

PR 2002/103 - Income tax: The Bellview Vineyard Project (Unplanted Vineyard Lots)

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 This document has changed over time. This is a consolidated version of the ruling which was published on *26 June 2002*



Product Ruling

Income tax: The Bellview Vineyard Project (Unplanted Vineyard Lots)

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Potential 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

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.

Potential participants 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 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 potential 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. Potential participants may wish to seek assurances from the promoter that the arrangement will be carried out as described in this Product Ruling.

Potential 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

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

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 Bellview Vineyard Project (Unplanted Vineyard Lots) or simply as 'the Project'.

Tax law(s)

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 40 (ITAA 1997);
 - Division 328 (ITAA 1997);
 - section 82KL of the *Income Tax Assessment Act 1936* ('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. The class of person to whom this Ruling applies will be a Grower who acquires an Unplanted Vineyard Lot by 30 June 2002. The Unplanted Vineyard Lots that are the subject of this ruling are lots 5B, 6, 8, 10, 11, 12 and 13.

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

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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

11. This Ruling applies prospectively from 26 June 2002, 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

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

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

- Application for Product Ruling for The Bellview Vineyard Project, dated 15 February 2002 and received by the ATO on 18 February 2002;
- The Bellview Vineyard Project Information Memorandum issued by R. G. & H Investments Pty Limited (RG&H), dated December 2001 and received by the ATO on 18 February 2002. The document

includes in sections 1 through 3 the following documents:

Section 1 – **Vineyard Management Agreement;**

Section 2 - **Contract for Sale of Land**, including annexure Title of Land, Draft Community Title, Vendor Disclosure documents;

Section 3 – **Water Supply Deed;**

- Addendum to Information Memorandum, dated March 2002 and received by the ATO on 8 April 2002;
- Community Management Statement, received by the ATO on 18 February 2002;
- Draft Grape Sale Agreement with Southcorp Wines Pty Ltd received by the ATO on 5 June 2002;
- Correspondence received by the ATO from the Applicant's representative dated 15, 20, and 26 February 2002, 11, 19, 20, 28 March 2002, 9 and 24 May 2002, 5, 6, 7 and 14 June 2002;
- Correspondence from the ATO to the Applicant's representative dated 8 and 18 March 2002, 16 April 2002, 20 and 29 May 2002 and 4, 5, and 6 June 2002.

Note: Certain information received from the applicant has been provided on a commercial-in-confidence basis and will not be disclosed or released under the Freedom of Information legislation.

15. The documents highlighted are those that the Growers enter into. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or an associate of the Grower will be a party to that are part of the arrangement to which this Ruling applies.

16. All Australian Securities and Investments Commission (ASIC) requirements are, or will be, complied with for the term of the agreements. The effect of the agreements may be summarised as follows.

Overview

17. The arrangement is called the Bellview Vineyard Project (Unplanted Vineyard Lots) and is summarised as follows:

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Location	22 kms North of Orange, NSW, and 16 kms East of Molong, NSW.
Type of business	Viticulture.
Number of hectares to be developed	55 hectares.
Name of development	The Bellview Vineyard Project (Unplanted Vineyard Lots).
Size of participation	Vineyard lots range in size from 7.739 hectares to 11.52 hectares with areas under vine ranging from 7.171 hectares to 11.2 hectares.
Number of vines per hectare	1,667.
Nature of the investment	Freehold title over land (subject to Community title).
The term of investment	Initial 15 year management agreement.
Initial Cost per hectare	Land and establishment costs of \$44,905 per hectare, comprising: <ul style="list-style-type: none"> • Freehold land \$ 4,777 • Roadworks \$ 265 • Pumps, pipes & drips \$19,061 • Land preparation \$ 2,744 • Vines & Planting \$ 4,448 • Trellising \$13,610
Ongoing costs	Management & Operating expenses estimated at \$9,015 in 2003, \$10,044 in 2004 and \$10,012 in 2005.

