



# ***PR 2003/21 - Income tax: Gunns Plantations Woodlot Project 2003***

 This cover sheet is provided for information only. It does not form part of *PR 2003/21 - Income tax: Gunns Plantations Woodlot Project 2003*

 This document has changed over time. This is a consolidated version of the ruling which was published on *7 May 2003*



## Product Ruling

### Income tax: Gunns Plantations Woodlot Project 2003

---

Contents	Para
What this Product Ruling is about	1
Date of effect	11
Withdrawal	13
Arrangement	14
Ruling	36
Explanations	53
Example	119
Detailed contents list	120

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 the 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 law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates. In this Ruling this arrangement is sometimes referred to as the 'Gunns Plantations Woodlot Project 2003 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 328 (ITAA 1997);
  - Section 82KL of the *Income Tax Assessment Act 1936* ('ITAA 1936');
  - Section 82KZL (ITAA 1936);
  - Sections 82KZME - 82KZMF (ITAA 1936);
  - Section 82KZMG (ITAA 1936); and
  - Part IVA (ITAA 1936).

### **Goods and Services Tax**

3. All fees and expenditure referred to in this Ruling include the 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 laws 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 potential 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 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 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 it. Growers who elect to market their own produce are also excluded from the class of persons to whom this Ruling applies.

### **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:

Commonwealth Copyright Administration  
Intellectual Property Branch  
Department of Communications, Information Technology and  
the Arts  
GPO Box 2154  
Canberra ACT 2601

or by e-mail: [commonwealth.copyright@dcita.gov.au](mailto:commonwealth.copyright@dcita.gov.au).

## Date of effect

---

11. This Ruling applies prospectively from 7 May 2003, 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 the private ruling if the income year to which the private ruling 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 2006. 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 persons' 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 dated 24 January 2003;
- Draft Product Disclosure Statement (PDS) dated 3 March 2003;
- **Draft Gunns Plantations Woodlot Project 2003 Constitution dated 24 January 2003;**
- **Draft Forestry Right Deed between a Landowner and Gunns Plantations Limited (Gunns Plantations) dated 24 January 2003;**
- **Draft Lease of Forestry Right between Gunns Plantations Limited (as the Landlord) and the Grower dated 24 January 2003;**
- Draft Compliance Plan for the Gunns Plantations Project 2003 to be adopted by Gunns Plantations Limited (as Responsible Entity) dated 24 January 2003;
- Deed Poll by Gunns Limited in favour of the Growers dated 24 January 2003;
- **Draft Management Agreement between Gunns Plantations Limited (Manager) and Gunns Limited and the Grower dated 24 January 2003;**
- **Draft Finance Package including the Standard Finance Package, Purple Finance Package, Blue Finance Package, Red Finance Package and Platinum Finance Package for the Gunns Plantations Woodlot Project 2003;**
- Draft Wood Sale Agreement between Gunns Plantations Limited (as agent for each Grower) and Gunns Limited dated 24 February 2003;
- Draft Custody Agreement between Gunns Plantations Limited (Trustee) and Gunns Limited (Custodian) dated 24 January 2003;
- Draft Amending Agreement to Custody agreement between Gunns Plantations Limited (Trustee) and Gunns Limited (Custodian) dated 13 March 2003; and
- Additional correspondence between the Tax Office and the Applicant and or Applicant's representative dated 10 February 2003, 13 February 2003, 21 February 2003, 6 March 2003, 7 March 2003, 17 March 2003, 20 March 2003, 21 March 2003, 3 April 2003, 4 April 2003, 10 April 2003, 16 April 2003, 24 April 2003, 28 April 2003, 29 April 2003.

**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 that Growers may enter into. For the purposes of describing the arrangement to which this Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate of a Grower, will be a party to, which are a part of the arrangement. The effect of these agreements is summarised as follows.

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

### Overview

17. The salient features of the Gunns Plantations Woodlot Project 2003 are as follows:

Location	A number of specified parcels of land in Northern Tasmania recorded by register
Type of business each participant is carrying on	Commercial growing of <i>Eucalyptus globulus</i> (Tasmanian Blue-Gum) and <i>Eucalyptus nitens</i> (Shining Gum) trees under one of two options:  <b>Option 1:</b> Eucalyptus for Pulpwood.  <b>Option 2:</b> Eucalyptus for Veneer and Pulpwood.
Number of hectares offered for cultivation	There is a target of 5,000 hectares under the PDS, however, oversubscriptions may be accepted.
Size of each interest	One hectare
Number of trees per hectare	Minimum average of 1,100
Term of the Project	Option 1: 13 years Option 2: 20 years
Initial cost per hectare	Application Fee of \$4,400 (including GST).

