



# ***PR 2004/34 - Income tax: Barkworth Olives Project No 8***

 This cover sheet is provided for information only. It does not form part of *PR 2004/34 - Income tax: Barkworth Olives Project No 8*

 This document has changed over time. This is a consolidated version of the ruling which was published on *24 March 2004*



## Product Ruling

### Income tax: Barkworth Olives Project No 8

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

#### *Preamble*

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

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

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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 Ruling is about

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1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax laws' identified below apply to the defined class of persons who take part in the arrangement to which this Ruling refers. In this Ruling this arrangement is sometimes referred to as the Barkworth Olives Project No 8 or simply as 'the Project'.

### Tax law(s)

2. The tax laws dealt with in this Ruling are:
- Section 6-5 of the Income Tax Assessment Act 1997 ('ITAA 1997');
  - Section 8-1 (ITAA 1997);
  - Section 17-5 (ITAA 1997);
  - Division 27 (ITAA 1997);
  - Division 35 (ITAA 1997);
  - Division 40 (ITAA 1997);
  - Division 328 (ITAA 1997);
  - Section 82KZME of the Income Tax Assessment Act 1936 ('ITAA 1936');
  - Section 82KZMF (ITAA 1936); and
  - Part IVA (ITAA 1936).

### Goods and Services Tax

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

### Changes in the Law

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

the application of this Ruling and, to that extent, this Ruling will be superseded.

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

### **Note to promoters and advisers**

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

### **Class of persons**

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

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

- intend to terminate their involvement in the arrangement prior to its completion;
- do not intend to derive assessable income from it;
- elect to manage their Grovelot(s);
- enter into finance arrangements with Barkworth Finances Pty Ltd or any associate of Barkworth Finances Pty Ltd;
- enter into this arrangement after 15 June 2004; or
- are not a resident of Australia under the ITAA 1936 or the ITAA 1997.

### **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 24 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 that private ruling if the income year to which it relates has ended or has commenced but not yet ended. However if the arrangement covered by the private ruling has not commenced, and the income year to which it relates has not yet commenced, this Ruling applies to the taxpayer to the extent of the inconsistency only (see Taxation Determination TD 93/34).

## Withdrawal

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13. This Product Ruling is withdrawn and ceases to have effect after 30 June 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**

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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 a Product Ruling that became valid on 28 October 2003 as constituted by documents provided on: 19 and 27 August 2003, 11 September 2003, 28 October 2003, 20 and 28 November 2003, 9 December 2003, 13 and 16 February 2004, 4 and 15 March 2004 and additional correspondence dated: 15 and 27 August 2003; 10 September 2003, 27 October 2003, 5, 19 and 27 November 2003, 11 and 24 December 2003, 3, 13, 16 and 19 February 2004, 4, 11, 15, 16 and 17 March 2004;
- Correspondence from the ATO to the Applicant dated: 20 and 29 August 2003, 18, 23 and 24 September 2003, 30 October 2003, 10 and 13 November 2003, 11 and 16 December 2003, 8 January 2004, 11, 16 and 24 February 2004, 15 and 16 March 2004;
- Draft 9 Product Disclosure Statement/Prospectus prepared for Barkworth Olives Management Limited A.C.N. 084 316 101 ('BOML') and Barkworth Land Corporation Limited A.C.N. 102 54 616 ('BLCL'), dated 3 March 2004 and received by the ATO on 4 March 2004;
- Draft **Constitution** of the Barkworth Olives Project No. 8 between BOML and each Grower, dated 3 March 2004 and received by the ATO on 4 and 15 March 2004;
- Draft **Licence Agreement** between BLCL, BOML and each Grower, dated 3 March 2004 and received by the ATO on 4 March 2004;
- Draft **Management Agreement** between BOML and each Grower, dated 3 March 2004 and received by the ATO on 4 March 2004;
- Draft Olive Purchase Agreement between Inglewood Olive Processors Limited ('IOPL') and BOML, received by the ATO on 19 August 2003;
- Draft Custodian Agreement between McMahon Clarke Legal and BOML, received by the ATO on 28 November 2003;

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- Draft Compliance Plan for the Project, received by the ATO on 19 August 2003;
- Draft Lease Agreement between Barkworth Olive Groves Limited ('BOGL') and BLCL, received by the ATO on 20 November 2003;
- Draft Water Supply Agreement between BOGL and BLCL, received by the ATO on 19 August 2003; and
- Profit & Loss forecasts for BOML and BLCL over the life of the Project, received by the ATO on 4 March 2004.

