 30 June 2016. The Commissioner will decide for such a Grower that it would be reasonable to exercise the second arm of the discretion until the year ended 30 June 2015. Subsection 35-55(2) prevents the Commissioner exercising the discretion beyond this year.

115. This Product Ruling is issued on a prospective basis (ie, before an individual Grower's business activity starts to be carried on). The Project, however, may fail to be carried on during the income years specified above (see paragraphs 55 and 56), in the manner described in the Arrangement (see paragraphs 14 to 38). If so, this Ruling, and specifically the decision in relation to paragraph 35-55(1)(b), that it would be unreasonable that the loss deferral rule in subsection 35-10(2) not apply, may be affected, because the Ruling no longer applies (see paragraph 9). Growers may need to apply for private rulings on how paragraph 35-55(1)(b) will apply in such changed circumstances.

116. In deciding that the second arm of the discretion in paragraph 35-55(1)(b) will be exercised on this conditional basis, the Commissioner has relied upon:

- the report of the independent forester;
- the independent market report; and
- independent, objective, and generally available information relating to the afforestation industry.

## **Section 82KL – recouped expenditure**

117. The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefits(s)'. Insufficient 'additional benefits' will be provided to trigger the application of section 82KL. It will not apply to deny the deduction otherwise allowable under section 8-1.

**Part IVA – general anti-avoidance provisions**

118. For Part IVA to apply there must be a ‘scheme’ (section 177A), a ‘tax benefit’ (section 177C) and a dominant purpose of entering into the scheme to obtain a tax benefit (section 177D).

119. The Willmott Forests Project - 2002 Prospectus will be a ‘scheme’. A Grower will obtain a ‘tax benefit’ from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 47, 48, 52 and 53, that would not have been obtained but for the scheme. However, it is not possible to conclude the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

120. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the wood produce. There are no facts that would suggest that Growers have the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There is no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing at arm’s length or, if any parties are not dealing at arm’s length, that any adverse tax consequences result. Further, having regard to the factors to be considered under paragraph 177D(b) it cannot be concluded, on the information available, that participants will enter into the scheme for the dominant purpose of obtaining a tax benefit.

**Example****Example – Entitlement to GST input tax credits**

121. Susan, who is a sole trader and registered for GST, contracts with a manager to manage her viticulture business. Her manager is registered for GST and charges her a management fee payable every six months in advance. On 1 December 2001 Susan receives a valid tax invoice from her manager requesting payment of a management fee in advance, and also requesting payment for an improvement in the connection of electricity for her vineyard that she contracted him to carry out. The tax invoice includes the following details:

**Management fee for period 1/1/2002 to 30/6/2002 \$4 400\***

Carrying out of upgrade of power for your vineyard as quoted	<u>\$2 200*</u>
Total due and payable by 1 January 2002 (includes GST of \$600)	<u>\$6 600</u>

\*Taxable supply

Susan pays the invoice by the due date and calculates her input tax credit on the management fee (to be claimed through her Business Activity Statement) as:

$$1/11 \times \$4400 = \$400.$$

Hence her outgoing for the management fee is effectively \$4400 *less* \$400, or \$4000.

Similarly, Susan calculates her input tax credit on the connection of electricity as:

$$1/11 \times \$2200 = \$200.$$

Hence her outgoing for the power upgrade is effectively \$2200 *less* \$200, or \$2000.

In preparing her income tax return for the year ended 30 June 2002, Susan is aware that the management fee is deductible in the year incurred. She calculates her management fee deduction as \$4000 (not \$4400).

Susan is aware that the electricity upgrade is deductible 10% per year over a 10 year period. She calculates her deduction for the power upgrade as \$200 (one tenth of \$2000 only, not one tenth of \$2200).

## **Detailed contents list**

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**Commissioner of Taxation**

14 November 2001

<i>Previous draft:</i>	- ITAA 1936 82KZMF
Not previously issued in draft form	- ITAA 1936 82KZMF(1)
	- ITAA 1936 Pt IVA
<i>Related Rulings/Determinations:</i>	- ITAA 1936 177A
TR 92/1; TR 92/20; TD 93/34;	- ITAA 1936 177C
TR 97/11; TR 97/16; TR 98/22;	- ITAA 1936 177D
TR 2000/8; PR 1999/95; IT 360	- ITAA 1936 177D(b)
	- ITAA 1997 6-5
<i>Subject references:</i>	- ITAA 1997 8-1
- carrying on a business	- ITAA 1997 17-5
- commencement of business	- ITAA 1997 Div 27
- fee expenses	- ITAA 1997 Div 35
- interest expenses	- ITAA 1997 35-10
- management fee expenses	- ITAA 1997 35-10(2)
- producing assessable income	- ITAA 1997 35-10(3)
- product rulings	- ITAA 1997 35-10(4)
- public rulings	- ITAA 1997 35-30
- schemes and shams	- ITAA 1997 35-35
- taxation administration	- ITAA 1997 35-40
- tax avoidance	- ITAA 1997 35-45
	- ITAA 1997 35-55
	- ITAA 1997 35-55(1)
<i>Legislative references:</i>	- ITAA 1997 35-55(1)(a)
- TAA 1953 Part IVAAA	- ITAA 1997 35-55(1)(b)
- ITAA 1936 Div 3 of Part III	- ITAA 1997 35-55(2)
- ITAA 1936 82KL	- ITAA 1997 Div 328
- ITAA 1936 82KL(1)	- ITAA 1997 Subdiv 328-F
- ITAA 1936 82KZL	- ITAA 1997 Subdiv 328-G
- ITAA 1936 82KZL(1)	- ITAA 1997 328-105
- ITAA 1936 82KZME	- ITAA 1997 328-105(1)(a)
- ITAA 1936 82KZME(1)	- ITAA 1997 328-105(1)(b)
- ITAA 1936 82KZME(2)	
- ITAA 1936 82KZME(3)	<i>Case references:</i>
- ITAA 1936 82KZME(4)	- FCT v. Lau 84 ATC 4929
- ITAA 1936 82KZME(7)	

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FOI status: **may be released**

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NO: T2001/013359

ISSN: 1441 1172