PR 2003/30 - Income tax: Brooklyn Park Organic Olive Groves Project No. 3

Product Ruling
Income tax: Brooklyn Park Organic Olive Groves Project No. 3

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Preamble

*The number, subject heading, and the **What this Product Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Withdrawal**, **Previous Ruling (optional heading required)**, **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.

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 investment fits an existing portfolio, etc. We recommend a financial (or other) adviser be consulted for such information.

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

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

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

Terms of use of this Product Ruling

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 Brooklyn Park Organic Olive Groves Project No. 3, 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);
- Part 3-1 (ITAA 1997);
- section 44 of the *Income Tax Assessment Act 1936*
- (ITAA 1936);
- section 82KL (ITAA 1936);
- section 82KZL (ITAA 1936);
- section 82KZME (ITAA 1936);
- section 82KZMF (ITAA 1936); and
- Part IVA (ITAA 1936).

Goods and Services Tax

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

Changes in the Law

4. The Government is currently evaluating further changes to the tax system in response to the Ralph *Review of Business Taxation* and continuing business tax reform is expected to be implemented over a number of years. Although this Ruling deals with the taxation legislation enacted at the time it was issued, later amendments may impact on this Ruling. Any such changes will take precedence over the application of this Ruling and, to that extent, this Ruling will be superseded.

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

Note to promoters and advisers

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

Class of persons

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

8. The class of persons to whom this Ruling applies does not include persons:

- who do not enter into a Management Agreement with the Manager but elect to maintain their Allotments themselves or through an approved contractor;
- who, under Clause 6 of the Management Agreement, elect to harvest their own Allotments or have the Manger harvest their Allotments separately or elect to retain the Olives from their Allotment for marketing and selling by the Grower themselves; or
- who intend to terminate their involvement in the arrangement prior to its completion or who otherwise do not intend to derive assessable income from it.

Qualifications

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

10. A Product Ruling may only be reproduced in its entirety. Extracts may not be reproduced. As each Product Ruling is copyright, apart from any use as permitted under the *Copyright Act 1968,* the Product Ruling cannot be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to:

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Date of effect

11. This Ruling applies prospectively from 28 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 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 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 person's involvement in the arrangement.

Arrangement

14. The arrangement that is the subject of this Ruling is described below. The relevant documents or parts of documents incorporated into this description of the arrangement are:

- Application for a Product Ruling dated 16 December 2002 as constituted by documents provided on 15 January 2003, 27 February 2003, 4 March 2003 and 25 March 2003 and additional correspondence dated 3 April 2003, 15 April 2003. 22 April 2003, 30 April 2003, 8 May 2003, 14 May 2003 and 15 May; 2003;
- Draft Prospectus for Brooklyn Park Organic Olive Groves Limited Stage III dated 20 March 2003;
- Constitution of Brooklyn Park Olive Groves Limited;
- Brooklyn Park Olive Groves Scheme Constitution dated 7 June 1999 and deed polls of Brooklyn Park Olive Groves Limited dated 8 February 2001 and 22 April 2003;
- Registered Compliance Plan for the Brooklyn Park Olive Groves Managed Investment Scheme;
- Draft **Management Agreement** between Australian Green and Gold Limited (as the Manager) Brooklyn Park Olive Groves Limited and the Grower, dated 13 March 2003;
- Draft **Licence to Occupy Agreement** between Brooklyn Park Olive Groves Limited and the Grower, dated 13 March 2003;
- Executed Loan Agreement between Brooklyn Park Olive Groves Limited (the borrower) and the Lender, dated 15 May 2000;
- Registered lease between Brooklyn Park Olive Groves Limited and TEYS Custodians Limited;
- Registered Sublease between TEYS Custodians Limited and Brooklyn Park Olive Groves Limited;

- Olive Procurement Agreement between Australian Green and Gold Limited and Inglewood Olive Processors Limited, dated 7 June 1999; and
- Executed Brooklyn Park Olive Groves **Water and Services Agreement** dated 7 June 1999.

NOTE: Certain information received from the applicant 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 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 Investment Commission (ASIC) requirements are, or will be, complied with for the term of the agreements. The effect of these agreements may be summarised as follows.

Overview of the Project

17. The salient features of the Brooklyn Park Organic Olive Groves Project No. 3 are.

Location	The Darling Downs Region of Queensland
Type of business each participant is carrying on	Commercial growing of olives for domestic and international sale
Number of hectares under cultivation	150 hectares
Size of each Allotment	0.2 hectares
Number of trees per Hectare	400
Number of trees per Allotment	80
Term of the Project	Approximately 18 years
Initial costs per Allotment	$16,950 for the first three years comprising $15,950 in the Project and $1,000 for shares in Brooklyn Park Olive Groves Limited
Initial costs per	$84,750

hectare	
Ongoing costs	Management Fees as a set percentage of gross harvest proceeds and annual Licence Fees increased by CPI

18. The Project will be a registered managed investment scheme under the *Corporations Act 2001*. Offers for interests in the Project will be made under a prospectus. Applicants that are accepted to participate in the Project will carry on a business of commercially growing olives for domestic and international sale. There is no minimum subscription for the Project, however, there is a maximum subscription of 750 interests. The Project will terminate on 30 June 2020, a period of approximately 18 years.