Description

18. The Bellview Vineyard is being developed as a Community Title vineyard located at Bellview Vineyard, Belgravia Road, Orange, NSW. The vineyard comprises 174.7 hectares, which is divided into 12 vineyard lots ranging in size from 7.171 hectares to 11.2 hectares. The total area under viticulture will be 104 hectares. The remaining 70.7 hectares is occupied by roads and common land that contains the necessary infrastructure for the Project.

19. Vineyard Lots 2, 3, 4, 7, 9 and 5A were established in September 2001 (Planted Vineyard Lots) and have a total of 49 planted hectares. Vineyard Lots 5B, 6, 8 10, 11 12 and 13 (Unplanted Vineyard Lots) are expected to be established in September 2002 and will total 55 planted hectares. Approximately 1,667 vines have been or will be planted per hectare of the Project (Planted and Unplanted Vineyard Lots). The vines planted will be

Shiraz 32.8 hectares, Merlot 20.7 hectares, Riesling 4.6 hectares, Chardonnay 36.2 hectares, Traminer 9.7 hectares, totalling 104 hectares.

20. RG&H have advised the ATO that the Unplanted Vineyard Lots should be planted with vines by 30 September 2002 and Growers who acquire one of these lots will be accepted into the Project by 30 June 2002. **This Product Ruling only applies to Growers who acquire an Unplanted Vineyard Lot by 30 June 2002.**

21. The first harvest is expected in 2004. For the initial 5 years of production 100% of the fruit produced by the vineyard will be purchased under contract by Southcorp Wines Pty Ltd, subject to the Draft Grape Sale Agreement being executed.

22. A Grower will participate in the project by:

- entering into a 'Contract for Sale and Purchase of Land' with RG&H to buy freehold title to an identified Unplanted Vineyard Lot, which is subject to Community Title. Under the terms of the Community Corporation by-laws the land may only be used for viticulture;
- entering into a Vineyard Management Agreement with RG&H to provide ongoing management services of the vineyard; and
- entering into a Water Supply Deed with RG&H to supply water to the Grower's Unplanted Vineyard Lot.

Contract for Sale and Purchase of Land

23. The Community Title associated with the vineyard is governed by the Community Land Development Act 1989. Under this Act the owner of a community lot owns all of the improvements on that lot and the common property is vested in the owners of the community lots as tenants in common.

24. The land purchase price of Unplanted Vineyard Lots is \$4,777 per hectare of which 50% is payable on the exchange of the Land Sale Contract and the remaining 50% is payable on settlement. Between the exchange and settlement date of the Land Sale Contract each Grower will have a licence over their specific Vineyard Lot. Under clause 2.8.1 the completion of the contract is subject to and conditional on the following pre-conditions:

- (a) satisfactory Development Consent to carry out the Development substantially in accordance with the terms of the Development Application obtained and Registration by 31 December 2002;

- (b) favourable ATO Product Ruling;
- (c) execution of the Southcorp Wines Pty Ltd Agreement for Sale and Purchase of Wine Grapes.

25. Where the above pre-conditions are not satisfied either RG&H or the Grower will be entitled to rescind the contract whereupon the Vineyard Management Agreement and Water Supply Deed will terminate (clause 2.8.2). All moneys paid by the Grower to RG&H under the Land Sale Contract, the Vineyard Management Agreement and the Water Supply Deed will be refunded in full by RG&H together with interest thereon calculated at the rate of 7% per annum from the date of payment of any amount until repayment in full (clause 11.2). **This Product Ruling has no application and the tax deductions outlined in the Ruling section are not allowable to a Grower where their Land Sale Contract is rescinded.**

Vineyard Management Agreement

26. Under clause 6.1 the Grower enters into a Vineyard Management Agreement with RG&H to provide ongoing management of the Vineyard for an initial period of 15 years. The Grower and RG&H will review the operation of this agreement not less than 2 years before the expiration of the term, with the intention that this agreement will be extended for a further term of 5 years (clause 6.2). The parties may then negotiate to further extend the Vineyard Management Agreement for a further extended term of 5 years (clauses 6.3 and 6.4).

