



# ***PR 2004/31 - Income tax: Great Southern Vineyards 2004 Project***

 This cover sheet is provided for information only. It does not form part of *PR 2004/31 - Income tax: Great Southern Vineyards 2004 Project*

 This document has changed over time. This is a consolidated version of the ruling which was published on *28 June 2006*



## Product Ruling

### Income tax: Great Southern Vineyards 2004 Project

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

#### *Preamble*

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

*[Note: This is a consolidated version of this document. Refer to the Tax Office Legal Database (<http://law.ato.gov.au>) to check its currency and to view the details of all changes.]*

#### **No guarantee of commercial success**

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

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

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

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

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

## **Terms of Use of this Product Ruling**

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

## **What this Product Ruling is about**

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1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax 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 'Great Southern Vineyards 2004 Project', or just 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 70 (ITAA 1997);
- Division 328 (ITAA 1997);
- Division 328 of the *Income Tax (Transitional Provisions) Act 1997*;
- Section 82KL of the *Income Tax Assessment Act 1936* (ITAA 1936);
- Section 82KZL (ITAA 1936);
- Sections 82KZME - 82KZMF (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.

### **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.

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## Date of effect

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11. This Ruling applies prospectively from 17 March 2004, 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).

Note: The Addendum to this Ruling that issued on 28 June 2006 applies on and from 1 July 2005.

## Withdrawal

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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**

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

- Application for Product Ruling dated 9 December 2003 and additional correspondence between the ATO and the Applicant dated 12 February 2004, 24 February 2004, 30 January 2004, 16 January 2004, 23 January 2004, 2 February 2004, 9 February 2004, 11 February 2004, 25 February 2004, 2 March 2004, 3 March 2004, 9 March 2004, 10 March 2004 and 11 March 2004;
- Draft PDS for the Great Southern Vineyards 2004 Project, to be issued by Great Southern Managers Australia Ltd ('GSMAL'), received 3 March 2004;
- Draft **Constitution** of the Great Southern Vineyards 2004 Scheme, dated 25 November 2003;
- Draft **Lease and Management Agreement** between GSMAL (as both the 'Lessor' and 'Responsible Entity') and the Grower, received 10 March 2004;
- Proforma lease between GSMAL and Great Southern Vineyard Holdings Pty Ltd (as the 'Landholder'), received 9 December 2003;
- Draft Compliance Plan for Great Southern Vineyards 2004 Project, received 9 December 2003;
- Draft Management Services Agreement between GSMAL and Great Southern Plantations Ltd ('GSPL'), received 9 December 2003; and
- **Loan Deed** between Great Southern Finance Pty Ltd (as the 'Lender') and the Borrower;

**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

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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 Great Southern Vineyards 2004 Project are as follows:

Location	The Frankland area of the South West region of Western Australia.
Type of business each participant is carrying on	Commercial growing of Wine grapes.
Number of hectares offered for cultivation	170
Size of each Vinelot	0.05 hectares
Number of vines per hectare	1852
Term of the Project	18 years and 1 month
Initial cost	\$5,225 (includes prepaid fees amount)
Initial cost per hectare	\$104,500 (includes prepaid fees amount)
Ongoing costs	<ul style="list-style-type: none"> <li>• Management fee of 88% of Net Proceeds of Sale for the Second, Third and Fourth Periods, subject to a minimum of \$275 in the Fourth Period;</li> <li>• Management fee of 33% of Net Proceeds of Sale for the Fifth Period (Years 4 to 18), subject to a minimum of \$275, and</li> <li>• Rent of 12% of Net Proceeds of Sale for all years after the Initial Management Period.</li> </ul>
Other costs	Growers will be charged for the cost of all insurance except Public Liability Insurance.

18. Under this PDS, GSMAL proposes to offer 3,400 interests called 'Vinelots' of 0.05 hectares. The Project is registered as a Managed Investment Scheme under the *Corporations Act 2001*. The

Responsible Entity for the Project is Great Southern Managers Australia Ltd ('GSMAL').