19. The Project will be situated at Brooklyn Park, a property approximately 22km west of Inglewood in the Darling Downs region of southern Queensland. Brooklyn Park Olive Groves Limited owns the Brooklyn Park property which is leased to TEYS Custodians Limited (the 'Custodian'). The Custodian holds this interest as Head Lessee for the security of the Growers. The property is sub-leased back to Brooklyn Park Olive Groves Limited for administration of the Project.

20. Growers accepted to participate in the Project will enter a Licence to Occupy Agreement with Brooklyn Park Olive Groves Limited in its capacity as lessee of the property. A Grower acquiring a single interest in the Project will hold a licence over a separate and distinct area (called an 'Allotment') of 0.2 hectare on which the Grower can plant and maintain 80 olive trees. Each Allotment will be separately identifiable on a plan prepared by Brooklyn Park Olive Groves Limited for that purpose.

21. Growers may acquire more than one Interest in the Project. However, for each Interest acquired the Grower must first apply for and be allotted a parcel of 1,000 $1 shares in Brooklyn Park Olive Groves Limited, the company that owns the land upon which the Allotments will be situated.

22. Growers will also have an option to enter into a Management Agreement with Australian Green & Gold Limited ('the Manager') whereby

the Manager will establish and maintain each Allotment during the term of the Project.

23. Unless a Grower elects otherwise, the Manager will harvest the olives on their behalf and use its best endeavours to sell the produce at the best available price. The Manager holds a contract with Inglewood Olive Processors, to buy and market the produce.

Scheme constitution

24. Upon entering into a Management Agreement, Growers become bound by the provisions of the Brooklyn Park Olive Groves Scheme Constitution. The Constitution primarily sets out the rights, powers, duties and obligations of the Manager. The Manager, Australian Green and Gold Limited, is the Responsible Entity for the Project and will have the primary responsibility for managing the Project, ensuring compliance with the Corporations Law, the Scheme Constitution and the Management Agreement.

25. Among other things, the Constitution sets out procedures for dealing with:

- Applications for Interests (clause 3);
- the issue of Certificates relating to those Interests (clause 4);
- the Application Moneys (clauses 3 and 5);
- preparation and execution of the Scheme Agreements and the preparation of an Allotment Plan (clause 6);
- responsibilities, powers and duties of the Manager and its Employees and Officers (clauses 7 and 8);
- Termination of the Scheme and procedures for calling and holding meetings of Members; (clauses 12, and clauses 17 to 22);
- the establishment and maintenance of a Growers' Register and the right of Members to inspect and copy the Register of Members (clause 16); and
- the right of Members to remove the Manager and the consequences of that removal (clauses 27 and 28).

Compliance plan

26. The Compliance Plan for the Brooklyn Park Olive Groves Managed Investment Scheme

describes how the Responsible Entity will ensure its compliance with the Corporations Law and the Project Scheme Constitution. The Compliance Plan is designed to protect the rights of Growers.

Licence to Occupy Agreement

27. Each Grower enters into a Licence to Occupy Agreement (the 'Agreement') with Brooklyn Park Olive Groves Limited until 30 June 2020 (clause 2.2). Under the Agreement, Brooklyn Park Olive Groves Limited grants the Grower a Licence to Occupy an Allotment on the Project Land for the purpose of conducting the 'Business' (clause 6.1). 'Business' is defined as planting, growing, cultivating, harvesting and marketing olives for domestic and overseas sale.

28. Each Allotment is 0.20 hectare in size and will have 80 olive trees planted on it (clause 3.2). Each Grower's Allotment will be a distinct area of the Project Land and will be identified on an Allotment Plan to be maintained by Brooklyn Park Olive Groves Limited (clause 3.3). Each tree position will be numbered and shown in relation to the boundaries of the Project Land. This will enable Growers to identify their individual Allotment and tree holding. Brooklyn Park Olive Groves Limited will advise Growers of the location of their individual Allotment(s).

29. The Agreement places certain obligations on the Grower to maintain the Allotment and use it in a certain manner (clause 4). It also permits the Grower to use dams, irrigation systems, roads and other infrastructure located on the Project Land (clause 2.3).

30. The Grower is required to pay an annual Licence Fee for each year of the Agreement. The Fee is $22 per year for the first 3 years (clause 7). From the fourth year onwards, the annual Fee will equal the Fee of the preceding year indexed by the All Groups Consumer Price Index for Brisbane ('CPI') in accordance with the formula in clause 7.2.

31. Under the Agreement the Grower will pay all telephone, garbage, waste, electric light and power charges levied against the Land or the Allotment in respect of the Grower's use of the Allotment to conduct the Business. Brooklyn Park Olive Groves Limited will pay for

all charges and assessments levied on the Allotment, including water and municipal rates (clause 8).