Ongoing costs	There will be no fees for ongoing costs such as maintenance or lease rental. These costs will be covered by a percentage of sale proceeds from the thinning in year 9 and from the clear fell in year 13 or 20, depending on which option is chosen.
Other costs	<p>Growers will be charged for the cost of any insurance (optional) except public liability insurance.</p> <p>A pruning fee will be payable for Option 2 in years 4 (\$736), 6 (\$788) and 7 (\$840) (inclusive of GST). These base costs will be increased in line with CPI.</p> <p>A fee for sales commission, planting, rental and maintenance will be charged at year 9 (i.e. at the time of thinning) and at the end of the Project. The fee will equal 12% (inclusive of GST) of the sale proceeds from the Woodlot.</p>

18. Growers participating in the Project acquire a lease of a Forestry Right by entering into a Lease Agreement with Gunns Plantations as the Landlord. The Forestry Right will comprise contractual rights in relation to an identifiable area of land called a Woodlot. Effectively, the Forestry Right will enable Growers to access the land to establish, maintain and ultimately harvest the Woodlot. The Growers will also contract with Gunns Plantations as the Responsible Entity, under a Management Agreement, to have eucalyptus planted on the Woodlot for the purpose of eventual felling and sale in approximately 13 or 20 years, depending on which option is chosen.

19. Under the Product Disclosure Statement (PDS), Gunns Plantations will offer Woodlots of one hectare for an initial cost of \$4,400 (including GST). Gunns Plantations has the right to accept oversubscriptions. There is no minimum amount that must be raised under the PDS. The land for the Project has been leased by Gunns Plantations either from Gunns Limited or a third party landowner. Additional land will be secured if necessary. Gunns Plantations is a wholly owned subsidiary of Gunns Limited.



**Constitution**

20. The Constitution for the Project sets out the general functions, powers and duties under which the Responsible Entity agrees to act for the Growers and to manage the Project. The Forestry Right Deed, Management Agreement, Forestry Right Lease Deed and Draft Wood Sale Agreement are Schedules to the Constitution. These Agreements will be executed on behalf of each Grower who has signed the Application and Power of Attorney Forms in the Product Disclosure Statement and who is accepted into the project. After acceptance and execution of the Agreements, Growers are bound by the Constitution, Lease and Management Agreements by virtue of their participation in the Project. The Responsible Entity will keep a register of Growers accepted into the Project.

**Compliance Plan**

21. The Responsible Entity has prepared a Compliance Plan in accordance with the *Corporations Act 2001*. Under the Compliance Plan, a Compliance Committee will monitor to what extent the Responsible Entity meets its obligations as the Responsible Entity of the Project and the rights of the Growers are protected.

**Interest in Land**

22. Growers participating in the arrangement will enter into Lease and Management Agreements with Gunns Plantations (the 'Responsible Entity' and 'Lessor'). Growers will acquire a lease of a Forestry Right for one or more Woodlots, each comprising approximately one hectare of land.

**Management Agreement and Lease of Forestry Right**

23. Under the Management Agreement, the Responsible Entity undertakes to use its best endeavours to ensure that all Establishment & Planting Services are provided in relation to each Woodlot before the earlier of 12 months following the date on which the Application Fee is paid, or the Manager is first permitted under the Forestry Right Deed to access the land for the purpose of commencing the Establishment & Planting Services. However, if that period extends beyond 30 June of the financial year immediately following the year in which the Application Fee is paid, the Responsible Entity is to ensure that the services will be provided by that 30 June (Management Agreement cl. 4.1(b) & 4.2(b)).

24. Under the Lease of Forestry Right and Management Agreement, Growers enter into a 13 or 20 year lease for one or more Forestry Rights and contract with Gunns Plantations to establish and maintain the plantation until maturity. Clause 3 of the Lease of Forestry Right agreement grants a lease of a Forestry Right to the Grower. Growers are not entitled to assign their rights under the Lease and Management Agreements, except in certain circumstances (cl 25.3 of the Management Agreement). Statements of interest are issued to Growers. Gunns Plantations keeps a register of Growers. Growers execute an Application and Power of Attorney Form enabling Gunns Plantations to act on their behalf as required.

25. Growers will appoint Gunns Plantations, acting as their agent, to sell the timber produce on the Grower's behalf (cl 11.1 of the Management Agreement), for the prevailing market price to Gunns Limited, but subject to the floor price (cl 5 of the Draft Wood Sale Agreement).