19. The land for the Project has been purchased by Great Southern Vineyard Holdings Pty Ltd ('GSVH'), a wholly owned subsidiary of GSMAL which will lease the land to GSMAL. There is no minimum subscription for this Project and GSMAL has the right to accept oversubscriptions.

20. Growers enter into a contract with GSMAL to manage their Vinelots for the eventual harvest and sale of their grape produce. GSMAL will manage and cultivate the vines and be responsible for harvesting and selling the grapes. GSMAL will arrange the marketing and sale of the grape produce.

21. Under the Product Disclosure Statement offer, Growers will enter the Project on or before 31 May 2004.

22. Upon application, Growers will execute a Power of Attorney enabling GSMAL to act on their behalf as required. Each Grower is provided with an ownership certificate and a copy of the vineyard grid map from which their land and vines can be identified.

### **Constitution**

23. The Constitution establishes the Project and operates as a deed binding on all of the Project's Growers and the Responsible Entity. The Constitution sets out the terms and conditions under which GSMAL agrees to act as Responsible Entity and thereby manage the Project. Growers are bound by the Constitution by virtue of their participation in the Project. Pursuant to clause 28 of the Constitution, the Responsible Entity will keep a register of Growers.

24. Under the terms of the Constitution, all moneys received from applications shall be paid to the Responsible Entity which will deposit those moneys into an Application Fund in the name of the Responsible Entity. The application moneys will be released by the Responsible Entity when it is reasonably satisfied that certain specified criteria in the Constitution have been met (clauses 7 and 8 of the Constitution).

### **Compliance plan**

25. As required by the Corporations Law, a Compliance Plan has been adopted by GSMAL for the Project. The purpose of the Compliance Plan is to ensure that GSMAL manages the Project in accordance with its obligations and responsibilities contained in the Constitution and that the interests of Growers are protected.

## **Lease and Management Agreement**

26. Growers participating in the arrangement will enter into a Lease and Management Agreement ('LMA') between GSMAL and the Grower.

27. The Lease and Management Agreement provides that each Grower appoints GSMAL to perform services under the agreement from the Commencement Date, being the date of execution of the Agreement. GSMAL will supervise and manage all viticultural activities on behalf of the Grower. The services to be performed are specified in Schedules 2 and 3 to the Agreement.

28. The Grower appoints the Responsible Entity to provide the Initial Management Services to be performed during the Initial Management Period, being the period from the Commencement Date to 30 June 2004. The Initial Management Services include the following:

- (a) All inspection, supervision and management activities from the Commencement Date, including the Responsible Entity's continual inspection and monitoring of the establishment of the Vineyard on behalf of Growers to ensure the Vineyard is of the quality required by Responsible Entity;
- (b) The obtaining of formal verification by 30 June from an Independent Viticulture Expert that the Vinelot is of an appropriate standard and all required services have been performed and to an appropriate standard;
- (c) All marketing activities in respect of the sale or future sale of the Grape Produce as necessary from the Commencement Date;
- (d) Obtaining all necessary approvals and consents required in relation to the provision of the services listed in this Schedule 2;
- (e) Activities in respect of arranging insurance of the Grape Produce;
- (f) Carrying out any other obligation to be performed by the Responsible Entity pursuant to the terms of any agreement entered into by the Responsible Entity;
- (g) All administrative services required in respect of providing the services listed in this Schedule 2;
- (h) Keeping in good order and condition any access road or roads within the Vineyard, keeping in good repair and condition all waterways, dams, irrigation and pumping equipment within the Vineyard, as necessary;

- (i) Undertaking pest control, fungicide control and other vine disease measures as necessary; and
- (j) Any other activity that may be required to generally maintain the Vineyard in accordance with good viticultural practice or in respect of the provisions of the services listed in this Schedule 2.