32. The Agreement allows the Grower to delegate the conduct of all or part of the Business to the Manager or an approved contractor (clause 11). As a consequence, the Agreement allows delegates of the Grower to enter upon the Allotment for the purpose of conducting the Grower's Business (clause 9.4).

33. The Agreement may be terminated prior to 30 June 2020, where either party defaults or does not fulfil its obligations (clause 10). Growers are not entitled to assign the Licence, except as set out in Brooklyn Park Olive Groves' Constitution (clause 9.1).

34. Upon termination of the Agreement Growers are not required to remove the Trees or restore the Allotment to its original condition (Clause 10.4). However, the Grower must remove any item brought onto the Allotment or any improvement constructed on the Allotment (clause 10.5(a)).

35. Brooklyn Park Olive Groves Limited will be legally entitled to any trees growing on the Allotment and things brought onto the Allotment by the Grower that are not removed within 14 days following termination of the Agreement (clause 10.5(b)).

Management Agreement

36. Growers may elect to use the services of the Manager, Australian Green and Gold Limited, by entering into a Management Agreement. Growers that do not execute a Management Agreement with Australian Green and Gold are outside the scope of this Product Ruling and the taxation consequences of their participation in the Project are not dealt with in this Ruling. A Grower who does not enter into a Management Agreement with the Manager may request a private ruling on the taxation consequences of their participation in the Project.

37. The parties to the Management Agreement are the Grower, the Manager and Brooklyn Park Olive Groves Limited. The Management Agreement will terminate on 30 June 2020, subject to the valid terminations as set out in clause 16 of the Agreement.

38. Under the Management Agreement, the Manager undertakes to establish the 'Business' of the Grower, including the planting of trees, as soon as is reasonably practicable. These services will begin to be performed and carried out by the Manager on behalf of the Grower immediately after the Grower enters into the relevant agreements. It is anticipated that planting will commence soon after the acceptance of the Grower into the Project. The olive trees are expected to be ready for the first commercial harvesting in 2006.

39. The Manager must carry out its duties under the Agreement in a manner consistent with best agricultural practice. Clause 4.2 of the Management Agreement provides that the Manager will carry out the following duties:

- properly prepare the Allotment, including the performance of soil conservation, irrigation and drainage work on the Land to the benefit of the Allotment;
- cause at least 80 trees to be planted on the Allotment; and
- identify the Grower's trees with appropriate markings.

40. The Manager will also provide additional services to the Grower as set out in clauses 5.2 and 5.3:

- procuring, planting and tending the trees on the Allotment;
- minimising soil erosion and maintaining soil quality on the Allotment;
- keeping the Allotment free from vermin, vegetation, insects and diseases that might inhibit the growth of the trees;
- maintaining and cultivating the trees, including watering, weeding and applying fertilisers, nutrients and herbicides;
- procuring all necessary plant, equipment, machinery and materials;
- maintaining windbreaks, access roads and tracks; and
- harvesting the trees and marketing and selling the olives produced (subject to the Grower's right to make an election regarding these services).

41. The Manager guarantees survival of the Grower's trees to the commencement of the fourth year of the term of the Agreement. Thereafter, the Manager does not guarantee survival of the Grower's trees or that they will produce olives (clause 4.4).

42. Under the Management Agreement, Growers may elect not to use all the services provided by the Manager. Growers may elect to have the Manager harvest the trees on their Allotment separately (clause 6.1) or they may elect to harvest the trees on their Allotment themselves (clause 6.2). Growers may also elect to retain the olives harvested from their Allotment and market, sell or otherwise deal with as they see fit (clause 6.3). This Ruling will not apply to any Grower who makes an election under clauses 6.1, 6.2 or 6.3. A Grower who makes such an election may request a private ruling on the taxation consequences of their participation in the Project.

43. The Manager is entitled to delegate all or any of the functions to be performed by it under the Agreement (clause 20).

44. The Manager will pool the olives produced by the Grower's trees with those of each other Grower, and market and sell all such olives (clause 7.1). The proceeds of the sale of all olives will be paid to the Custodian, to be divided among all Growers. Subject to clause 7.3 the allocation of Gross Sales Proceeds to each Grower makes no reference to the quality, quantity, prices or to any other factor relating to the olives produced by the Grower's Allotment (clause 7.2).

45. Clause 7.3 provides that, where the quantity of olives from a Grower's Allotments is less than 90% of the average of olives harvested on all Grower's Allotments then the Grower's sale proceeds will be reduced by an amount determined by the Manager (clause 7.3).

46. The Custodian will establish an account for each Grower, to which the Grower's share of sale proceeds will be credited (clause 7.4). The Manager will account for the gross sale proceeds received and Management Fees payable and must provide each Grower with certain financial information in respect of the Grower's olives (clause 7.6). The Manager is also required to provide the Grower with various reports, including half yearly reports on the Management Services provided and the

progress and condition of the Allotment (clause 14).