**Note:** certain information has been provided by the Applicant on a commercial-in-confidence basis and will not be disclosed or released under Freedom of Information legislation.

15. The documents highlighted are those Growers enter into or become a party to. 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 part of the arrangements to which this Ruling applies.

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

**Overview**

17. This arrangement is called the Barkworth Olives Project No 8 (the Project).

Location	Bassano/Kingston Park Property near Griffith, New South Wales
Type of business each participant is carrying on	Cultivating olive trees on their designated 0.256 hectare (approximate) olive Grovelot(s) and harvesting the olives for production and sale of olive oil.
Number of hectares under cultivation	Up to 250
Number of olive trees per hectare	An average of 320 trees
Size of each Grovelots	0.256 hectares approximately
Number of olive trees per Grovelot	80

Minimum number of Grovelots per Grower	1
The term of the project in years	Approximately 20 years commencing on acceptance of a Grower's Application and ending on 30 June 2024
Subscription amount per Grovelot	\$5,227.75 in year ended 30 June 2004 consisting of an initial management fee of \$4,994 and a licence fee of \$233.75.
Minimum subscription for Project	None
Management fees	\$2,266 in each of the years ended 30 June 2005 and 30 June 2006, \$1,210 for the year ended 30 June 2007, \$1,320 for the year ended 30 June 2008 and \$1,430 from the year ended 30 June 2009.
Licence fees	\$233.75 each year indexed to CPI from 30 June 2007.
Ongoing and other Grower Costs	Incentive fees and optional insurance costs.
Option to take up shares in Landholding Company	Each Grower will be issued with 1 Call Option to take up ten shares in the capital of BLCL for each Grovelot in the Project that the Grower subscribes for. The Growers' options to subscribe for shares are exercisable between 1 July 2024 and 31 July 2024.

18. Before the Project can commence the following needs to occur:

- Separate land titles for the land on which the Project is to be conducted are required to be registered;
- BOGL, the owner of the Project land, is to transfer the Project land to BLCL for market value and the transfer of the Project land is to be lodged for registration in accordance with the law relating to the registration of transfer of land in the place where the Project land is situated;
- BLCL, as the Land Holder, will lease the Project land to BOML as the Responsible Entity for the Project. The lease will be a valid lease which will be lodged for

registration, under the *New South Wales Real Property Act 1900*, within 45 days from 15 June 2004; and

- BLCL, as the Land Holder, is to establish olive Grovelots on the Project land.

19. To participate in the Project a potential Grower will need to complete the application form and power of attorney attached to the Product Disclosure Statement. On acceptance into the Project BOML will execute a Licence Agreement and a Management Agreement on the Grower's behalf under the power of attorney the potential Grower grants BOML on Application to enter the Project. On execution of the Licence Agreement and Management Agreement a Grower becomes a party to the Project's Constitution. The Licence Agreement and Management Agreement can be executed when the Grower's Grovelot has been established on or before 15 June 2004.

20. BOML's responsibilities as Responsible Entity for the Project include the following:

- Register the Project as a Managed Investment Scheme pursuant to the *Corporations Act 2001*;
- Issue the Product Disclosure Statement;
- Comply with the terms of the Project Constitution;
- Enter into the Custodian Agreement with McMahon Clarke Legal ('the Custodian') under which the Custodian will hold project property as agent for BOML;
- Register the Compliance Plan for the Project with the Australian Securities and Investment Commission;
- Lease the Project land from BLCL and register the lease under the *New South Wales Real Property Act 1900*;
- Enter into a Licence Agreement with each Grower and BLCL;
- Enter into a Management Agreement with each Grower; and
- Enter into the Olive Oil Purchase Agreement, as agent for the Growers, with IOPL to sell all of the processed olive oil attributable to the Project.