29. The Grower appoints the Responsible Entity to provide the Ongoing Management Services in respect to their Vinelots for an 18 year period commencing on 1 July 2004. The Agreement defines Ongoing Management Services to mean all commercial viticultural activities required to be carried on to manage and maintain the vines according to good viticultural and vineyard practice, including but not limited to:

- (a) Cultivating, tending, culling, watering, pruning, replanting, spraying and otherwise caring for the Vines, as and when necessary;
- (b) Keeping in good order and condition any access road or roads within the Vineyard, keeping in good repair and condition all waterways, dams, irrigation and pumping equipment within the Vineyard, as required;
- (c) Undertaking pest control, fungicide control and other vine disease measures as required on the Vinelots;
- (d) Controlling rabbits and other vermin by fumigating and poisoning and complying with the provisions of all statutes, regulations and by-laws (and all amendments) thereto with respect to the same, and any other statutes, rules or regulations and by-laws relating to or affecting the Vinelot or the Grower in respect thereof;
- (e) Keeping in good repair and condition all fences, trellising, irrigation and adequate fire-breaks within the Vineyard;
- (f) Obtaining a Report from the Independent Viticulture Expert within 6 months after the completion of planting of all vines within the Project, at least six monthly for the first year thereafter and then annually, to be provided to the Grower;
- (g) Carrying out any other obligation to be performed by the Responsible Entity pursuant to the terms of any agreement entered into by the Responsible Entity;
- (h) Obtaining all necessary approvals and consents required in relation to the provision of the services listed in this Schedule 3; and

- (i) Any other activity that may be required to generally maintain the Vineyard in accordance with good viticultural practice.

30. Growers participating in the Project will, pursuant to the terms of the Lease and Management Agreement, be granted an interest in the Vineyard by GSMAL in the form of a sub-lease to use their Vinelot for the purpose of conducting their viticultural business.

31. The Lease gives the Grower a sub-lease over an identifiable area of land for a period of 18 years following the Initial Management Period or until the Project is terminated.

32. Each Grower must pay Rent to the Lessor in an amount specified in Item 6 of Schedule 1 to the Lease and Management Agreement. The amount of Rent is determined as a percentage of the Net Proceeds of Sale.

33. Some of the conditions of the lease are that the Grower:

- will not use, or permit to be used, the Vinelot for a purpose other than that of commercial viticulture;
- will not use, or permit to be used, the Vinelot for residential, recreational or tourist purposes;
- must pay annual insurance premiums;
- shall keep the Vinelot in good and substantial repair; and
- must not install upon or remove anything from the Vinelot.

## **Fees**

34. The fees payable under the Lease and Management Agreement per Vinelot are as follows:

- An Application fee of \$5,225 payable on application. This fee is made up of \$3,850 for the Initial Management Services, \$825 for the Ongoing Management Services in the Second Period and \$550 for the Ongoing Management Services in the Third Period;
- Management fee of 88% of a Growers Net Proceeds of Sale for the Second, Third and Fourth Periods, subject to a minimum payment of \$275 in the Fourth Period;
- Management fee of 33% of a Growers Net Proceeds of Sale for each year in the Fifth Period (Years 4 to 18), subject to a minimum payment of \$275; and

- Rent of 12% of the Growers Net Proceeds of Sale in each year in which the Vinelot is harvested.

35. GSMAL will use its best endeavours to arrange insurance of the Vinelot on behalf of the Grower to cover against fire and other usual risks.

### **Harvesting and Sale**

36. Commencing from the date of the first harvestable grape crop, or at such other time or times as the Responsible Entity in its absolute discretion considers appropriate, the Responsible Entity will harvest, or arrange for the harvest of, the Grape Produce at such times or times as in the opinion of the Responsible Entity, will result in Grape Produce suitable for the purposes of making quality wines (clause 18).

37. The Grower has appointed GSMAL to sell the Grape Produce on behalf of the Grower for the maximum practicable price available (clause 19 of the LMA). At all times the Grower has full right, title and interest in the Grape Produce and the right to have the Grape Produce sold for their benefit (clause 11.3 of the LMA).