47. Growers are not entitled to assign their rights or obligations under the Management Agreement, except in certain limited circumstances. Where a Grower's interest is assigned, the Grower will no longer be entitled to rely on this Ruling.

Grower Fees

48. For a Grower accepted into the Project the table below sets out the amounts payable, per Interest, upon Application.

Amount Payable	**Amount of Fee**
Part Payment of Shares	$200
Licence Fee	$22
Management Fee (Part Management fee for month 1)	$1,118.50
Landcare Operations	$2,049.50
Total payable on Application	**$3,390.00**

49. Other than the amount payable upon application, during the first 36 months of the Project Management Fees for each year are payable by 30 June of that year.

50. These Management Fees accrue on a monthly basis (referred to as a 'Grower Month') and relate wholly to services provided by the Manager and completed during the month. For each Interest held in the Project Growers incur the amounts set out in the table below. The amount payable for Management Fees on the 30 June of a particular year will vary according to the month that a Grower is accepted to participate in the Project.

Amount Payable	**Grower Month**	**Amount of Fee**
Supply & Plant Olive Trees	1	$412.50
Irrigation establishment costs	1	$1,464.00
Management Fee (balance of Initial Management fee – see	1	$5,575.50

Note below)		
Management Fee	2 to 12	$308.00
Management Fee	13 to 36	$78.17

Note: Total Management Fee for Month 1 is $6694, being $1,118.50 payable on application plus $5,575.50 payable by 30 June.

51. In the event that an applicant is accepted as a Grower after the 1st of the month (referred to as a 'Part Grower Month'), the Management Fees payable shall be calculated according to the following formula:

$$A = \frac{(B \times C)}{D} - E$$

Where :

A = the amount payable for Management Fees for the Part Grower Month

B = Number of days of the Part Grower Month up to 30 June

C = Management Fee payable for Month 1

D = 30

E = If the Part Grower Month is June – $1,118.50, otherwise NIL

52. It is the intention of the Manager that in all months, other than June, applications will be accepted and work will only be commenced on the 1st of the month following the application.

53. For Year 4 and subsequent years, the annual Management Fee will be calculated using the percentages (set out in the table below) of 'Gross Sale Proceeds' of the 'Olives' harvested in the immediately preceding financial year:

Year	Percentage
4	88%
5	77%
6	66%
7	55%
8 - termination	44%

Examples of Fees Payable by 30 June in Year of Application

54. **Example 1:** Grower joins the Project on 1st June 2003:

Shares	$200.00
Licence Fee	$22.00
Landcare Operation	$2,049.50
Irrigation Establishment	$1,464.00
Purchase and Planting Trees	$412.50
Management Fee	$6,694.00
Total Amount Payable for Year ended 30 June 2003	**$10,842.00**

55. **Example 2**: Grower joins the Project on 15th June 2003:

Shares	$200.00
Licence Fee	$22.00
Landcare Operation	$2,049.50
Irrigation Establishment	$1,464.00
Purchase and Planting Trees	$412.50
Management Fee (**see Note below**)	$2,228.50
Total Amount Payable for Year ended 30 June 2003	**$6,376.50**

Note: As the Grower has joined the Project part way through the month the Management Fee is calculated as follows:

$$A = \frac{(B \times C)}{D} - E$$

$$= \frac{(15 \times 6{,}694)}{30} - 1{,}118.50$$

$$= \$2{,}228.50$$

Where :

A = the amount payable for management fees for the Part Grower Month

B = 15, that is the number of days of the Part Grower Month up to 30 June

C = $6694, that is the total Management Fee payable for Month 1

D = 30

E = $1118.50 – as the Part Grower Month is June

56. **Example 3**: Grower joins the Project on 1st September 2004:

Shares	$200.00
Licence Fee	$22.00
Landcare Operation	$2,049.50
Irrigation Establishment	$1,464.00
Purchase and Planting Olive Trees	$412.50
Management Fee (see Note below)	$9,466.00
Total Amount Payable for Year ended 30 June 2004	**$13,614.00**

Note: The Management Fee consists of the following amounts:

On application
$1,118.50

By 30 June 2004

September (Balance of Month 1 fees)
$5,575.50

October to June (Month 2 to month 9 @ $308)
$2,772.00

Total Management Fee
$9,466.00

Licence Fee

57. In addition to the Management Fee a Grower is required to pay a $22 Licence Fee each year. From Year 4 onwards the Licence Fee will be increased annually by the amount of the CPI for the year.

Shares in Brooklyn Park Olive Groves Limited

58. For each Interest acquired in the Project a Grower must first apply for and be allotted shares in Brooklyn Park Olive Groves Limited, the landowning company. The minimum subscription for an investor is 1,000 shares of $1 each, with further applications to be made in parcels of 1,000 shares. For each Interest a part payment of $200 is payable on application. A further $400 will be payable on or before 30 June in the financial year following the Application. The remaining $400

is payable on or before 30 June in the next financial year.

