



# ***PR 2001/156 - Income tax: Tasmanian Forest Project 2000***

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 This document has changed over time. This is a consolidated version of the ruling which was published on *21 November 2001*



## Product Ruling

### Income tax: Tasmanian Forest Project 2000

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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.

#### **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**

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The Australian Taxation Office (ATO) **does not** sanction or guarantee this product. 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.

Participants must form their own view about the commercial and financial viability of the product. This involves 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 this product fits an existing portfolio, etc. We recommend a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for participants 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, participants lose the protection of this Product Ruling. Participants may wish to seek assurances from the promoter that the arrangement has been carried out as described in this Product Ruling.

Participants 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**

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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.

## 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 Tasmanian Forest Project 2000, or just simply as 'the Project'.

### Tax laws

2. The tax law dealt with in this Ruling is:
- Division 35 of the *Income Tax Assessment Act 1997* ('ITAA 1997').

### 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 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 those persons who were accepted into the project between 6 June 2000 and 5 June 2001. 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 as set out in the description of the arrangement. 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 the Project.

**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 Product Ruling 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 21 November 2001, for Growers who, between 6 June 2000 and 5 June 2001, entered into the specific arrangement that is set out below. 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 2002. The Ruling continues to apply, even following its withdrawal, in respect of the tax laws ruled upon, to all persons within the specified class who entered into the specified arrangement between 6 June 2000 and 5 June 2001. This is subject to there being no material difference in the arrangement or in the persons' involvement in the arrangement.

## Arrangement

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

- Application for Product Ruling dated 19 September 2001;
- **Prospectus** prepared for Ausforestry Limited A.C.N. 055 969 429 ("Ausforestry"), dated 6 June 2000;
- The **Management Agreement** to be entered into by each Grower and Ausforestry;
- The **Agreement to Lease** to be entered into by each Grower and Forest Enterprises Australia Ltd A.C.N. 009 553 548;
- The **Loan Agreement** which may be entered into by the Grower and Forest Enterprises Australia Limited A.C.N. 009 553 548, an entity associated with Ausforestry;
- The Trust Deed entered into by Tasmanian Trustees Ltd ("the Trustee") and Ausforestry.

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 the Growers entered into. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate of the Grower, was or is a party to. The effect of these agreements is summarised as follows.

**Overview**

16. This arrangement is called the “Tasmanian Forest Project 2000” and is registered as a managed investment scheme under the Corporations Law. Growers participating in the Project would have entered into a lease of land in Tasmania with Forest Enterprises Australia Ltd. The lease will conclude on clear fall of any trees planted on the relevant land.

17. The Growers would have also entered into a Management Agreement with Ausforestry for the establishment and maintenance of a plantation of Tasmanian Shining Gum (*eucalyptus nitens*) trees for the purpose of clear fell at approximately 13 years.

18. The Manager has entered into a Trust Deed with Tasmanian Trustees Ltd. The Trustee’s role is to protect the interests of Growers, by ensuring all establishment, maintenance and marketing activities by the Manager are properly conducted.

19. The minimum area of land to be leased by a Grower under the Project is three woodlots, or one hectare. There are approximately 400 trees on each woodlot (approximately 1,200 per hectare). Projected returns for Growers are outlined on page 12 of the Prospectus. The Prospectus also sets out the other assumptions underpinning those projected returns and advises that participation in the Project is a long-term venture in commercial forestry with all the attendant risks and, therefore, should be considered as speculative.

**Management Agreement**

20. Under the Management Agreement, Growers would have contracted with Ausforestry (“the Project Manager”) to establish and maintain a plantation of trees upon their leased area of land until maturity, at which time the trees will be harvested and sold on behalf of the Grower. The Project Manager was to provide the “Establishment Services” under the agreement which include:

- the establishment and maintenance of fire breaks on and around the land in accordance with good forestry practice;
- the completion of all preparatory work necessary for the planting of seedlings on the land including all ploughing and vermin control deemed necessary by the Project Manager;
- the supply and planting of healthy seedlings to an average density per hectare appropriate to the soil and climatic circumstances of the land; and

- the control of weeds and other vegetation which might inhibit the growth of the seedlings on the land.