26. Gunns Plantations, as manager of the 2003 project, will enter into a Deed Poll with Gunns Limited whereby Gunns Limited will agree to purchase the harvested wood for a fair and reasonable price having regard to several factors (refer clause 5 of the Draft Wood Sale Agreement) including the market price of similar wood and its quality. However, the purchase price under that Agreement will not be less than:

- in the case of wood harvested from sale as pulpwood, the price per tonne equal to 35% FOB (expressed in green metric tonnes) for the average price of Australian hardwood plantation woodchip exports at the time of Harvest as published by Gunns Limited (Gunns) and the price paid by Gunns to other major Tasmanian plantation timber suppliers for wood of the same or similar species, quality and quantity as determined by Gunns Plantations (the Average Comparative Price);
- in the case of wood harvested for sale as veneer logs, the price per m<sup>3</sup> determined by Gunns Plantations in accordance with the following formula:  $ASP \times Yield \times 7\%$  (where 'ASP' = average selling price for Gunns eucalypt veneer leaves (expressed in \$/m<sup>2</sup>) derived from plantations as defined in the audited accounts of Gunns Limited and 'Yield' = m<sup>2</sup> saleable veneer/m<sup>3</sup> plantation log input as defined in the audited accounts of Gunns Limited) and the Average Comparative Price; and

- Gunns Limited will not be obliged to purchase the timber produce in the event of a material adverse change in Gunns Limited's level of committed sales. In the event of such material adverse change, Gunns Plantations will be authorised to sell the timber produce to another party. In accordance with the Management Agreement and the Constitution, each Grower is entitled to an allocation of that Grower's proportional interest in the Wood Sales Proceeds for the option(s) they have chosen less costs and any unpaid expenses applicable to that particular Grower.

## **Fees**

27. The Application Fee payable under the Management Agreement is \$4,400 (including GST). There will be no ongoing fees for rent or maintenance charges. A single fee for sales commission, planting, lease and maintenance will be payable at year 9 (i.e. at the time of thinning) as well as at the end of the 13 or 20 year option period. The fee will equal 12% (inclusive of GST) of the sale proceeds from the Woodlot.

28. A pruning fee will be payable for Option 2 in years 4 (\$736), 6 (\$788) and 7 (\$840) (inclusive of GST). These base-line costs will be increased in-line with CPI.

29. The Application Fee will be banked into the relevant Applications Portion Account for the respective planting option chosen by the grower. These monies will be released to Gunns Plantations when certain specified criteria have been met (clause 8 and 9 of the Constitution).

## **Establishment and maintenance of the plantation**

30. Gunns Plantations has the capacity and resources to carry out the establishment program in accordance with clause 4.1(b) of the Management Agreement. Gunns Plantations will maintain the trees in accordance with good silvicultural practice. The services to be provided by Gunns Plantations over the term of the Project are defined in clauses 4, 5 and 6 of the Management Agreement. Gunns Plantations will also be responsible for the maintenance of access roads and fire breaks, and is required to keep the Woodlots free from vermin.

**Harvesting and Sale**

31. Gunns Plantations will also be responsible for arranging the sale of the timber produce (clause 11.1 of the Management Agreement). The time for harvest will vary depending on the option selected and will be determined according to set criteria including growth rates, market demand, and volume of wood on the Woodlot (clauses 7 and 9 of the Management Agreement). Gunns Plantations will provide ongoing reports to the Growers on the progress of the plantation.

32. Gunns Plantations will ensure that the gross Wood Sale Proceeds of each option are paid into the relevant portion of the Fund. The Growers' proportional shares of the costs of felling and costs of sale will be paid to Gunns Plantations from the gross Wood Sale Proceeds. Gunns Plantations will receive from the Wood Proceeds Portion Account an amount equal to 12% (inclusive of GST) of the gross Wood Sale Proceeds, as sales commission, planting, rental and maintenance. This percentage has been calculated to ensure that Gunns Plantations makes a profit in providing these services. The balance of the Wood Sale Proceeds for each option will be held by the Custodian on trust for the Growers.

**Finance**

33. Growers can choose to fund their investment themselves, borrow from an unassociated lending body or can fund their involvement in the Project by borrowing from Gunns Finance Pty Ltd (GFPL) (a lender associated with the Responsible Entity). All cash payable at the time of application shall be delivered by an applicant directly to the Responsible Entity (R/E) or Custodian. The R/E shall ensure monies will be banked into the Applications Portions account.

34. The following dates apply only to Growers who enter into the arrangement on or before 30 June 2003. The dates are adjusted accordingly for Growers who enter into the arrangement after 30 June 2003. There is a range of finance packages to be offered by GFPL, all will be on commercial terms. Some common aspects contained in these finance arrangements are:

- Security is held by mortgage over the interest in the project in all finance arrangements.
- Growers pay an Application Fee of \$150 depending on the finance arrangements entered into.

- For interest bearing loans (other than the 9 year principal and interest loan), after the first 5 years the interest rate is reviewed, and is reviewed every 5 years thereafter, and set at 4% above the ANZ Banking Group Ltd's 5 year swap reference rate.
- Additional interest per annum applies to overdue repayments.

The features of the range of finance arrangements Growers may enter into are as follows:

### **Standard Finance Package features:**

#### **Principal only loan**

- Growers will also be entitled to elect to enter into a non-interest bearing loan with GFPL.
- Growers who enter into this finance arrangement will be required to pay a 10% deposit and make 12 equal monthly instalments for the balance.