Water and Services Agreement

59. Upon application, the Grower becomes a party to a Water and Services Agreement. The other parties to the Agreement are the owner of the property adjoining the Project Land ('the Supplier'), and the Manager. The effect of this Agreement will be to supplement the water supply and infrastructure available for the Project. Infrastructure refers to accommodation and administration buildings, machinery service sheds and storage sheds located on the adjoining property. Under this Agreement all fees are the responsibility of the Manager. No fees are payable by the Grower. The Term of the Agreement is 20 years.

Finance

60. There is no financing facility offered by the Manager or any other party to the arrangement. Growers can fund their investment in the Project themselves, or borrow from an independent lender. Regardless of the source of loan funds, this Ruling will not apply to Growers if the Manager accepts their Application subject to finance approval by a lending institution and the full amount payable at the time of Application, plus other moneys payable in the year of Application, are not paid to the Manager by 30 June in the year of Application.

61. This Ruling does not apply if a Grower enters into a finance agreement that includes or has any of the following features:

(a) there are split loan features of a type referred to in Taxation Ruling TR 98/22;

(b) there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;

(c) '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;

(d) the loan or rate of interest is non-arm's length;

(e) repayments of the principal and payments of interest are linked to the derivation of income from the Project;

(f) 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;

(g) lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; and

(h) 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

62. Subject to the exclusions set out in the Arrangement and the Class of Persons paragraphs, this Ruling applies only to Growers who are accepted to participate in the Project and who have executed a Management Agreement and a Licence to Occupy Agreement:

- on or before 15 June 2003; or
- on or after 1 July 2003 and on or before 15 June 2004.

This Ruling will not apply to Growers who are accepted to participate in the Project on or after 16 June 2003 and on or before 30 June 2003 or, on or after 16 June 2004 and on or before 30 June 2004.

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

64. For a Grower accepted to participate in the Project **on or before 15 June 2003** a reference to Years 1, 2, and 3 in the Tables below is a reference to deductions allowable the income years ended 30 June 2003, 30 June 2004 and 30 June 2005 respectively.

65. Alternatively, for a Grower accepted into the Project **on or after 1 July 2003 and on or before 15 June 2004** references to Years 1, 2 and 3 in the Tables below is a reference to the deductions allowable in the income years ended 30 June 2004, 2005 and 2006 respectively.

66. 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

67. For a Grower participating in the Project, the recognition of income and the timing of tax deductions will depend upon whether, in an income year(s), the Grower is an 'STS taxpayer' or is not 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

68. 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

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

70. The Grower recognises ordinary income from carrying on the business of olive growing at the time that income is derived.

Deductions for Management Fees and Licence Fees

Section 8-1

71. A Grower who is not an 'STS taxpayer' may claim, on a per Allotment basis, tax deductions for the following revenue expenses:

Fee type	ITAA 1997 Section	Year 1	Year 2	Year 3
Management fee	8-1	See Note (i) & (ii) below	See Note (i) & (ii) below	See Note (i) & (ii) below
Licence fee	8-1	$22 See Note (i) & (ii) below	$22 See Note (i) & (ii) below	$22 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 144; and

(ii) The amount of Management Fees incurred will depend upon the date the Grower is accepted into the Project. Where a Grower incurs the Management Fees and the Licence Fees as required by the Management Agreement and the Licence to Occupy Agreement those fees are deductible in full in the year incurred. (See paragraphs 54 to 56 for examples of how the Management Fees are calculated).

However, if a Grower chooses to prepay fees for the doing of things (e.g. the provision of management services or the leasing of land) that will not be wholly done in the same income year as the fees are incurred, then the prepayments 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 paragraphs 115 to 116 unless the expenditure is 'excluded expenditure'. 'Excluded expenditure', being expenditure of less than $1,000, is an 'exception' to any prepayment rules that apply and is deductible in full in the year in which it is incurred.

Tax deductions for capital expenditure

Division 40

72. A Grower who is not an 'STS taxpayer' will also be entitled to tax deductions relating to water facilities (e.g. irrigation), a 'landcare operation' and the establishment of the olive trees. All deductions shown on a per Allotment basis in the following Table are determined under Division 40

Fee type	Section of the ITAA 1997	Year 1	Year 2	Year 3
Landcare operations	40-630	$2,049.50 – see Note (iii) & (iv) below	Nil	Nil
Irrigation expenditure	40-515	$488– see Note (iii) & (v) below	$488– see Note (iii) & (v) below	$488– see Note (iii) & (v) below
Establishment of horticultural plants	40-515	Nil– see Note (vi) below	Nil– see Note (vi) below	Nil– see Note (vi) below

Notes:

(iii) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (e.g. input tax credits): Division 27. See Example at paragraph 144;

(iv) Any capital expenditure incurred for a 'landcare operation' (as defined in section 40-635) is fully deductible in the year it is incurred under Subdivision 40-G, section 40-630;

(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 installation 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); and

(vi) Olive trees are a 'horticultural plant' as defined in subsection 40-525(2). As Growers hold the land under a licence relating to the land, one of the conditions in subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the olive trees is determined using the formula in section 40-545 and is based on the capital expenditure incurred by the Grower that is attributable to their establishment. The olive trees have an 'effective life' of greater than 30 years for the purposes of section 40-545. This results in a straight-line write-off at a rate of 7%. The deduction is allowable when the olive trees enter their first commercial season (section 40-530, item 2). The Manager will inform Growers of when the olive trees enter their first commercial season.