**Draft Constitution**

21. The Dictionary of Terms is contained at Schedule 1 of the Constitution. The defined terms listed below will also apply to other Project documents unless they are defined within the specific Project document.

Applicant	A person who has applied to become a Grower in the Project by completing an application form but who is not yet a Grower;
Application	The process a person undertakes to complete an application form from the Product Disclosure Statement and deliver it to the Responsible Entity;
Application Fund	A bank account into which the Application Money is deposited;
Application Money	The money paid by Applicants to acquire an Interest;
ASIC	The Australian Securities and Investments Commission;
Call Option	An option to be granted to a Grower to acquire shares in the capital of the Land Holder on the terms and conditions set out in Schedule 5;
CPI	The Consumer Price Index (All Groups) Brisbane as published by the Australian Bureau of Statistics;
Grovelot	That area of the Land which is licensed by the Responsible Entity to each Grower. Each Grovelot will be approximately 0.256 hectares planted or to be planted on or before 15 June 2004 with approximately 80 olive trees;
Grower	A person who has acquired, and still holds, a Grovelot or an interest in a Grovelot and who accordingly becomes a party to the Constitution;
Interest	The interest in the Project a Grower acquires by applying under a Product Disclosure Statement and having the Application accepted by the Responsible Entity. An Interest includes: <ul style="list-style-type: none"> <li>(a) a Grower's participation in a Licence Agreement and Management Agreement (which in turn comprises a right to use and occupy a Grovelot);</li> </ul>

- (b) a legal interest in the trees on the Grower's Grovelot from the date on which a Grower's Interest is issued until the end of the Project;
- (c) the Grower's business in carrying on the business of cultivating, growing, tending and harvesting olive trees and processing and selling the olive oil;
- (d) the net proceeds which result from the Grower carrying on its business; and
- (e) the Grower's proportional interest in the Project Property including in the Proceeds Fund as determined by clause 16.

For the sake of clarity, an Interest can continue as the case requires despite the end or termination of a Licence or Management Agreement in order to give effect to this Constitution (e.g. the term of the agreement may have expired, but the Grower is still due the net proceeds of harvest);

Land Holder	Barkworth Land Corporation Limited;
Proceeds Fund	The fund into which proceeds from the businesses conducted by Growers is deposited;
Project Property	That property determined as being property of the Project in accordance with the definitions of 'Scheme Property' contained in Section 9 of the Corporations Act; and
Register	The register of Growers required to be kept according to the <i>Corporations Act 2001</i> .

22. The Commencement Date as defined in the Licence Agreement and Management Agreement in Schedule 2 respectively means the date on which the Responsible Entity accepts the Grower's Application in accordance with clause 13 of the Constitution. Clause 13.3(c) of the Constitution requires that the terms of clause 2(a)(ii) of the Licence Agreement must be satisfied. Clause 2(a)(ii) of the Licence Agreement requires that the Capital Works be completed by 31 May 2004 or no later than 15 June 2004. Accordingly, all Capital Works on a Grovelot must be completed prior to the date on which a Grower's Interest is issued. Capital Works as defined in the Licence Agreement in Schedule 2 means the infrastructure and capital works BLCL has carried out or agreed to carry out, pursuant to clause 2(a)(ii) of the Licence Agreement.

23. BOML is the Responsible Entity and intends to issue a Product Disclosure Statement to invite the public to participate in the Project. Each Applicant whose Application is accepted will become a Grower in respect of one or more Grovelots. Each Applicant will be granted a licence from BOML in respect of one or more Grovelots on the terms set out in the Licence Agreement which permits each several Grower to use the Grovelots for the purpose of carrying on the business of cultivating, growing, tending and harvesting olive trees and processing and selling the olive oil. Each Grower engages BOML under the Management Agreement to manage the Growers' Grovelots and to process the olives grown and sell the oil produced on behalf of the Grower.