27. The Growers appoint RG&H to do all things necessary or advisable for the efficient and economic establishment, development, maintenance and conduct of the Project (clause 6.6).

28. RG&H will also act as the Community Corporation Manager and will be responsible for discharging the statutory functions and business affairs of the Community Corporation.

29. Fruit from each lot will be pooled and on-sold to the purchasing winery under the Power of Attorney granted by the Growers to RG&H (clause 4). The gross proceeds from the sale of the grapes produced by the Project shall be aggregated and divided between the respective Growers bases on the number of planted hectares owned by a Grower in the Project who contributes to the pool.

30. Growers are required to pay RG&H the Establishment Costs, outlined at paragraph 34 below (clause 11). Pursuant to clause 12 Growers are also required to pay RG&H a Vineyard Management Fee, subject to annual indexation, and their share of the Operating Expenses calculated as a percentage of the planted hectares owned by

a Grower to the total planted hectares of all Growers (clause 12.3). The Vineyard Management Fee and the Operating Expenses shall be paid by a Grower to RG&H by equal six monthly instalments (clause 12.4).

31. Operating Expenses are defined at clause 1.14 to mean all operating costs, charges, expenses, fees taxes (other than income or capital gains tax) and other payments and expenditures of and incidental to the conduct of the Project. The amounts a Grower is required to pay under the Water Supply Deed are classed as Operating Expenses.

Water Supply Deed

32. RG&H is the holder of the Bell River Licence, the Woolshed Dam License and the Bore Licenses and has applied for additional licenses for water from the Bell River Authority and the Woolshed Dam Authority. Subject to the granting of the additional licenses each Grower will have a surface water entitlement of 2 megalitres per developed hectare (clause 4.3).

33. In accordance with clause 4.4 Growers are liable for their share of all fees, costs or charges levied from time to time by the Department of Land & Water Conservation or other authority. Under clause 7.1 each Grower shall pay a Delivery Fee to RG&H which will be calculated based on a fixed charge and usage charge for each megalitre delivered per annum.

Grower Payments

34. The growers will incur the following costs per hectare commencing by 30 June 2002.

Description	Due date for Payment	Amount
Payments to acquire and develop 1 hectare lot		
Purchase Freehold Land (including roads & water licence)	30 June 2002 On settlement	2,389 2,388
Roadworks	30 June 2002	265
Pumps Pipes & Drips	30 June 2002 2003 financial year	18,822 239
Establish Vines	30 June 2002 2003 financial year 2004 financial year	3,348 3,728 117
Trellising – Vines	30 June 2002 2003 financial year	12,682 229

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	2004 financial year	698
Total Land and Establishment Costs		44,905
Year 1 (2002)		
Vineyard Management Fees	½ yearly	0
Operating Expenses	½ yearly	0
Year 2 (2003)		
Estimated Vineyard Management Fees	½ yearly	1,102
Estimated Operating Expenses	½ yearly	7,913
Year 3 (2004)		
Estimated Vineyard Management Fees	½ yearly	1,129
Estimated Operating Expenses	½ yearly	8,915

Finance

35. Growers can fund their investment in the Project themselves or borrow from an independent lender. Growers are required to obtain their own finance for the Project.

36. 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

Application of this Ruling

37. This Ruling applies only to Growers who are accepted to participate in the Project by 30 June 2002 and who have exchanged the Land Sale Contract and executed the Vineyard Management Agreement and the Water Supply Deed by 30 June 2002.