Tax outcomes for Growers who are 'STS taxpayers'

Assessable Income

Section 6-5 and section 328-105

73. 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.

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

Deductions for Management fees and Licence fees

Section 8-1 and section 328-105

75. A Grower who may claim, on a per Allotment basis, the deductions for revenue expenses:

Fee type	ITAA 1997 Section	Year 1	Year 2	Year 3
Management fee	8-1 & 328-105	See Note (vii), (viii) & (ix) below	See Note (vii), (viii) & (ix) below	See Note (vii), (viii) & (ix) below

Licence fee	8-1 & 328-105	$22 See Note (vii), (viii) & (ix) below	$22 See Note (vii), (viii) & (ix) below	$22 See Note (vii), (viii) & (ix) below

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 144;

(viii) If, for any reason, an amount referred to or 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 referred to or shown in the Table above that 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 Management Fees and the Licence Fees as required by the Management Agreement and the Licence to Occupy Agreement those fees are deductible in full in the year in which they are paid. (See paragraphs 54 to 56 for examples of how the management fees are calculated.); and

(x) However, if a Grower chooses to prepay fees for the doing of things (eg the provision of management services or the leasing of land) that will not be wholly done in the same income year as the fees are incurred, then the prepayments 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 paragraphs 115 to 116 unless the expenditure is 'excluded expenditure'. 'Excluded expenditure', being expenditure of less than $1,000, is an 'exception' to any prepayment rules that apply and is deductible in full in the year in which it is incurred.

Tax deductions for capital expenditure

Subdivision 328-D and Subdivisions 40-F and 40-G

76. A Grower who is an 'STS taxpayer' will also be entitled to tax deductions relating to landcare operations, water facilities (e.g. irrigation) and olive trees. An 'STS taxpayer' may claim deductions in relation to landcare operations under Subdivision 40-G and water facilities expenditure under Subdivision 40-F. If the 'landcare operations' or 'water facility' expenditure is on a 'depreciating asset' used to carry on the business, they may choose to claim deductions under Division 328. Deductions for the olive trees establishment costs must be determined under Subdivision 40-F.

77. 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 landcare operations and water facilities under Subdivisions 40-F and 40-G 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.

78. Under Division 328, if the 'cost' of a 'depreciating asset' at the end of the income year is less than $1,000 (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	**ITAA 1997 Section**	**Year 1**	**Year 2**	**Year 3**
Landcare operations	40-630	$2,049.50 – see Note (x) & (xi) below	Nil	Nil
Irrigation expenditure	40-515	$488– see Note (x) & (xii) below	$488– see Note (x) & (xii) below	$488– see Note (x) & (xii) below
Establishment of horticultural plants	40-515	Nil– see Note (xiii) below	Nil– see Note (xiii) below	Nil– see Note (xiii) below

Notes:

(xi) 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 144;

(xii) Any capital expenditure incurred for a 'landcare operation' (as defined in section 40-635) is fully deductible in the year it is incurred under Subdivision 40-G, section 40-630. 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-G (although expenditure on some items of plant can only be deducted under Division 328). 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 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', the expenditure is fully deductible under Subdivision 40-G;

(xiii) 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 $1,000, 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 2003 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 installation 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); and

(xiv) Olive trees are a 'horticultural plant' as defined in subsection 40-525(2). As Growers hold the land under a Licence to Occupy, one of the conditions in subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the olive trees is determined using the formula in section 40-545 and is based on the capital expenditure incurred by the Grower that is attributable to their establishment. The olive trees have an 'effective life' of greater than 30 years for the purposes of section 40-545. This results in a straight-line write-off at a rate of 7%. The deduction is allowable when the olive trees enter their first commercial season (section 40-530, item 2). The Manager will inform Growers of when the olive trees enter their first commercial season.

Tax outcomes that apply to all Growers

Shares

79. The shares in Brooklyn Park Olive Groves Limited are CGT assets (section 108-5 of the ITAA 1997) and the amount paid by a Grower to acquire those assets is an outgoing of capital and not allowable as a deduction.

80. The amount paid for each share will represent the first element of the cost base of the share (subsection 110-25(2)). Any disposal of the shares by a Grower will be a CGT event and may give rise to a capital gain or loss.

Dividends

81. Dividends paid out of profits by Brooklyn Park Olive Groves Limited are included in the assessable income of shareholders under section 44(1) of the ITAA 1936.

Interest

82. 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 109 to 116 (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

83. For a Grower who is an individual, who has executed a Management Agreement and has not made an election under clause 6 of that Agreement, and who enters the Project:

- on or before 15 June 2003; or
- on or after 1 July 2003 and on or before 15 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 these Growers for the income years ending 30 June 2003 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.