24. Under clause 2(a) an Applicant must pay an initial amount of \$5,227.75 per Interest in order to acquire an Interest. Applications from Applicants to acquire an Interest in the Project are to be made on the application form and power of attorney, attached to the Product Disclosure Statement. The Application Money for each Grovelot is to be paid in full at the time of the Application (clause 13.1), or by instalments in accordance with clause 13.2. All cheques or payment orders in relation to Applications for Interest are to be drawn in favour of BOML or its appointed agent (clause 12.1). BOML will open an Application Fund account, into which all money received from Applicants will be deposited, and a Proceeds Fund account into which proceeds from the businesses conducted by Growers will be deposited (clause 12.2).

25. Where BOML allows an Applicant to pay the Application Money by instalment then the Applicant must pay BOML, at the time of delivering the Application, the amount shown in the Application under the heading Deposit. The amount shown in the Application under the heading Balance must be paid by the Applicant (or Grower if that Application has been accepted by BOML), to BOML by the date specified, which must be within 45 days of the date the Deposit was paid (clause 13.2).

26. BOML may accept or refuse Applications in its absolute discretion (clause 13.4). On acceptance of an Application, BOML is taken to have issued an Interest to an Applicant and BLCL and the Applicant will be deemed to have been granted the Call Options (clauses 13.5 and 13.6). Under clause 14.1 a person is a Grower in the Project where they hold an Interest. To hold an Interest a Licence Agreement and Management Agreement must be entered into and be in force. Within 21 days of acceptance BOML must register the description of the Grovelot and the Grower in the Register.

27. BOML is not able to transfer money held in the Application Fund until BLCL is able to grant the licence under the Licence Agreement (clause 14.1 and clause 15), the Licence Agreement and Management Agreement have been entered into and Interests have been issued. Any bank interest earned on Application Money will be retained by BOML (clauses 12.3 and 16.1). Once an Applicant becomes a Grower they acknowledge further amounts are payable pursuant to the Licence Agreement and Management Agreement (clauses 2(b) and 7.1).

28. A Grower has an interest in the Proceeds Fund equal to the proportion the Grower's Interest or Interests bear to the total number of Growers' Interests (clause 16.2). BOML must pay proceeds from the sale of olive oil, receipts from insurances from which the Growers are entitled to benefit and any other amounts related to the proceeds of the Growers' Interests into the Proceeds Fund (clause 31.8). BOML will deduct all fees and other amounts payable under the Licence Agreement, Management Agreement and Constitution from the Proceeds Fund. Any amounts remaining in the Proceeds Fund after all deductions are made by BOML must be paid by BOML to the relevant Grower within 5 months after 30 June each year (clause 31.9).

29. If a Grower's Grovelot is partially or totally destroyed, or the level of production is otherwise reduced or inadequate compared to other Grovelots, BOML will adjust the Grower's interest in the Proceeds Fund to reflect the reduced number of olive trees or olives on the Grower's Grovelot brought about by the destruction or the reduced or inadequate production (clause 31.12). Insurance proceeds are to be divided between those Growers affected by the insurance claim (clause 31.10).

30. A Grower who makes an election under clause 6.7 of the Management Agreement to harvest and process their olives and market their olive oil does not have any entitlement to the harvested olives, processed olive oil or the Proceeds Fund for the period the Grower made an election (clause 31.4). A Grower who makes an election is **not** covered by this Product Ruling (refer paragraph 8 above).

### **Option to acquire an equity interest in BLCL**

31. Schedule 5 of the Constitution outlines the terms and conditions of Call Options. BLCL will issue each Grower, or nominated associate, with the number of Call Options that is equal to the number of Grovelots that have been allocated to the Grower under clause 13.6(a) of the Constitution. The options to subscribe for shares are exercisable between 1 July 2024 and 30 July 2024 (clause 1.2 of Schedule 5). A Grower or its associate may exercise the option by serving an exercise notice of the option on BLCL and paying the

subscription price of \$1,000 per option. The exercise of options will only be effective if at least 30% of all options issued are exercised.

32. For each share in BLCL issued to a Grower, or nominated associate, a share will be issued to an entity nominated by BLCL. Accordingly the Growers will at all times only acquire a 50% interest in BLCL.