38. GSMAL will ensure that the Gross Proceeds of Sale are paid into the Proceeds Fund trust bank account. The Growers' proportional share of the costs of harvesting will be paid from the Gross Proceeds of Sale to GSMAL, or the relevant third party. GSMAL will pay the Rent and Management Fee from the Net Proceeds of Sale. On or before each Distribution Date, GSMAL will distribute to the Growers, out of the Proceeds Fund, each Grower's Proportional Interest of the Proceeds Fund relating to the last Accounting Period. The terms 'Proceeds Fund' and 'Grower's Proportional Interest' are defined in clause 1 of the LMA.

### **Finance**

39. Growers can fund their participation in the Project themselves, borrow from Great Southern Finance Pty Ltd (a lender associated with GSMAL) or borrow from an independent lender.

40. Finance is available from Great Southern Finance Pty Ltd under the following arrangements. Normal debt recovery procedures, including legal action, will be taken in the case of defaulting borrowers:

Option A – Interest Free Finance – 1 or more Vinelots:

- equal monthly principle instalments of \$396 over a 12 month period;

- instalments paid by direct debit commencing on 15 July 2004;
- GST is payable on execution of the Lease and Management Agreement (\$475 per Vinelot); and
- No interest applicable.

Option B – Principal and Interest Finance - Minimum of 2 Vinelots:

The terms of the principal and interest finance arrangements provided by Great Southern Finance Pty Ltd include options of loans for a minimum of 2 years up to a maximum of 10 year terms as follows:

- 2 to 3 year option - interest rate of 10.0% fixed for the term of the loan;
- 4 to 5 year option - interest rate of 10.5% fixed for the term of the loan;
- 6 to 7 year option - interest rate of 11.0% fixed for the term of the loan; and
- 8 to 10 year option - interest rate of 11.5% fixed for the term of the loan.

For all loans under Option B, the following will apply:

- GST is payable on execution of the Lease and Management Agreement (\$475 per Vinelot);
- application fee of 1.1% of the loan advance (GST inclusive);
- legal administration fee of \$275 (GST inclusive);
- regular monthly repayments in accordance with repayment table; and
- security taken over Lease and Management Agreement.

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

- entities associated with the Project, other than Great Southern Finance Pty Ltd, are involved in the provision of finance for the Project;
- 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' 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 terms or rate of interest are of a non-arm's length nature;
- repayments of the principal and 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) back to the lender or any associate; or
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers.

## **Ruling**

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### **Application of this Ruling**

42. This Ruling applies only to Growers who are accepted to participate by 31 May 2004, where the Grower has executed a Lease and Management Agreement on or before that date.

43. The Grower's participation in the Project must constitute the carrying on of a business of primary production (See Explanations at paragraphs 63 to 75). 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')**

44. 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'.

44A. Changes to the STS rules apply from 1 July 2005. From that date, 'STS taxpayers' may use the accruals accounting method. For a Grower participating in the Project, the recognition of income and the timing of tax deductions is different depending on whether the Grower who was an 'STS taxpayer' prior to 1 July 2005 continues to use the cash accounting method (called the 'STS accounting method') – see

sections 328-120 and 328-125 of the *Income Tax (Transitional Provisions) Act 1997*.

### **Qualification**

45. 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***

46. That part of the gross sales proceeds from the Project attributable to the Grower's produce, less any GST payable on these proceeds (section 17-5), will be assessable income of the Grower under section 6-5.

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

#### **Trading Stock**

##### ***Section 70-35***

48. A Grower who is not an 'STS taxpayer' may, in some years, hold grapes that will constitute trading stock on hand. Where, in an income year, the value of trading stock on hand at the *end* of an income year exceeds the value of trading stock on hand at the *start* of an income year a Grower must include the amount of that excess in assessable income.

49. Alternatively, where the value of trading stock on hand at the start of an income year exceeds the value of trading stock on hand at the end of an income year, a Grower may claim the amount of that excess as an allowable deduction.