38. **This Ruling has no application where a Grower's Land Sale Contract is rescinded prior to settlement. No tax deductions in relation to the Project will be available. Where a Grower claims tax deductions in his/her income tax return as a result of their participation in this Project and their Land Sale Contract is later rescinded they will need to amend their income tax return to exclude the claimed income tax deductions.**

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

40. For a Grower participating in the Project, the recognition of income and the timing of tax deductions, including those related to capital allowances, 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

41. 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

42. That part of the gross sales 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.

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

Deductions for Vineyard Management Fees and Operating Expenses for Growers who are accepted into the Project by 30 June 2002

Section 8-1

44. A Grower who is not an ‘STS taxpayer’ may claim tax deductions for the following revenue expenses:

Fee Type for each developed hectare	ITAA 1997 Section	Year ended 30 June 2002	Year ended 30 June 2003	Year ended 30 June 2004
Estimated Vineyard Management Fees	8-1	Nil	\$1,102 – See Notes (i) & (ii) (below)	\$1,129 – See Notes (i) & (ii) (below)
Estimated Operating Expenses	8-1	Nil	\$7,913 – See Notes (i) & (ii) (below)	\$8,915 – See Note (i) & (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 112.
- (ii) The Vineyard Management Fees and Operating Expenses shown in the Vineyard Management Agreement and Water Supply Deed are deductible in

full in the year that they are incurred. The fees shown in the table above are estimates and the actual amount to be paid will be invoiced by RG&H by equal six monthly instalments. 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 86 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.

Deductions for capital expenditure

Division 40

45. A Grower who is not an 'STS taxpayer' will also be entitled to tax deductions relating to trellising, water facilities (e.g., irrigation) and grapevines. All deductions shown in the following Table are determined under Division 40.

Fee Type for each developed hectare	ITAA 1997 section	Year ended 30 June 2002	Year ended 30 June 2003	Year ended 30 June 2004
Trellising	40-25	Must be calculated – See Notes (iii) and (iv) below	Must be calculated – See Notes (iii) and (iv) below	Must be calculated – See Notes (iii) and (iv) below
Water facility (e.g., irrigation, dam, bore, etc)	40-515	\$6,274 - see Notes (iii) & (v) below	\$6,354 – see Notes (iii) & (v) below	\$6,354 – see Notes (iii) & (v) below
Establishment of horticultural plants (grapevines)	40-515	Nil – see Notes (iii) & (vi) below	Must be calculated – see Notes (iii) & (vi) below	Must be calculated – see Notes (iii) & (vi) below

Notes:

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- (iii) If the Grower is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted as relevant for GST (e.g., input tax credits): Division 27. See example at paragraph 112.
- (iv) Trellising is a 'depreciating asset'. Each Grower's interest in the trellising is a 'depreciating asset'. The 'cost' of the asset is the amount paid by each Grower. The decline in value of the asset is calculated using the formula in either subsection 40-70(1) ('diminishing value method') or subsection 40-75(1) ('prime cost method'). Both formulas rely on the 'effective life' of the trellising.

Growers can either self-assess the 'effective life' (section 40-105) or use the Commissioner's determination of 'effective life' (section 40-100). The Commissioner has determined that trellising has an 'effective life' of 20 years. For Growers who are accepted into the Project by 30 June 2002 the trellising will commence to decline in value from that date. RG&H has advised the trellising has been installed on the Unplanted Vineyard Lots.

- (v) Any irrigation system, dam or bore is a 'water facility' as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. A deduction is available under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one third of the capital expenditure incurred by each Grower on the acquisition of the 'water facility' in the year in which it is incurred and one third in each of the next 2 years of income (section 40-540).
- (vi) The conditions in subsection 40-525(3) are met when the grapevines are affixed to land which the Grower owns. The grapevines are eligible for the 4 year write-off under section 40-550 from the date they were established. Growers who acquire Unplanted Vineyard Lots will not own the land until the Land Sale Contract is settled. Where the Land Sale Contract is settled before the grapevines are established the 4 year write-off period will commence from the date of establishment of the grapevines. Where the Land Sale Contract is settled after the grapevines are established the 4 year write-off period still commences from the date of establishment, however a Grower's write-off period will commence from the date of settlement of

the Land Sale Contract to the end of the 4 year period after establishment. No deduction is available for the period between the date of establishment to the settlement date of the Land Sale Contract. The establishment cost available for write-off will be the actual cost incurred by RG&H (exclusive of GST) and not the amount paid by the Grower under the Vineyard Management Agreement. RG&H have advised they plan to establish the grapevines before 30 September 2002 and they will provide Growers with the necessary information in accordance with section 40-575.