### **Licence Agreement**

33. The agreement will be between BLCL as the Land Holder, BOML as the Responsible Entity and the Grower named in Schedule 1 of the agreement. BOML is not able to accept an Application Form from an Applicant to participate in the Project until after BLCL has completed all necessary Capital Works on the Project land (clause 2). The Capital Works are to be completed by BLCL by no later than 15 June 2004 and are listed at clause 2(a)(ii) as follows::

- (a) Prepare, for the planting and cultivation of olive trees, that part of the Grovelot which can reasonably be used for the cultivation of olives;
- (b) if required, construct or cause to be constructed a fence along the external boundary of the Land or such other location as the Responsible Entity deems suitable in order to restrain livestock from neighbouring properties from straying onto the Grovelot;
- (c) construct and continue to maintain suitable access roads and pathways to and from the Grovelot;
- (d) install appropriate irrigation equipment and carry out the necessary irrigation works to ensure proper reticulation of water to the olive trees on the Grovelot;
- (e) ensure and subsequent to the entry of this Agreement continue to ensure, that the Grovelot has adequate drainage, and perform work necessary to help prevent soil erosion on the Grovelot;
- (f) control, so far as is reasonably possible, any pests and competitive weeds which may affect the growth or yield of the olive trees on the Grovelot;
- (g) plant 80 olive trees on each Grovelot, stake, survey and erect stakes and if required, construct trellising in accordance with good horticultural practices so that the olives from the olive trees on the Grovelot can be harvested; and

- (h) by the date of this Agreement, have performed any other works, services or things which, in the reasonable opinion of the Land Holder, are incidental or ancillary to the effective establishment and provision of the works referred to in clauses 2(a)(ii)A to 2(a)(ii)G.

34. The Licence Agreement is subject to and conditional upon the Grower entering into a Management Agreement with BOML (clause 2). Under clause 3.1 BOML grants to the Grower, starting on the Commencement Date, a contractual licence to use and occupy the Grovelot(s) only for the purpose of cultivating, growing and tending the olive trees and harvesting of the olives from the olive trees. The licence also enables a Grower to use in common with all other Growers' the infrastructure on the land required for the Project and to have access through the land at all reasonable times in order for the Grower to conduct its business on the Grovelot(s).

35. The Grower must pay the licence fee under the Agreement of \$233.75 per annum per Grovelot (clause 6.1). This amount will be indexed by the CPI from the year ended 30 June 2007. Under clause 7 the Grower must only use the Grovelot(s) for the purpose of conducting the business of cultivating, growing, maintaining and harvesting olive trees and related operations and must comply with good horticultural and environmental practices and relevant laws and regulations. The Grower must permit access to the Grovelot(s) for the purposes of the Project under the Licence Agreement and the Management Agreement.

36. Under clause 8.2 the Land Holder (BLCL) is to maintain water licences for the term of the Agreement and ensure that its rights under the water licences are fully exploited to maximise the use and enjoyment of them by the Grower.

37. At the expiration of the term of the Licence Agreement, each Grower must return the Grovelot(s) to BLCL in good condition but is not required to remove the olive trees or restore the Grovelot(s) to their original condition (clause 4.2).

## **Management Agreement**

38. The Management Agreement is between BOML as the Responsible Entity and Manager of the Project and the Grower named in Schedule 1. The Management Agreement is subject to and conditional upon the Grower entering into a Licence Agreement with BOML (clause 2).

39. Under clause 3 the Grower engages BOML as an independent contractor to manage the Grovelot(s) on the terms and conditions contained in the agreement. The agreement commences on the Commencement Date and ends the earlier of the termination of the

Grower's Interest in the Project, 30 June 2024, termination of the Licence Agreement or termination of the Project (clause 4).