#### **Principal and interest loans (3, 4 or 5 year term)**

- Initial deposit equal to 20% (\$880) of the Application Fee.
- Interest rate of 10%.
- Interest payments will commence in July 2003.

#### **5 year principle and interest with balloon payment**

- Initial deposit equal to 10% (\$440) of the Application Fee.
- Investors pay a further 20% of the Application Fee by 30 Sept 2003.

### **Non – standard finance arrangements:**

#### **Purple Finance Package (9 Year Principal & Interest Loan) features:**

- Initial deposit of 20% (\$880) of Application Fee paid by the Grower, with an interest rate of 10%. Repayments are to be made monthly.

#### **Blue Finance Package**

- Initial deposit of 50% (\$2,200) of application fee applies.
- Interest only payments, in advance, are due and payable on the last day of June in each year.

- Interest rate of 9.9% applies.
- Repayments of principal in Option 1 occur in 2012 and 2016, for Option 2, 2012 and 2023 respectively.

**Platinum Finance Package**

- An initial deposit of 20% (\$880) of application fee applies.
- Interest only repayments (in arrears) 60 equal instalments commence on the last day of July 2003. This repayment plan is followed by Principal and interest repayments in 60 equal instalments. An interest rate of 10% applies.
- The term of the loan is 10 years.

**Red Finance Package**

- An initial deposit of 10% (\$440) of application fee applies.
- Investors pay a further 20% by 30 September 2003.
- The interest rate of 10% applies.
- For Options 1 & 2, repayments of outstanding principal are due in 2012. Interest only repayments (monthly in arrears).
- Term of loan 9 years.

35. 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, other than Gunns Finance Pty Ltd are involved or become involved in the provision of finance to Growers for the Project.

## Ruling

---

### Application of this Ruling

36. This Ruling applies only to Growers who are accepted to participate in the Project on or before 30 June 2004 and who have executed a Management Agreement and a Lease Agreement on or before that date. The Grower's participation in the Project must constitute the carrying on of a business of primary production.

37. 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*

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

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

### Qualification

39. 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***

40. 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.

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

#### **Deductions for Application fee and Interest**

##### ***Section 8-1***

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

<b>Fee Type</b>	<b>ITAA 1997 Section</b>	<b>Year ended 30 June 2003</b>	<b>Year ended 30 June 2004</b>	<b>Year ended 30 June 2005</b>
<b>Application Fee</b>	8-1	\$4,400 See Notes (i) & (ii) below		
<b>Interest on loans with GFPL</b>	8-1	As incurred See Note (iii) below	As incurred See Note (iii) below	As incurred See Note (iii) 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 1 at paragraph 119.
- (ii) Expenditure for ‘seasonally dependent agronomic activities’ is deductible in the income year in which it is incurred.
- (iii) The deductibility or otherwise of interest arising from loan agreements entered into with financiers other than GFPL, the internal financier, is outside the scope of this Ruling. However all Growers, including those who finance their participation in the Project other than with



Gunns Finance Pty Ltd, should read the discussion of the prepayment rules in paragraphs 71 to 78 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant loan agreement or is at the Grower's choice.

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

#### **Assessable Income**

##### ***Section 6-5 and section 328-105***

43. 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.

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

#### **Deductions for Application fee and Interest**

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

45. A Grower who is an 'STS taxpayer' may claim tax deductions for the revenue expenses in the following Table.

46. However, if, for any reason, an amount shown in the Table 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 below which is not paid in the year in which it is incurred will be deductible in the year in which it is actually paid.

<b>Fee Type</b>	<b>ITAA 1997 Section</b>	<b>Year ended 30 June 2003</b>	<b>Year ended 30 June 2004</b>	<b>Year ended 30 June 2005</b>
<b>Application Fee</b>	8-1 & 328-105	\$4,400 See Notes (iv) & (v) below		
<b>Interest on loans with GFPL</b>	8-1 & 328-105	When paid See Note (vi) below	When paid See Note (vi) below	When paid See Note (vi) below

**Notes:**

- (iv) 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). See Example 1 at paragraph 119.
- (v) Expenditure for 'seasonally dependent agronomic activities' is deductible in the income year in which it is incurred.
- (vi) The deductibility or otherwise of interest arising from loan agreements entered into with financiers other than GFPL, the internal financier, is outside the scope of this Ruling. However all Growers, including those who finance their participation in the Project other than with GFPL, should read the discussion of the prepayment rules in paragraphs 71 to 78 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant loan agreement or is at the Grower's choice.

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

47. For a Grower who is an individual and who enters the Project during the year ended 30 June 2003 the rule in section 35-10 may apply to the business activity comprised by their involvement in this Project. Under paragraph 35-55(1)(b) the Commissioner will decide for the income years ending 30 June 2003 to 30 June 2015 (Option 1) and for the income years ending 30 June 2003 to 30 June 2022 (Option 2) 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.