Tax outcomes for Growers who are ‘STS taxpayers’

Assessable Income

Section 6-5 and section 328-105

46. That part of the gross sales 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.

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

Deductions for Vineyard Management Fees and Operating Expenses for Growers who are accepted into the Project by 30 June 2002

Section 8-1 and section 328-105

48. A Grower who is an ‘STS taxpayer’ may claim tax deductions for the following revenue expenses:

Fee Type for each developed hectare	ITAA 1997 Sections	Year ended 30 June 2002	Year ended 30 June 2003	Year ended 30 June 2004
Estimated Vineyard Management Fee	8-1 & 328-105	Nil	\$1,102 – See Notes (vii), (viii) & (ix) (below)	\$1,129 – See Notes (vii), (viii) & (ix) (below)
Estimated Vineyard Operating Expenses	8-1 & 328-105	Nil	\$7,913 – See Note (vii), (viii) & (ix)	\$8,915 – See Note (vii), (viii) & (ix)

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			(below)	(below)
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Notes:

- (vii) 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 112.
- (viii) If, for any reason, an amount shown in the Table above is not fully paid in the year in which it is incurred by a Grower who is an 'STS taxpayer' then the amount 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 shown in the Table above which is not paid in the year in which it is incurred will be deductible in the year in which it is actually paid.
- (ix) Where a Grower who is an 'STS taxpayer', pays the Vineyard Management Fees and Operating Expenses in the relevant income years shown in the Vineyard Management Agreement and Water Supply Deed, those fees are deductible in full in the year that they are paid. The fees shown in the table above are estimates and the actual amount to be paid will be invoiced by RG&H by equal six monthly instalments. However, if a Grower **chooses** to prepay fees for the doing of a thing (e.g., the provision of management services) that will not be wholly done in the income year the fees are incurred, the prepayment rules of the ITAA may apply to apportion those fees (see paragraphs 809 to 93) . In such cases, the tax deduction for the prepaid fee must be determined using the formula shown in paragraph 86, 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.

Deductions for capital expenditure***Subdivision 328-D and Subdivision 40-F***

49. A Grower who is an 'STS taxpayer' will also be entitled to tax deductions relating to trellising, water facilities (e.g., irrigation) and grapevines. Deductions relating to the 'cost' of trellising must be determined under Division 328. An 'STS taxpayer' may claim

deductions in relation to water facilities under Subdivision 40-F. If the 'water facility' expenditure is on a 'depreciating asset' used to carry on the business, they may choose to claim a deduction under Division 328. Deductions for the grapevines must be determined under Subdivision 40-F.

50. The deductions shown in the following Table assume, for representative purposes only, that a Grower has either chosen to or can only claim deductions for expenditure on water facilities under Subdivisions 40-F and not under Division 328. If the expenditure has been incurred on 'depreciating assets' and is claimed under Division 328, the deduction is determined as discussed in Note (xi) below.

51. Under Division 328, if the 'cost' of a 'depreciating asset' at the end of the income year is less than \$1000 (a 'low-cost asset'), it can be claimed as an immediate deduction when first used or 'installed ready for use'. This is so provided the Grower is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income.

Fee Type for each developed hectare	ITAA 1997 section	Year ended 30 June 2002	Year ended 30 June 2003	Year ended 30 June 2004
Trellising	328-185 & 328-190	\$1,902 – See Notes (x) & (xi) below	\$3,268 – See Notes (x) & (xi) below	\$2,427 - See Notes (x) & (xi) below
Water facility (e.g. irrigation, dam, bore, etc.)	40-515	\$6,274 – see Notes (x) & (xii) below	\$6,354 – see Notes (x) & (xii) below	\$6,354 - see Notes (x) & (xii) below
Establishment of grapevines	40-515	Nil - see Notes (x) & (xiii) below	Must be calculated – see Notes (x) & (xiii) below	Must be calculated - see Notes (x) & (xiii) below

Notes:

- (x) If the Grower is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted as relevant for GST (e.g., input tax credits): Division 27. See example at paragraph 112.