40. From the date the agreement commences, in accordance with clause 6.1, BOML agrees to provide initial management duties with greater intensity, care and attention than the ongoing management duties to be provided under clause 6.3. The initial management duties must be carried out from the date of commencement of the agreement to 30 June 2004. Under clause 6.1 BOML must do the following:

- (a) Tie and stake the olive trees or attach them to trellises;
- (b) Prune and shape olive trees;
- (c) Tend the olive trees and Grovelot in a proper and skilful manner, this includes but is not limited to:
  - (i) Fertilise and condition the soil on the Grovelot as required to ensure the initial establishment, growth and future yield of the olive trees;
  - (ii) Control as far as reasonably possible any pests or competitive weeds which may affect the initial establishment, growth or yield of the olive trees including applying herbicides or pesticides to olive trees to protect them from such infestations or competing growths;
  - (iii) Keep the improvements on the Grovelot in good repair;
  - (iv) Maintain firebreaks in accordance with sound agricultural and environmental practices, and in accordance with any legislation or regulation;
  - (v) Inspect and repair all stakes, fences and irrigation equipment;
  - (vi) Irrigate the Grovelot using the irrigation system licensed to the Grower;
  - (vii) Examine each of the olive trees to determine whether any olive trees need to be replaced or may need to be replaced and destroy olive trees as required;
- (d) Embark on such operations as may be required to prevent or combat land degradation on the Grovelot or land surrounding the Grovelot; and
- (e) Attend to all administrative duties associated with the allocation and maintenance of the Grower's Grovelot, including but not limited to complying with the Grower's licence conditions under the Licence

Agreement (except those relating to payment of fees) and compliance costs.

41. At clause 6.3 BOML must continue to maintain the Grower's Grovelot following the completion of the duties in clause 6.1. BOML must cultivate and tend the Grovelot, harvest the olives from the Grovelot, process the olives into olive oil and sell the olive oil in a manner according to sound agricultural, environmental and proper workplace practices, including but not limited to carrying out the following duties to the extent necessary:

- (a) Tie and stake olive trees or attach them to trellises;
- (b) Prune and shape olive trees.
- (c) Tend the olive trees and Grovelot in a proper and skilful manner, this includes but is not limited to:
  - (i) Fertilise and condition the soil on the Grovelot as required to ensure the growth and future yield of the olive trees;
  - (ii) Control as far as reasonably possible any pests or competitive weeds which may affect growth or yield of the olive trees including applying herbicides or pesticides to olive trees to protect them from such infestations or competing growths;
  - (iii) Keep the improvements on the Grovelot in good repair;
  - (iv) Maintain firebreaks in accordance with sound agricultural and environmental practices, and in accordance with any legislation or regulation;
  - (v) Inspect and repair all stakes, fences and irrigation equipment;
- (d) Irrigate the Grovelot using the irrigation system licensed to the Grower;
- (e) Examine each of the olive trees to determine whether any olive trees need to be replaced or may need to be replaced and destroy olive trees as required
- (f) Embark on such operations as may be required to prevent or combat land degradation on the Grovelot or land surrounding the Grovelot;
- (g) Attend to all administrative duties associated with the allocation and maintenance of the Growers Grovelot, including but not limited to complying with the Grower's licence conditions under the Licence

- Agreement (except those relating to payment of fees) and compliance costs;
- (h) On behalf of the Grower, harvest the olive trees on the Grovelots at or around the time estimated by the Responsible Entity to maximise the produce from all of the Grovelots. However, the Responsible Entity is not required to do this if the Grower has elected to harvest its own Grovelots in accordance with Clause 6.7;
  - (i) On behalf of the Grower, procure the processing of all harvested olives into olive oil. However, the Responsible Entity is not required to do this if the Grower has elected to harvest then process olives into olive oil in accordance with clause 6.7 of the Agreement;
  - (j) On behalf of the Grower, market and sell the olive oil, using reasonable endeavours to obtain the maximum price available for the olive oil. However, the Responsible Entity is not required to do this if the Grower has elected to market and sell their olive oil in accordance with clause 6.7; and
  - (k) Unless the Grower has made an election pursuant to clause 6.7, then account to the Grower for the proceeds of the sale of the olive oil. In accounting to the Grower for the proceeds of the sale of the olive oil, the Responsible Entity need not refer or consider the quality or quantity of olives produced from an individual Grovelot. Rather the Responsible Entity will distribute the proceeds in accordance with the terms of the Constitution.