**Deductions for Management fees, Interest and Capital Expenditure****Section 8-1**

50. A Grower who is not an 'STS taxpayer' may claim tax deductions for the following revenue expenses on a per Vinelet basis, as set out in the Table below:

**Division 40**

51. A Grower who is not an 'STS taxpayer' will also be entitled to a tax deduction relating to grapevines, as set out in the Table below:

Fee Type	ITAA 1997 Section	30/6/2004 (Initial Period)	30/6/2005 (Second Period)	30/06/2006 (Third Period)
<b>Management Services</b>	8-1	\$3,850 See Notes (i) & (ii)	\$687.50 See Notes (i) & (ii)	\$687.50 See Notes (i) & (ii)
<b>Interest</b>	8-1	As incurred See Note (iii)	As incurred See Note (iii)	As incurred See Note (iii)
<b>Establishment of horticultural plants (Grapevines)</b>	40-515			See Notes (i) & (iv)

**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 115.
- (ii) The amount of \$5,225 payable on application consists of an Initial Management Services fee of \$3,850 and a prepayment of the Second and Third Period fees of \$1,375. The Initial Management Services fee of \$3,850 is payable on application for services to be provided in the Initial Management Period and is deductible in the year in which it is incurred. However, the amount of \$1,375 prepaid in respect of the Ongoing Management Services is **NOT** deductible in the year in which it is incurred for non-'STS taxpayers'. Deductions for this amount **must** be determined using the formula in subsection 82KZMF(1) (see paragraphs 80 to 87 below). This section operates to apportion expenditure over the eligible service period or ten years, whichever

is the lesser. The 'eligible service period' commences on 1 July 2004 and ends on 30 June 2006.

Accordingly, an amount of \$687.50 is deductible in each of the years ended 30 June 2005 and 30 June 2006.

- (iii) The deductibility or otherwise of interest arising from agreements entered into with financiers other than Great Southern Finance Pty Ltd, 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 Great Southern Finance Pty Ltd, should read carefully the discussion of the prepayment rules in paragraphs 80 to 87 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.
- (iv) As Grapevines are affixed to land which the Grower does not own, they are not owned by the Grower, the conditions in subsection 40-525(3) cannot be met, and the Grapevines are not eligible for the 4 year write-off under section 40-550. However, Grapevines are a 'horticultural plant' as defined in subsection 40-525(2). As Growers hold the land under a lease, the condition in item 3 of 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 Grapevines is determined using the formula in section 40-545 and is based on the capital expenditure incurred that is attributable to their establishment. If the Grapevines have an 'effective life' of greater than 13 but fewer than 30 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 13%. The deduction is allowable when the Grapevines enter their first commercial season (section 40-530, item 2). The Project Manager will inform Growers of when the Grapevines enter their first commercial season.

## **Tax outcomes for Growers who are ‘STS taxpayers’**

### **Assessable Income**

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

52. That part of the gross sales proceeds from the Project attributable to the Grower’s produce, less any GST payable on these proceeds (section 17-5), will be assessable income of the Grower under section 6-5.

53. For the 2005 and prior income years, a Grower recognises ordinary income from carrying on the business of afforestation at the time the income is received (paragraph 328-105(1)(a)). For the 2005-06 and later income years, a Grower who is an ‘STS taxpayer’ using the accruals accounting method will be assessable on this income in the income year in which the income is derived and a Grower who is an ‘STS taxpayer’ using the cash accounting method will be assessable on this income in the income year in which the income is received.

### **Trading stock**

#### ***Section 328-285***

54. A Grower who is an ‘STS taxpayer’ may, in some years, hold grapes that will constitute trading stock on hand. Where, for such a Grower, for an income year, the difference between the value of all their trading stock at the start and a reasonable estimate of it at the end, is less than \$5,000, they do not have to account for that difference under the ordinary trading stock rules in Division 70 (subsection 328-285(1)).