21. The Project Manager was also to provide the “Management Services” under the agreement which include:

- the general maintenance of the plantation including control of weeds, suckers, vermin or other pests which may impede the growth of the seedlings;
- the maintenance in good condition and repair of all fire breaks and access roads in and about the Land;
- the application of fertiliser to the land in such form and in such quantities as to maintain satisfactory growth;
- the provision of a written report in relation to the progress of the plantation to the Grower annually; and
- the provision of advice and assistance to the Grower generally in relation to the thinning and pruning of the plantation and the general management thereof in accordance with the best practices of the forestry industry.

22. The Project Manager is to provide the services of harvesting and marketing the trees, which involves the Project Manager determining the appropriate time for the clear felling of trees on the land, and the marketing and selling of the trees which have been grown on the land, on behalf of the Grower.

## **Agreement to Lease**

23. Growers were to enter into an Agreement to Lease with Forest Enterprises Australia Ltd (“the Lessor”) which, upon identification and allocation of the specified area of land to the Grower, became a Lease Agreement. This Lease Agreement is for the lease of a specified area of land upon which their plantation was established.

24. Under this agreement the Grower would agree to pay to the Lessor the specified rent for the lease of the specified area of land for the term of the lease period. The term of the agreement is from the date of signing of the application by the Lessor, until the final clear fall of the trees upon the land.

## **Fees**

25. The total fees payable by a grower over the life of the project would vary depending on the subscription option selected by the grower.

26. Subscription Option 1:
- an initial subscription amount of \$1,650 per woodlot was payable upon application;
  - annual lease payments of \$65 per woodlot for the second year of the Project ending 30 June 200, and CPI adjusted for each subsequent year;
  - a maintenance fee during the year ending 30 June 2001, of \$71.50 per woodlot, and CPI adjusted for each subsequent year.
27. Subscription Option 2:
- an initial subscription amount of \$2,640 per woodlot was payable upon application to cover all lease and management fees for the life of the project.

**Finance**

28. Growers could fund their investment in the Project themselves, borrow from Forest Enterprises Australia Ltd (“Forest Enterprises”) (a lender associated with the Responsible Entity).

29. Those Growers may enter into the following finance arrangement. The finance offered by Investment Nominees was available to a maximum of 90% of the amount that must be subscribed for each woodlot. The terms of finance were either:

- One year interest free Monthly instalments;
- 8.0% reducing interest:  
Monthly principal and interest repayments over a 2 year term; or
- 9.0% reducing interest:  
Quarterly principal and interest repayments over a 3 year term; or
- 10.0% reducing interest:  
Monthly principal and interest repayments over a 4 year term.

30. The security for the loan is provided by the assignment to Forest Enterprises Australia Ltd of the Grower’s rights and interest in the Management Agreement and the trees planted under it, and every other document, interest or right held in connection with the cultivation of the trees, including the Lease Agreement.

31. The loan provided by Forest Enterprises is on a full recourse basis and recovery action will be taken in respect of any default by the borrower.



32. This Ruling does not apply if a Grower entered into a finance agreement that 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 other than Forest Enterprises Australia Ltd ("Forest Enterprises"), are involved or become involved, in the provision of finance to Members for the Project.

## Ruling

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

#### **Section 35-55 – Commissioner's discretion**

33. For a Grower who is an individual and who entered the Project between 6 June 2000 and 5 June 2001, 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 has decided for the income years ended 30 June 2001 to 30 June 2008 that the rule in section 35-10 does not apply to this business activity provided that the Project has been, and continues to be carried on in a manner that is not materially different to the arrangement that is set out in paragraphs 14 to 32 of this Product Ruling.

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

- the ‘exception’ in subsection 35-10(4) applies (see paragraph 40 in the Explanations part of this ruling, below).
- a Grower’s business activity satisfies one of the objective tests in sections 35-30, 35-35, 35-40 or 35-45; or
- the Grower’s business activity produces assessable income for an income year greater than the deductions attributable to it for that year (apart from the operation of subsection 35-10(2); or
- the Commissioner is precluded from exercising the discretion under paragraph 35-55(1)(b) because of subsection 35-55(2).

35. Where, the “exception” in subsection 35-10(4) applies, or the Grower’s business activity satisfies one of the tests, the discretion in subsection 35-55(1) is exercised, 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.

36. 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.