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- (xi) Trellising is a 'depreciating asset'. Each Grower's interest in the trellising is a 'depreciating asset' which can be allocated to a 'general STS pool'. The 'cost' of the asset is the amount paid by each Grower. The tax deduction allowable is determined in the year ended 30 June 2002 by multiplying the 'cost' of the interest by half the 'general STS pool rate, i.e. by 15%. Each Grower's interest in the trellising is allocated to their 'general STS pool' at the end of the year ended 30 June 2002 and that part of the 'cost' not deducted in the first year is added to the pool balance. In subsequent years, the full pool rate of 30% will apply.
- (xii) Any irrigation system, dam or bore is a 'water facility' as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. If the expenditure is on a 'depreciating asset' (the underlying asset), the Grower may choose to claim a deduction under either Division 328 or Subdivision 40-F. For the purposes of Division 328, each Grower's interest in the underlying asset is itself deemed to be a 'depreciating asset'. If the 'cost' apportionable to that deemed 'depreciating asset' is less than \$1000, the deemed asset is treated as a 'low-cost asset' and that amount is deductible in full when the underlying asset is first used or 'held' ready for use. This is so provided the Grower is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income. If the deemed asset is not treated as a 'low-cost asset', the tax deduction allowable in the year ended 30 June 2002 is determined by multiplying its 'cost' by half the relevant STS pool rate. At the end of the year, it is allocated to the relevant STS pool and in subsequent years the full pool rate will apply. If the expenditure is not on a 'depreciating asset', or if they choose to use Subdivision 40-F, Growers must claim deductions under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one third of the capital expenditure incurred by each Grower on the acquisition of the 'water facility' in the year in which it is incurred and one third in each of the next 2 years of income (section 40-540).
- (xiii) The conditions in subsection 40-525(3) are met when the grapevines are affixed to land which the Grower

owns. The grapevines are eligible for the 4 year write-off under section 40-550 from the date they were established. Growers who acquire Unplanted Vineyard Lots will not own the land until the Land Sale Contract is settled. Where the Land Sale Contract is settled before the grapevines are established the 4 year write-off period will commence from the date of establishment of the grapevines. Where the Land Sale Contract is settled after the grapevines are established the 4 year write-off period still commences from the date of establishment, however a Grower's write-off period will commence from the date of settlement of the Land Sale Contract to the end of the 4 year period after establishment. No deduction is available for the period between the date of establishment to the settlement date of the Land Sale Contract. The establishment cost available for write-off will be the actual cost incurred by RG&H (exclusive of GST) and not the amount paid by the Grower under the Vineyard Management Agreement. RG&H have advised they plan to establish the grapevines before 30 September 2002 and they will provide Growers with the necessary information in accordance with section 40-575.

Tax outcomes that apply to all Growers

52. The deductibility or otherwise 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. However all Growers who borrow funds in order to participate in the Project, should read the discussion of the prepayment rules in paragraphs 80 to 93 (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.

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

Section 35-55 – Commissioner's discretion

53. 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 2005 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.

54. 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 100 in the Explanations part of this ruling, below); or
- a Grower's business activity satisfies one of the 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).

55. Where, the exception in subsection 35-10(4) applies, the Grower's business activity satisfies one of the tests, or 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.

56. 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

57. For a Grower who participates in the Project and incurs expenditure as required by the Vineyard Management Agreement and the Water Supply Deed 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 80 to 93);
- 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

Is the Grower carrying on a business?