55. Alternatively, a Grower who is an ‘STS taxpayer’ may instead choose to account for trading stock in an income year under the provisions of Division 70 (subsection 328-285(2)).

### **Deductions for Management fees, Interest and Capital Expenditure**

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

56. A Grower who is an ‘STS taxpayer’ may claim deductions for the revenue expenses in the following Table on a per Vinelot basis. However, if for any reason, an expense referred to in the Table is not fully paid in the year in which it is incurred by a Grower who is an ‘STS taxpayer’ (for the 2005 and prior income years) or is an ‘STS taxpayer’ using the cash accounting method (for the 2006 and later income years) then the amount is only deductible to the extent to which it has been paid, or has been paid for the Grower

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(paragraph 328-105(1)(b)). For these taxpayers, any expense or part of an expense shown in the Table, which is not paid in the year in which it is incurred, will be deductible in the year in which it is actually paid.

**Subdivision 40-F**

57. A Grower who is an 'STS taxpayer' will also be entitled to a tax deduction relating to grapevines as set out in the Table below:

Fee Type	ITAA 1997 Section	30 June 2004 (Initial Period)	30 June 2005 (Second Period)	30 June 2006 (Third Period)
Management Services	8-1	\$3,850 See Notes (v) & (vi)	\$687.50 See Notes (v) & (vi)	\$687.50 See Notes (v) & (vi)
Interest	8-1	When paid See Note (vii)	When paid See Note (vii)	See Note (vii)
Establishment of horticultural plants (Grapevines)	40-515			See Notes (v) & (viii)

**Notes:**

- (v) 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 115.
- (vi) The amount of \$5,225 payable on application consists of an Initial Management Services fee of \$3,850 and a prepayment of the Second and Third Period fees of \$1,375. The Initial Management Services fee of \$3,850 is payable on application for services to be provided in the Initial Management Period and is deductible in the year in which it is paid by, or for, Growers who are 'STS taxpayers'. However, the amount of \$1,375 prepaid in respect of the Ongoing Management Services is **NOT** deductible in the year that it is paid by, or for, Growers who are 'STS taxpayers'. Deductions for this amount **must** be determined using the formula in subsection 82KZMF(1) (see paragraphs 80 to 87 below). This section operates to apportion expenditure over the eligible service period or ten years, whichever is the lesser. The 'eligible service period' commences on 1 July 2004 and ends on 30 June 2006. Accordingly, an amount of \$687.50 is

deductible in each of the years ended 30 June 2005 and 30 June 2006.

- (vii) The deductibility or otherwise of interest arising from loan agreements entered into with financiers other than Great Southern Finance Pty Ltd, 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 Great Southern Finance Pty Ltd, should read carefully the discussion of the prepayment rules in paragraphs 80 to 87 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.
- (viii) As Grapevines are affixed to land which the Grower does not own, they are not owned by the Grower, the conditions in subsection 40-525(3) cannot be met, and the Grapevines are not eligible for the 4 year write-off under section 40-550. However, Grapevines are a 'horticultural plant' as defined in subsection 40-525(2). As Growers hold the land under a lease, the condition in item 3 of 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 Grapevines is determined using the formula in section 40-545 and is based on the capital expenditure incurred that is attributable to their establishment. If the Grapevines have an 'effective life' of greater than 13 but fewer than 30 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 13%. The deduction is allowable when the Grapevines enter their first commercial season (section 40-530, item 2). The Project Manager will inform Growers of when the Grapevines enter their first commercial season.

## **Tax outcomes that apply to all Growers**

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

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

58. For a Grower who is an individual and who enters the Project by 31 May 2004, the rule in section 35-10 may apply to the business activity comprised by their involvement in the Project. Under

paragraph 35-55(1)(b) the Commissioner will decide for the income years ending 30 June 2004 to 30 June 2007 for Growers entering by 31 May 2004 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.