84. 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 129 in the Explanations part of this ruling, below);
- 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)).

85. 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.

86. 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

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

87. For a Grower who participates in the Project and incurs expenditure as required by the Management Agreement and Licence to Occupy, the following provisions of the ITAA 1936 have application as indicated:

- expenditure by a Grower who participates in the Project does not fall within the scope of sections 82KZME - 82KZMF;
- 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 within this Ruling.

Explanations

Is the Grower carrying on a business?

88. For the amounts set out in the Tables above to constitute allowable deductions the Grower's horticulture activities as a participant in the Brooklyn Park Organic Olive Groves Project No. 3 must amount to the carrying on of a business of primary production. These horticulture activities will fall within the definitions of

'horticulture' and 'commercial horticulture' in section 40-535 of the ITAA 1997.

89. For schemes such as that of the Brooklyn Park Organic Olive Groves Project No. 3, 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) 54 ALR 167; (1984) 84 ATC 4618; (1984) 15 ATR 932.

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

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

91. In this Project, each Grower enters into a Management Agreement and a Licence to Occupy. Under the agreement each individual Grower will have rights over a specific and identifiable area of land. The agreement provides the Grower with an ongoing interest in the specific olive trees on the area the subject of the Licence for the term of the Project. Under the Licence the Grower must use the land in question for the purpose of carrying out horticultural activities and for no other purpose. The Licence allows the Manager to come onto the land to carry out its obligations under the agreement.

92. Under the Management Agreement and the Licence to Occupy the Manager is engaged by the Grower to establish and maintain an Allotment on the Grower's identifiable area of land during the term of the Project. The Manager has provided evidence that it has access to the appropriate professional skills and credentials to provide the management services to establish and maintain the Allotment on the Grower's behalf.

93. In establishing the Allotment, the Grower engages the Manager to install irrigation and to acquire and plant seedlings on the Grower's Allotment. During the term of the Project these assets will be used wholly to carry out the Grower's horticultural activities. The Manager is also engaged to harvest and sell, on the Grower's behalf, the olives grown on the Grower's Allotment.

94. 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.

95. 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 olives 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.

96. The pooling of olives grown on the Grower's Allotment with the olives of other Growers is consistent with general horticultural practices. Each Grower's proportionate share of the sale proceeds of the pooled olives will reflect the proportion of the olives contributed from their Allotment.

97. The Project Manager's services and the installation of assets on the Grower's behalf are also consistent with general horticultural practices. The assets are of the type ordinarily used in carrying on a business of horticulture. While the size of an Allotment is relatively small, it is of a size and scale to allow it to be commercially viable. (see Taxation Ruling IT 360).

98. 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 Allotment(s) and the activities carried out on the Grower's behalf. Growers are able to terminate arrangements with the Manager in certain instances, such as cases of default or neglect.

99. The horticultural 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' horticultural activities in the Brooklyn Park Organic Olive Groves Project No. 3 will constitute the carrying on of a business.

The Simplified Tax System ('STS')

Division 328

100. 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.

101. 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 Management Fees and Licence Fees

Section 8-1

102. Consideration of whether the initial Management Fees and Licence Fees 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 sufficient connection with activities to produce assessable income.

103. The Management Fees and Licence Fees associated with the horticultural activities will relate to the gaining of income from the Grower's business of horticulture (see above), and hence have a sufficient connection to the operations by which income (from the regular sale of olives) 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 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

104. Under the Management Agreement and Licence to Occupy neither the Management Fees nor the Licence Fee 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.

105. 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 109 to 116) 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

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

107. If the Grower is not an 'STS taxpayer', the Management Fees and the Licence Fees are deductible in the year in which they are incurred.

108. If the Grower is an 'STS taxpayer' the Management Fees and the Licence Fees 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

109. 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 licence of an area 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.

110. 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

111. 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)).

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

(a) the taxpayer's allowable deductions under the agreement for the 'expenditure year' exceed any assessable income attributable to the agreement for that year; and

(b) 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

(c) either :

- there is more than one participant in the agreement in the same capacity as the taxpayer; or
- the person who promotes, arranges or manages the agreement (or an associate of that person) promotes similar agreements for other taxpayers.

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

114. 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.

115. 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.

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

116. 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

117. For each Allotment in this Project, an initial Management Fee (amount dependent upon the date the Grower is accepted into the Project) and Licence Fee of $22 will be incurred on execution of the Licence to Occupy and Management Agreement. The Management Fee and the Licence Fee are charged for providing management services and leasing land to a Grower by 30 June of the year of execution of the agreement. Under the agreement, further monthly expenditure is required each year during the term of the Project for the provision of management services and land until 30 June in those years.

118. In particular, the Management Fee is expressly stated to be for a number of specified services. No explicit conclusion can be drawn from the description of the arrangement that the initial Management Fee has been inflated to result in reduced fees being payable for Management Fees in subsequent years.