## **Explanations**

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

37. Division 35 applies to losses from certain business activities for the income year ended 30 June 2001 and subsequent years. Under the rule in subsection 35-10(2) a deduction for a loss made by an individual (including an individual in a general law partnership) from certain business activities will not be taken into account in an income year unless:

- the ‘exception’ in subsection 35-10(4) applies;

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- one of four tests in sections 35-30, 35-35, 35-40 or 35-45 is met; or
- if one of the tests is not satisfied, the Commissioner exercises the discretion in section 35-55.

38. 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.

39. Losses that cannot be taken into account in a particular year of income, because of subsection 35-10(2), can be applied to the extent of future profits from the business activity, or are deferred until one of the tests is passed, the discretion is exercised, or the exception applies.

40. For the purposes of applying the tests, Division 35 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 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.

41. In broad terms, the tests require:

- (a) at least \$20,000 of assessable income in that year from the business activity (section 35-30);
- (b) the business activity results in a taxation profit in 3 of the past 5 income years (including the current year)(section 35-35);
- (c) at least \$500,000 of real property, or an interest in real property, (excluding any private dwelling) is used on a continuing basis in carrying on the business activity in that year (section 35-40); or
- (d) at least \$100,000 of certain other assets (excluding cars, motor cycles and similar other vehicles) is used on a continuing basis in carrying on the business activity in that year (section 35-45).

42. A Grower who was accepted into and who has participated in the Project since 6 June 2000 is carrying on a business activity that is subject to these provisions.

43. Information provided with the application for this Product Ruling and additional information provided since, indicates that a Grower who acquires the minimum allocation of three woodlots in the

Project is unlikely to have their business activity pass one of the tests. Growers who acquired more than three woodlots in the Project may however, find that their activity meets one of the tests prior to the year ended 30 June 2009.

44. Therefore, 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.

45. 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; and
- (ii) because of its nature, it has not yet met one of the tests set out in Division 35; and
- (iii) there is an expectation that the business activity of an individual taxpayer will either pass one of the tests or produce a taxation profit within a period that is commercially viable for the industry concerned.

46. The information provided by the applicant indicates that a grower who acquires the minimum allocation of three woodlots in the Project is expected to be carrying on a business activity that will either pass one of the tests, or produce a taxation profit, for the year ended 30 June 2009. The Commissioner has decided for such a Grower that it would be reasonable to exercise the second arm of the discretion until the year ended 30 June 2008. Subsection 35-55(2) prevents the Commissioner exercising the discretion for these Growers beyond the year ended 30 June 2008.

47. The applicant has stated that the business activity comprised by a Grower's involvement in this Project has started to be carried on, and will continue to be carried on in a manner that is not materially different to that described in the Arrangement in this Product Ruling. If, however, the Project is not carried on during the income years specified above (see paragraph 43), in the manner described in the Arrangement (see paragraphs 14 to 32), 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.

48. In deciding to exercise the discretion in paragraph 35-55(1)(b) the Commissioner has relied upon:

- the report of the independent forester and scientific evidence provided by the Responsible Entity with the application and subsequently, in further information requested by the Commissioner;
- independent, objective, and generally available information relating to the afforestation industry which substantially supports cash flow projection and other claims, including prices and costs, in the Product Ruling application submitted by the Responsible Entity.

## Detailed contents list

49. Below is a detailed contents list for this Product Ruling:

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**Commissioner of Taxation**21 November 2001

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*Previous draft:*

Not previously issued in draft form

*Related Rulings/Determinations:*PR 1999/95; TR 92/1; TR 97/16;  
TR 92/20; TR 98/22; TD 93/34*Subject references:*

- carrying on a business
- commencement of a business
- management fees
- primary production
- producing assessable income
- product rulings
- public rulings
- schemes
- tax avoidance
- tax benefits

*Legislative references:*

- ITAA 1997 Div 35
- ITAA 1997 35-10
- ITAA 1997 35-10(2)
- ITAA 1997 35-10(3)
- ITAA 1997 35-10(4)
- ITAA 1997 35-30
- ITAA 1997 35-35
- ITAA 1997 35-40
- ITAA 1997 35-45
- ITAA 1997 35-55
- ITAA 1997 35-55(1)
- ITAA 1997 35-55(1)(a)
- ITAA 1997 35-55(1)(b)
- ITAA 1997 35-55(2)
- ITAA 1936 82KL
- ITAA 1936 Pt IVA
- TAA 1953 Part IVAAA

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*ATO references:*

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