59. 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 102 in the Explanation part of this Ruling);
- a Grower's business activity satisfies one of the tests in sections 35-30, 35-35, 35-40 or 35-45; or
- the Grower's business activity produces assessable income for an income year greater than the deductions attributable to it for that year (apart from the operation of subsection 35-10(2)).

60. 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 the 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.

61. 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 subsection 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**

62. For a Grower who commences participation in the 2004 Project and incurs expenditure as required by the Lease and Management 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.

## **Explanation**

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

63. For the amounts set out in the Tables above to constitute allowable deductions, the Grower's viticultural activities as a participant in the Great Southern Vineyards 2004 Project must amount to the carrying on of a business of primary production.

64. Where there is a business, or a future business, the gross proceeds from the sale of the grape produce will constitute 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.

65. For schemes such as those of the Great Southern Vineyards 2004 Project, Taxation Ruling TR 2000/8 sets out in paragraph 89 the circumstances in which the Grower's activities can constitute the carrying on of a business. As Taxation Ruling TR 2000/8 sets out, these circumstances have been established in court decisions such as *Commission of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

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

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

67. In this Project, each Grower enters into a Lease and Management Agreement. 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 vines on the leased area for the term of the Project. Under the agreement, the Grower must use the land in question for the purpose of carrying out viticultural activities, and for no other purpose. The agreement allows Great Southern Managers Australia Ltd, the

Landholder and the Responsible Entity, to come onto the land to carry out its obligations.

68. Under the Lease and Management Agreement, the Responsible Entity is engaged by the Grower to maintain a Vinelot on the Grower's identifiable area of land during the term of the Project. The Responsible Entity has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to maintain the Vinelot on the Grower's behalf.

69. The Responsible Entity is also engaged to harvest and sell, on the Grower's behalf, the grape produce grown on the Grower's Vinelot.

70. 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.

71. 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 grape 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.

72. The pooling of grape produce from vines grown on the Grower's Vinelot with the grape produce of other Growers is consistent with general viticultural practices. Each Grower's proportionate share of the sale proceeds of the pooled grape produce will reflect the proportion of the produce contributed from their Vinelot(s).

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

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

75. The viticultural 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' viticultural activities in the Project will constitute the carrying on of a business.

## **The Simplified Tax System**

### ***Division 328***

76. 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.

77. 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**

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

78. Consideration of whether the initial management 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.

79. The fee payable on application is associated with the viticultural activities that will relate to the gaining of income from the Grower's business of viticulture (see above), and hence has a sufficient connection to the operations by which income (from the harvesting and sale of grape produce) is to be gained from this business. It will thus be deductible under the first limb of section 8-1. Further, no 'non-income producing' purpose in incurring the fee is identifiable from the arrangement. 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.

**Prepayment provisions*****Sections 82KZL to 82KZMF***

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

81. For this Project, only section 82KZL (an interpretive provision) and sections 82KZME and 82KZMF are relevant. 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) (see paragraph 86 below). 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***

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

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

- the taxpayer's allowable deductions under the agreement for the 'expenditure year' exceed any assessable income attributable to the agreement for that year;
- the taxpayer does not have effective day to day control over the operation of the agreement. That is, the significant aspects of the arrangement are managed by someone other than the taxpayer; and

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

84. For the purpose of these provisions, the agreement includes all activities that relate to the agreement (subsection 82KZME(4)). This has particular relevance for a Grower in this Project who, in order to participate in the Project may borrow funds from a financier other than Great Southern Finance Pty Ltd. 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 a Grower prepays interest under such financing arrangements, the deductions allowable will be subject to apportionment under section 82KZMF.

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

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

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

87. In the formula 'eligible service period' (defined in subsection 82KZL(1)) means, the period during which the thing under the agreement is to be done. The eligible service period begins on the day on which the thing under the agreement commences to be done or on the day on which the expenditure is incurred, whichever is the later, and ends on the last day on which the thing under the agreement ceases to be done, up to a maximum of 10 years.