119. There is also no evidence that might suggest the management services covered by the fee could not be provided within the relevant expenditure year. Thus, for the purposes of this Ruling, it can be accepted that no part of the initial Management Fee, and the fees for subsequent years, is for the Manager doing 'things' that are not to be wholly done within the expenditure year. Under the Licence to Occupy, the Licence Fee is payable annually on the anniversary of the Grower's entry into the Project for the licence of the land during the expenditure year.

120. On this basis, provided a Grower incurs expenditure as required under the Project's agreement, as set out in paragraphs 48 to 53, 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

121. Although not required under the Licence to Occupy or the Management Agreement, 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 104 above, section 82KZMF will apply to apportion the expenditure and allow a deduction over the period in which the prepaid benefits are provided.

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

Interest deductibility

Section 8-1

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

124. 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 109 to 116).

Expenditure of a capital nature

Division 40 and Division 328

125. 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 water facilities, a 'landcare operation', and the establishment of the olive trees is of a capital nature. This expenditure falls for consideration under Division 40 or Division 328 of the ITAA 1997.

126. 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'.

127. The tax treatment of capital expenditure has been dealt with in a representative way in paragraphs 72 and 78 (above) in the Tables and the accompanying Notes.

Deferral of losses from non-commercial business activities

Division 35

128. 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.

129. 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.

130. 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.

131. 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.

132. 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).

133. A Grower who participates in the Project will be carrying on a business activity that is subject to these provisions. Information provided with the application for this Product Ruling indicates that a Grower who acquires the minimum allocation of one Allotment in the Project is unlikely to have their activity pass one of the tests until the income year ended 30 June 2008. Growers who acquire more than one interest in the Project may however, find that their activity meets one of the tests in an earlier income year.

134. 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.

135. 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) 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.

136. Information provided with this Product Ruling indicates that a Grower who acquires the minimum allocation of one Allotment 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.

137. The Commissioner will decide for the Growers described in paragraphs 62 and 63 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 2005.

138. 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 13), in the manner described in the Arrangement (see paragraphs 14 to 61). 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.

139. 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 Independent Agricultural Report reproduced in the prospectus;
- the Olive Procurement Agreement with Inglewood Olive Processors Limited; and

- independent, objective, and generally available information relating to the olive industry which substantially supports cash flow projections and other claims, including prices and costs, in the Product Ruling application submitted by the Manager.

Section 82KL - recouped expenditure

140. 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

141. 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).

142. The Brooklyn Park Organic Olive Groves Project No. 3 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 71 to 76, it is not possible to conclude the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

143. 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 olives and/or olive produce. There are no facts that would suggest that Growers have the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There is no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing at arm's length or, if any parties are not dealing at arm's length, that any adverse tax consequences result. Further, having regard to the factors to be considered under paragraph 177D(b) it cannot be concluded, on the information available, that participants will enter into the scheme for the dominant purpose of obtaining a tax benefit.

Example

Entitlement to GST input tax credits

144. Susan, who is a sole trader and registered for GST, contracts with a manager to manage her afforestation 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	$2,200*
Total due and payable by 1 January 2002 (includes GST of $600)	$6,600

*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 x $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:

1/11 x $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 2002, 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

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

Commissioner of Taxation
28 May 2003

Previous draft:
Not previously issued in draft form

Related Rulings/Determinations:
TR 92/1; TR 92/20; TD 93/34; TR 97/11; TR 97/16; TR 98/22; PR 1999/95; TR 2000/8; IT 360

Subject References:
- carrying on a business
- commencement of business
- horticulture
- irrigation expenses
- management fees expenses
- primary production
- primary production expenses
- primary production income
- producing assessable income
- product rulings
- public rulings
- schemes and shams
- tax administration
- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters

Legislative References:
- ITAA 1997 Part 3-1
- 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 40
- ITAA 1997 40-F
- ITAA 1997 40-G
- ITAA 1997 40-515
- ITAA 1997 40-515(1)(a)
- ITAA 1997 40-515(1)(b)
- ITAA 1997 40-520(1)
- ITAA 1997 40-525(2)
- ITAA 1997 40-530
- ITAA 1997 40-530(2)
- ITAA 1997 40-535
- ITAA 1997 40-540
- ITAA 1997 40-545
- ITAA 1997 40-630

- ITAA 1997 40-635
- ITAA 1997 108-5
- ITAA 1997 110-25(2)
- ITAA 1997 Div 328
- ITAA 1997 Subdiv 328-D
- ITAA 1997 Subdiv 328-G
- ITAA 1997 328-105
- ITAA 1997 328-105(1)(a)
- ITAA 1997 328-105(1)(b)
- ITAA 1936 44
- ITAA 1936 44(1)
- ITAA 1936 82KL
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
- 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 Div 3 of Part III
- ITAA 1936 Part IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)
- TAA 1953 Part IVAAA
- Corporations Act 2001
- Copyright Act 1968

Case references:

- FCT v. Lau 84 ATC 4929; (1984) 16 ATR 932

ATO references:
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