48. For a Grower who is an individual and who enters the Project on or after 1 July 2003 (i.e. during the year ended 30 June 2004) 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 2004 to 30 June 2016 (Option 1) and for the years ending 30 June 2004 to 30 June 2023 (Option 2) 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.

49. 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 97 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
- a 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)).

50. 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, ie., 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.

51. 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) 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.

### ***Section 82KL, and Part IVA***

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

- 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?

53. For the amounts set out in the Tables above to constitute allowable deductions the Grower's afforestation activities as a participant in the Gunns Plantations Woodlot Project 2003 must amount to the carrying on of a business of primary production.

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

55. For schemes such as that of the Gunns Plantations Woodlot Project 2003, Taxation Ruling TR 2000/8 sets out in paragraph 89 the circumstances in which the Grower's activities can constitute the carrying on of a business. As Taxation Ruling TR 2000/8 sets out, these circumstances have been established in court decisions such as *FCT v Lau* 84 ATC 4929; (1984) 16 ATR 55.

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

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

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

58. Under the Lease Agreement each individual Grower will have rights over a specific and identifiable area of one hectare of land. The Lease Agreement provides the Grower with an ongoing interest in the specific trees on the leased area for the term of the Project. Under the lease the Grower must use the land in question for the purpose of carrying out afforestation activities, and for no other purpose. The

lease allows the Project Manager come onto to the land to carry out its obligations under the Management Agreement.

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

60. The Project Manager is also engaged to harvest and sell, on the Grower's behalf, the wood produce grown on the Grower's Woodlot.

61. 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.

62. The activities that will be regularly carried out during the term of the Project demonstrate a significant commercial purpose. Based on reasonable projections, a Grower in the Project will derive assessable income from the sale of the wood produce that will return a before-tax profit, i.e. a profit in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

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

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

65. The Grower's degree of control over the Project Manager as evidenced by the Management Agreement, and supplemented by the *Corporations Act 2001*, is sufficient. During the term of the Project, the Manager will provide the Grower with regular progress reports on the Grower's Woodlot and the activities carried out on the Grower's behalf. Growers are able to terminate arrangements with the Project Manager in certain instances, such as cases of default or neglect.

66. The afforestation activities, and hence the fees associated with their procurement, are consistent with an intention to commence regular activities that have an 'air of permanence' about them. For the purposes of this Ruling, the Growers' afforestation activities in the Gunns Plantations Woodlot Project 2003 will constitute the carrying on of a business.

## **The Simplified Tax System**

### ***Division 328***

67. 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.

68. 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 application fee**

### ***Section 8-1***

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

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

70. The application fee associated with the afforestation activities will relate to the gaining of income from the Grower's business of afforestation (see above), and hence have a sufficient connection to the operations by which income (from the harvesting and sale of wood produce) is to be gained from this business. 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 application fee. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

**Prepayment provisions*****Sections 82KZL to 82KZMG***

71. 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 pruning of trees under Option 2) 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.

72. For this Project, only section 82KZL (an interpretive provision) and sections 82KZME, 82KZMF and 82KZMG are relevant. Subject to section 82KZMG, if 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 them from the operation of section 82KZMF.

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

73. Other than expenditure deductible under section 82KZMG, if 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)).

74. 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
- 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.

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

76. 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.

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

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

78. 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.

### ***Section 82KZMG***

79. Under section 82KZMG(1), expenditure is excluded from the prepayment rules that would otherwise apply, to the extent that the prepaid amount satisfies the requirements of subsections 82KZMG(2) to (4).



80. Subsection 82KZMG(2) requires that the expenditure is
- incurred on or after 2 October 2001 and on or before 30 June 2006;
  - the eligible service period must be 12 months or shorter and must end on or before the last day of the year of income after the expenditure year; and
  - for the doing of a thing under the agreement that is not to be wholly done within the expenditure year.
81. To satisfy subsection 82KZMG(3) the agreement must satisfy the following requirements:
- it must be an agreement for planting and tending trees for felling;
  - be an agreement where the taxpayer does not have day to day control over the operations arising out of the agreement. (a right to be consulted or to give directions does not equate to day to day control for the purposes of this requirement); and
  - either:
    - (i) there is more than one participant in the agreement in the same capacity as the taxpayer; or
    - (ii) the manager manages, arranges or promotes the agreement, or an associate of the manager, manages, arranges or promotes similar agreements.
82. Under subsection 82KZMG(4) the expenditure incurred by the taxpayer must be paid for ‘seasonally dependent agronomic activities’ undertaken by the manager during the ‘establishment period’ for the relevant planting of trees for felling.
83. Subsection 82KZMG(5) defines the ‘establishment period to commence at the time that the first ‘seasonally dependent agronomic activity’ is performed in relation to a specific planting of trees and to conclude with the planting of trees. Where it is necessary to apply a fertiliser or herbicide to the trees at the same time as planting then those activities fall within the establishment period. Planting of trees refers to the main planting of the particular plantation and expressly excludes specific planting to replace existing seedlings that have not survived.