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

88. Under the Lease and Management Agreement, a Grower incurs fees on application of \$5,225 per Vinelot. These fees are made up of :

- \$3,850 for the Initial Management Services to be provided in the Initial Management Period from the Commencement Date to 30 June 2004; and
- prepayment of \$1,375 for Ongoing Management Services to be provided in the Second Period and Third Period from 1 July 2004 to 30 June 2006.

89. The fee of \$3,850 for the Initial Management Services is for services to be provided within the year in which the fee is incurred and is therefore deductible in that year.

90. The expenditure incurred by a Grower in the Project for the Ongoing Management Services meets the requirements of subsections 82KZME(1) and (2) and is incurred under an 'agreement' as described in subsection 82KZME(3). Therefore, unless one of the exceptions to 82KZME applies, the amount and timing of those deductions for those fees are determined under section 82KZMF.

91. The prepaid Ongoing Management fees do not fall within any of the 5 exceptions to section 82KZME. Therefore, the deduction for each year is determined using the formula in subsection 82KZMF(1). Section 82KZMF will apportion the deduction for prepaid Ongoing Management fees over the eligible service period which commences on 1 July 2004 and ends on 30 June 2006.

## **Interest deductibility**

### ***(i) Growers who use Great Southern Finance Pty Ltd as the finance provider***

92. Some Growers may finance their participation in the Project through a loan facility with Great Southern 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 management fees.

93. The interest incurred by these Growers will be in respect of a loan to finance the Project business operations of growing grapes and is therefore 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.

94. In the absence of any application of the prepayment provisions (see paragraphs 80 to 87), the timing of deductions for interest will again depend upon whether a Grower is an 'STS taxpayer' or is not an 'STS taxpayer'.

95. For the 2005 and prior income years, if the Grower is not an 'STS taxpayer', interest is deductible in the year in which it is incurred. For the 2006 and later income years, if the Grower is not an 'STS taxpayer' or is an 'STS taxpayer' using the accruals accounting method, interest is deductible in the year in which it is incurred.

96. If a Grower is an 'STS taxpayer' (or in the case of the 2006 and later income years is an 'STS taxpayer' using the cash accounting method), interest is deductible in the income year in which it is paid, or is paid for the Grower. If interest that is properly incurred in an income year remains unpaid at the end of the 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 Great Southern Finance Pty Ltd as the finance provider***

97. 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 Great Southern Finance Pty Ltd 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.

98. 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 relevant prepayments provisions of the ITAA 1936 (see paragraphs 80 to 87).

**Division 35 - deferral of losses from non-commercial business activities**

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

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

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

100. 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.

101. 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.

102. 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.

103. 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 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).

104. 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 Vinelot is unlikely to have their activity pass one of the tests until the year ended 30 June 2010.

105. 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.

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

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

107. Information provided with this Product Ruling application indicates that a Grower who acquires the minimum allocation of one Vinelot in the 2004 Project is expected to be carrying on a business activity that will produce a taxation profit for the income year ended 30 June 2008.

108. The Commissioner will decide for such a Grower that it would be reasonable to exercise the second arm of the discretion for all years up to, and including, the year ended 30 June 2007.

109. 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 58) in the manner described in the Arrangement (see paragraphs 14 to 41). 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.

110. 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 Viticultural Expert and additional evidence provided with the application by the Responsible Entity; and

- independent, objective and generally available information relating to the grape growing 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**

111. The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefit(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**

112. 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).

113. The Project will be a 'scheme'. A Grower will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 50 to 56 that would not have been obtained but for the scheme. However, it is not possible to conclude that the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

114. 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 grape 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 are no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing with each other at arm's length, or, if any parties are not 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**

115. 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**

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**Commissioner of Taxation**

17 March 2004

*Previous draft:*

Not previously issued in draft form

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

*Other Rulings/ Determinations*

TR 2001/14

*Subject references:*

- carrying on a business
- commencement of business
- fee expenses
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NO 2003/12233  
ISSN: 1441 1172