58. For the amounts set out in the Tables above to constitute allowable deductions the Grower's viticulture activities as a participant in the Bellview Vineyard Project must amount to the carrying on of a business of primary production. These viticulture activities will fall within the definitions of 'horticulture' and 'commercial horticulture' in section 40-535 of the ITAA 1997.

59. For schemes such as that of the Bellview Vineyard Project, 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* (1984) 16 ATR 55; 84 ATC 4929.

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

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

61. In this Project, each Grower will have freehold ownership of their own Vineyard Lot under a Community Title Development from the settlement date of their Land Sale Contract. Between the exchange and settlement date of the Land Sale Contract each Grower will have a licence over their specific Vineyard Lot. Each Grower will also enter into a Vineyard Management Agreement and a Water Supply Deed.

62. This product ruling relates only to those Growers who acquire a Vineyard Lot that will be developed by RG&H before 30 September 2002. The lots to be developed (Unplanted Vineyard Lots) are lots 5B,

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6. 8, 10, 11, 12 and 13. The lots that were developed by RG&H in September 2001 (Planted Vineyard Lots), lots 2, 3, 4, 7, 9 and 5A, were ruled on in a separate product ruling. Under the Community Title Development the Vineyard Lots are to be used for the purpose of carrying out viticultural activities and for no other purpose.

63. The Vineyard Management Agreement allows RG&H to come onto the land to carry out its obligations under the agreement. Under the agreement RG&H is engaged by the Grower to establish and maintain the Grower's Vineyard Lot during the term of the Project. RG&H has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the Vineyard Lot on the Grower's behalf.

64. In purchasing the Vineyard Lot, the Grower acquires from RG&H the trellising, water facilities (e.g., irrigation) and grapevines that are to be established on the Grower's Vineyard Lot. During the term of the Project, these assets will be used wholly to carry out the Grower's viticulture activities. RG&H is also engaged to harvest and sell, on the Grower's behalf, the grapes grown on the Grower's Vineyard Lot.

65. 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.

66. 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 its grapes 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.

67. The pooling of grapes grown on the Grower's Vineyard Lot with the grapes of other Growers is consistent with general viticulture practices. Each Grower's proportionate share of the sale proceeds of the pooled grapes will reflect the proportion of the grapes contributed from their Vineyard Lot.

68. RG&H's services on the Grower's behalf are also consistent with general viticulture practices. The established assets are of the type ordinarily used in carrying on a business of viticulture. While the size of a Vineyard Lot is relatively small, it is of a size and scale to allow it to be commercially viable (see Taxation Ruling IT 360).

69. The Grower's degree of control over RG&H as evidenced by the Vineyard Management Agreement, and supplemented by the Corporations Act, is sufficient. During the term of the Project, RG&H will provide the Grower with regular progress reports on the Grower's Vineyard Lot and the activities carried out on the Grower's behalf.

Growers are able to terminate arrangements with RG&H in certain instances, such as cases of default or neglect.

70. The viticulture 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 Growers’ viticulture activities in the Bellview Vineyard Project will constitute the carrying on of a business.

The Simplified Tax System

Division 328

71. 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.

72. 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’.

Deductibility of Vineyard Management Fees and Operating Expenses

Section 8-1

73. Consideration of whether the Vineyard Management Fees and Operating Expenses are 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

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sufficient connection with activities to produce assessable income.

74. The Vineyard Management Fees and Operating Expenses associated with the viticulture activities will relate to the gaining of income from the Grower's business of viticulture (see above), and hence have a sufficient connection to the operations by which income (from the regular sale of grapes) is to be gained from this business. They 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 Vineyard 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

75. Under the Vineyard Management Agreement and the Water Supply Deed neither the Vineyard Management Fees nor the Operating Expenses are 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.

76. 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 80 to 93) 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

77. In the absence of any application of the prepayment provisions, the timing of deductions for the Vineyard Management Fees or the Operating Expenses will depend upon whether a Grower is an 'STS taxpayer' or is not an 'STS taxpayer'.