**Application of the prepayment provisions to this Project**

84. Under the Management Agreement, a Grower incurs an Application Fee consisting of expenditure of \$4,400 for 'seasonally dependent agronomic activities'. The Management Agreement also requires that a Grower incurs Pruning Fees (in Option 2) and 12% (inclusive of GST) will be deducted from the Grower's entitlements to Wood Sale Proceeds for sales commission and the performance of maintenance services, planting and lease fee during the term of the Project.

85. The Management Agreement also requires that the Manager provide the Establishment & Planting Services in accordance with good silvicultural practice. The 'seasonally dependent agronomic activities' that will be carried out by the Manager on the Grower's behalf during the 'establishment period' include all ploughing and cultivation required for the purpose of planting the seedlings, including the procuring of those seedlings. These activities are to be completed before 12 months from the date the Application Fee is paid or the Manager is first permitted under the Forestry Right Deed to access the land for the purposes of commencing the Establishment & Planting Services, whichever is the later. However, if that period would extend beyond 30 June of the financial year immediately following the year in which the Application Fee is paid, the Establishment & Planting Services are to be completed by that 30 June.

86. As the requirements of section 82KZMG have been met, a deduction is allowable in the income year ended 30 June 2003 for the expenditure incurred under the Management Agreement for 'seasonally dependent agronomic activities'.

**Interest deductibility*****Section 8-1***

*(i) Growers who use Gunns Finance Pty Ltd as the finance provider AND who enter into Gunns Finance Pty Ltd finance arrangements that have been provided to the ATO*

87. Some Growers may finance their participation in the Project through a loan facility with Gunns Finance Pty Ltd. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of lease and management fees.

88. The interest incurred for the year ended 30 June 2003 and in subsequent years of income will be in respect of a loan to finance the Grower's business operations - the cultivation and growing trees and the lease of the land on which the trees will have been planted - that

will continue to be directly connected with the gaining of 'business income' from the Project. Such interest will, therefore, have a sufficient connection with the gaining of assessable income to be deductible under section 8-1.

89. As with the application fee, in the absence of any application of the prepayment provisions (see paragraphs 71 to 78), the timing of deductions for interest will again depend upon whether a Grower is an 'STS taxpayer' or is not an 'STS taxpayer'.

90. If the Grower is not an 'STS taxpayer', interest is deductible in the year in which it is incurred.

91. If the Grower is an 'STS taxpayer' interest is not deductible until it has been both incurred and paid, or is paid for the Grower. If interest that is properly incurred in an income year remains unpaid at the end of that income year, the unpaid amount is deductible in the income year in which it is actually paid, or is paid for the Grower.

*(ii) Growers who DO NOT use Gunns Finance Pty Ltd as the finance provider OR who enter into Gunns Finance Pty Ltd finance arrangements that have not been provided to the ATO*

92. The deductibility of interest incurred by Growers who finance their participation in the Project through a loan facility with a bank or financier other than GFPL is outside the scope of this Ruling. Product Rulings only deal with arrangements where all details and documentation have been provided to, and examined by the Tax Office.

93. While the terms of any finance agreement entered into between relevant Growers and such financiers are subject to commercial negotiation, those agreements may require interest to be prepaid. Alternatively, a Grower may choose to prepay such interest. Unless such prepaid interest is 'excluded expenditure' any tax deduction that is allowable will be subject to the prepayment provisions of the ITAA 1936 (see paragraphs 71 to 78).

## **Deferral of losses from non-commercial business activities**

### ***Division 35***

94. 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.

95. 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.

96. 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.

97. 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.

98. 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).

99. A Grower who participates in the Project under Option 1 will be carrying on a business activity that is subject to these provisions. Information provided with the application for this Product Ruling indicates that a Grower who acquires the minimum allocation of one Woodlot in the Project under Option 1 for either the year ended 30 June 2003 or 30 June 2004 is unlikely to have their activity pass one of the tests.

100. A Grower who participates in the Project under Option 2 will be carrying on a business activity that is subject to these provisions. Information provided with the application for this Product Ruling indicates that a Grower who acquires the minimum allocation of one Woodlot in the Project under Option 2 for either the year ended 30 June 2003 or 30 June 2004 is unlikely to have their activity pass one of the tests.

101. 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.

102. 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 the business activity has started to be carried on and for that, or those income years:

- because of its nature, the business activity has not satisfied, or will not satisfy one of the tests set out in Division 35; and
- 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.

103. Information provided with this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot, Option 1, in the Project on or before 30 June 2003 is expected to be carrying on a business activity that will produce a taxation profit, for the income years ended 30 June 2012 and 30 June 2016.