78. If the Grower is not an 'STS taxpayer', the Vineyard Management Fees and Operating Expenses are deductible in the year in which they are incurred.

79. If the Grower is an 'STS taxpayer' the Vineyard Management Fees and Operating Expenses are deductible in the income year in which they are paid, or are 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.

Prepayment provisions

Sections 82KZL to 82KZMF

80. 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 licencing 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.

81. For this Project only section 82KZL (an interpretative 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

82. 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)).

83. 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 assessable income attributable to the agreement for that year; and

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- 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.

84. For the purpose of these provisions, the agreement includes all activities that relate to the agreement (subsection 82KZME(4)).

85. 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.

86. 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.

$$\text{Expenditure X} \frac{\text{Number of days of eligible service period in the year of income}}{\text{Total number of days of eligible service period}}$$

87. 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

88. In this Project, the initial fees payable on acceptance are for capital expenditure. The Vineyard Management Fee and Operating Expenses are not payable until after 30 June 2002 for providing management services or operating expenses to a Grower by

30 June 2003. Under the Agreements, further annual expenditure is required each year during the term of the Project for the provision of management services and operating expenses until 30 June in those years.

89. There is 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 Vineyard Management Fees and Operating Expenses are for RG&H doing 'things' that are not to be wholly done within the expenditure year.

90. On this basis, provided a Grower incurs expenditure as required under the Project agreements, as set out in paragraph 34, 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

91. Although not required under either the Vineyard Management Agreement or the Water Supply Deed, a Grower participating in the Project may choose to prepay fees for a period beyond the 'expenditure year'. Where this occurs, contrary to the conclusion reached in paragraph 90 above, section 82KZMF will apply to apportion the expenditure and allow a deduction over the period in which the prepaid benefits are provided.

92. For these Growers, the amount and timing of deductions for any relevant prepaid Vineyard Management Fees or Operating Expenses will depend upon when the respective amounts are incurred and what the 'eligible service period' is in relation to these amounts.

93. However, as noted above, prepaid fees of less than \$1,000 incurred in an expenditure year will be 'excluded expenditure' and will be not subject to apportionment under section 82KZMF.

Expenditure of a capital nature

Division 40 and Division 328

94. Any part of the expenditure of a Grower that is attributable to acquiring an asset or advantage of an enduring kind is generally capital or capital in nature and will not be an allowable deduction under section 8-1. In this Project, expenditure attributable to trellising, water facilities and the establishment of the grapevines is of a capital nature. This expenditure falls for consideration under Division 40 or Division 328 of the ITAA 1997.

95. The application and extent to which a Grower claims deductions under Division 40 and Division 328 depends on whether or not the Grower is an 'STS taxpayer'.

96. The tax treatment of capital expenditure has been dealt with in a representative way in paragraphs 45 and 51 (above) in the Tables and the accompanying Notes.

Deferral of losses from non-commercial business activities

Division 35

97. 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;
- 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.

98. 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.

99. 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.

100. For the purposes of applying 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' 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.

101. 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 vehicles) are used on a continuing basis in carrying on the business activity in that year (section 35-45).

102. 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 an Unplanted Vineyard Lot in the Project is unlikely to have their activity pass one of the tests until the income year ended 30 June 2006.

103. Therefore, prior to this time, 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.

104. 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.

105. Information provided with this Product Ruling indicates that a Grower who acquires the minimum allocation of vineyard lots 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 2006. 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 2005. Subsection 35-55(2) prevents the Commissioner exercising the discretion beyond this year.

106. This Product Ruling is issued on a prospective basis (i.e., 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 paragraph 53), in the manner described in the Arrangement (see paragraphs 14 to 36). 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.

107. 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 viticulturist.

Section 82KL - recouped expenditure

108. 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 tax avoidance provisions

109. 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).

110. The Bellview Vineyard Project 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 44, 45, 48 and 51 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.

111. 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 their grapes. 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

Entitlement to GST input tax credits

112. 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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