104. The Commissioner will decide for such a Grower that it would be reasonable to exercise the second arm of the discretion for all income years up to, and including the income year ended 30 June 2015. The taxation profit that is projected for the income year ended 30 June 2012 does not affect the period of the Commissioner's discretion as it is considered to be a 'one-off' event that is specific to the afforestation industry.

105. Information provided with this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot, Option 1, in the Project on or after 1 July 2003 is expected to be carrying on a business activity that will produce a taxation profit for the income years ended 30 June 2013 and 30 June 2017.

106. The Commissioner will decide for such a Grower, in Option 1, that it would be reasonable to exercise the second arm of the discretion for all income years up to, and including the income year ended 30 June 2016. The taxation profit that is projected for the income year ended 30 June 2013 does not affect the period of the Commissioner's discretion as it is considered to be a 'one-off' event that is specific to the afforestation industry.

107. Information provided with this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot, Option 2, in the Project on or before 30 June 2003 is expected to be carrying on a business activity that will produce a taxation profit, for the income years ended 30 June 2012 and 30 June 2023.

108. The Commissioner will decide for such a Grower, in Option 2, that it would be reasonable to exercise the second arm of the discretion for all income years up to, and including the income year ended 30 June 2022. The taxation profit that is projected for the income year ended 30 June 2012 does not affect the period of the Commissioner's discretion as it is considered to be a 'one-off' event that is specific to the afforestation industry.

109. Information provided with this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot, Option 2, in the Project on or after 1 July 2003 is expected to be carrying on a business activity that will produce a taxation profit, for the income years ended 30 June 2013 and 30 June 2024.

110. The Commissioner will decide for such a Grower, in Option 2, that it would be reasonable to exercise the second arm of the discretion for all income years up to, and including the income year ended 30 June 2023. The taxation profit that is projected for the income year ended 30 June 2013 does not affect the period of the Commissioner's discretion as it is considered to be a 'one-off' event that is specific to the afforestation industry.

111. 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 47), in the manner described in the Arrangement (see paragraphs 14 to 35). 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.

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

- the report of the independent forester and additional expert or scientific evidence provided with the application by the Responsible Entity;
- the Draft Wood Sale contract with Gunns Limited for the sale of the wood produce setting out prices that realistically reflect the existing market and/or the projected market in the geographical region where the wood produce is grown; and
- independent, objective, and generally available information relating to the afforestation industry which substantially supports cash flow projections and other claims, including prices and costs, in the Product Ruling application submitted by the Responsible Entity.

## **Section 82KL - recouped expenditure**

113. Section 82KL is a specific anti-avoidance provision that operates to deny an otherwise allowable deduction for certain expenditure incurred, but effectively recouped, by the taxpayer. Under subsection 82KL(1), a deduction for certain expenditure is disallowed where the sum of the ‘additional benefit’ plus the ‘expected tax saving’ in relation to that expenditure equals or exceeds the ‘eligible relevant expenditure’.

114. ‘Additional benefit’ (see the definition of ‘additional benefit’ at subsection 82KH(1) and paragraph 82KH(1F)(b)) is, broadly speaking, a benefit that is additional to the benefit for which the expenditure is ostensibly incurred. The ‘expected tax saving’ is essentially the tax saved if a deduction is allowed for the relevant expenditure.

115. Section 82KL’s operation depends, among other things, on the identification of a certain quantum of ‘additional benefits’. Here, there may be a loan provided to the Grower’s. The loan will be provided on a full recourse basis, and on commercial terms. Insufficient ‘additional benefits’ will be provided in respect of this Project, to trigger the application of section 82KL. It will not apply to deny the deductions otherwise allowable under section 8-1.

**Part IVA - general tax avoidance provisions**

116. 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).

117. The Gunns Plantations Woodlot Project 2003 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 42 and 45 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.

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

**Example****Example 1 - Entitlement to GST input tax credits**

119. 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 2002, 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 1/1/2003 to 30/6/2003	\$4,400*
Carrying out of upgrade of power for your vineyard as quoted	<u>\$2,200*</u>
Total due and payable by 1 January 2003 (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:

$$\frac{1}{11} \times \$4,400 = \$400.$$

Hence her outgoing for the management fee is effectively \$4,400 *less* \$400, or \$4,000.

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

$$\frac{1}{11} \times \$2,200 = \$200.$$

Hence her outgoing for the power upgrade is effectively \$2,200 *less* \$200, or \$2,000.

In preparing her income tax return for the year ended 30 June 2003, Susan is aware that the management fee is deductible in the year incurred. She calculates her management fee deduction as \$4,000 (not \$4,400).

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 \$2,000 only, not one tenth of \$2,200).

## **Detailed contents list**

---

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

	<b>Paragraph</b>
<b>What this Product Ruling is about</b>	<b>1</b>
Tax law(s)	2
Goods and Services Tax	3
Changes in the Law	4
Note to promoters and advisers	6
Class of persons	7
Qualifications	9
<b>Date of effect</b>	<b>11</b>
<b>Withdrawal</b>	<b>13</b>
<b>Arrangement</b>	<b>14</b>
Overview	17
Constitution	20
Compliance plan	21

Interest in Land	22
Management Agreement and Lease of Forestry Right	23
Fees	27
Establishment and maintenance of the plantation	30
Harvesting and Sale	31
Finance	33
<b>Ruling</b>	<b>36</b>
Application of this Ruling	36
The Simplified Tax System ('STS')	38
<i>Division 328</i>	38
Qualification	39
Tax outcomes for Growers who are not 'STS taxpayers'	40
Assessable income	40
<i>Section 6-5</i>	40
Deductions for Application fee and Interest	442
<i>Section 8-1</i>	442
Tax outcomes for Growers who are 'STS taxpayers'	43
Assessable income	43
<i>Section 6-5 and section 328-105</i>	43
Deductions for Application fee and Interest	45
<i>Section 8-1 and section 328-105</i>	45
Tax outcomes that apply to all Growers	47
Deferral of losses from non-commercial business activities	47
Division 35	47
<i>Section 35-55 – Commissioner's discretion</i>	47
<i>Section 82KL and Part IVA</i>	52
<b>Explanations</b>	<b>53</b>
Is the Grower carrying on a business?	53
The Simplified Tax System	67
<i>Division 328</i>	67
Deductibility of application fee	69
<i>Section 8-1</i>	69
Prepayment provisions	71

<i>Sections 82KZL – 82KZMG</i>	71
<i>Sections 82KZME - 82KZMF</i>	73
<i>Section 82KZMG</i>	79
Application of the prepayment provisions to this Project	84
Interest deductibility	87
<i>Section 8–1</i>	87
<i>(i) Growers who use Gunns Finance Pty Ltd as the finance provider AND who enter into Gunns Finance Pty Ltd finance arrangements that have been provided to the ATO</i>	87
<i>(ii) Growers who DO NOT use Gunns Finance Pty Ltd as the finance provider OR who enter into Gunns Finance Pty Ltd finance arrangements that have not been provided to the ATO</i>	92
Deferral of losses from non-commercial business activities	94
Division 35	94
Section 82KL – recouped expenditure	113
Part IVA – general tax avoidance provisions	116
<b>Example</b>	<b>119</b>
Example 1 – Entitlement to GST input tax credits	119
<b>Detailed Contents List</b>	<b>120</b>

**Commissioner of Taxation**

7 May 2003

<i>Previous draft:</i>	- product rulings
Not previously issued in draft form	- public rulings
	- seasonally dependent agronomic activity
<i>Related Rulings/Determinations:</i>	- taxation administration
TR 92/1; TR 92/20; TD 93/34;	- tax avoidance
TR 97/11; TR 97/16; TR 98/22;	- tax benefits under tax avoidance schemes
PR 1999/95; TR 2000/8; IT 360	- tax shelters
<i>Subject references:</i>	- tax shelters project
- advance deductions and expenses for certain forestry expenditure	
- carrying on a business	<i>Legislative references:</i>
- commencement of business	- ITAA 1936 82KH(1)
- fee expenses	- ITAA 1936 82KH(1F)(b)
- forestry agreement	- ITAA 1936 82KL
- interest expenses	- ITAA 1936 82KZL
- management fees	- ITAA 1936 82KZL(1)
- producing assessable income	- ITAA 1936 82KZME

- ITAA 1936 82KZME(1)
- ITAA 1936 82KZME(2)
- ITAA 1936 82KZME(3)
- ITAA 1936 82KZME(4)
- ITAA 1936 82KZME(7)
- ITAA 1936 82KZMF
- ITAA 1936 82KZMF(1)
- ITAA 1936 82KZMG
- ITAA 1936 82KZMG(1)
- ITAA 1936 82KZMG(2)
- ITAA 1936 82KZMG(3)
- ITAA 1936 82KZMG(4)
- ITAA 1936 82KZMG(5)
- ITAA 1936 Pt IVA
- ITAA 1936 Div 3 Pt III
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)
- ITAA 1997 6-5
- ITAA 1997 8-1
- ITAA 1997 17-5
- ITAA 1997 Div 27
- 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 Div 328
- ITAA 1997 328-105
- ITAA 1997 328-105(1)(a)
- ITAA 1997 Subdiv 328-F
- ITAA 1997 Subdiv 328-G
- TAA 1953 Pt IVAAA
- Copyright Act 1968
- Corporations Act 2001

*Case references:*

- FCT v. Lau 84 ATC 4929; (1984)  
16 ATR 55

## ATO references

NO: 2003/001900  
ISSN: 1441-1172