42. Under clause 6.7 the Grower may elect to harvest and process the olives and market the olive oil. An election will not be valid until after the commencement of the third year of the agreement. Growers who make an election will be entitled to a reduction in the fees payable to BOML. The amount of the reduction is the fees payable by a Grower who does not make an election, less 25%.

43. At clause 7.1 the management fees BOML is entitled to receive for carrying out its initial management duties under clause 6.1 is \$4,994 per Grovelot, payable on or before 30 June 2004, unless BOML has agreed to accept payment of the Application Money by instalment in accordance with clause 13.2 of the Constitution.

44. In accordance with clause 7.2 BOML will be entitled to receive the following management fees for carrying out its duties under clause 6.3:

- For the period from 1 July 2004 to 30 June 2005 BOML is entitled to be paid \$2,266 per Grovelot, payable in advance on or before 31 October 2004; and
- For the period from 1 July 2005 to 30 June 2006 BOML is entitled to be paid \$2,266 per Grovelot, payable on or before 31 October 2005.

45. Clause 8.1 details the management fees BOML is entitled to receive for carrying out its duties under clause 6.3 beyond 30 June 2006. There is a fixed fee component of \$1,210 for the year ended 30 June 2007, \$1,320 for the year ended 30 June 2008 and \$1,430 for the year ended 30 June 2009 which is indexed by 2.5% in each subsequent financial year of the Project. There is also an incentive fee so that if the gross income is greater than the threshold income per Grovelot, the fee will be 20% of the amount the gross income exceeds the threshold income. The gross income is the income earned from the sale of the relevant Grower's Interests in the olive oil in the year in which the management fee is being calculated. The threshold income per Grovelot and the relevant percentage over the life of the Project are detailed in the table in clause 8.1(c)(ii).

46. At clause 8.1(d) the Grower instructs BOML to make the payment of the fees calculated under clause 8.1 directly from gross income earned from the sale of the relevant Grower's Interest in the olive oil for the relevant year before making any distribution of income to the Grower. At clause 8.1(e) the Grower instructs BOML to pay any fees owed by the Grower to BOML pursuant to the Licence Agreement, before making any distribution of income to the Grower.

47. Under clause 10.1 BOML must maintain, at its own cost, public risk insurance for an amount of not less than \$5 million. BOML must insure on behalf of the Grower the olive trees, however, BOML is not required to insure the olives or the olive oil (clause 10.2). A Grower is at liberty to take out additional insurance at their own cost and expense (clause 10.3).

48. Clause 11 enables BOML to delegate any of its duties or functions under the agreement. The Management Agreement terminates if the Licence Agreement is terminated in respect of a Grower. If BOML is entitled to terminate the agreement it has absolute discretion to do so as against a particular party, and that termination does not affect the obligations of any other party to the agreement (clauses 13.4 and 13.5).

**Custodian Agreement**

49. The Custodian Agreement for the Project is between BOML as the Responsible Entity and McMahon Clarke Legal as the Custodian. Under clause 2(a) the Custodian's role will be to hold Project Property as agent for BOML. Project Property as defined in Schedule 1 means cash amounts received by BOML including Application Money from Growers within the last six months or any cash held by the Custodian on behalf of BOML pending payment to Growers or to meet expected expenses.

50. The Custodian Agreement will commence on the date the Project is registered with ASIC and will continue until the winding up of the Project, unless terminated earlier as provided under the agreement (clause 4).

**Lease of Project Land**

51. BLCL will lease the land on which the Project will be conducted to BOML. The lease will be over proposed Lot 1, 81.36 hectares, and proposed Lot 4, 234.8 hectares. Rates, taxes and other outgoings will be payable by BOML (clause 4). The licence fees payable under the lease will be \$1 plus an amount equal to the licence fees actually received by BOML under the Licence Agreements BOML enters into with Growers in the Project (clause 3).

52. Interests in the Project will not be issued until there is an executed lease in place between BLCL and BOML. This executed lease will be lodged for registration, under the *New South Wales Real Property Act 1900*, within 45 days from 15 June 2004.

**Olive Oil Purchase Agreement Draft 3**

53. The agreement is between IOPL and BOML. BOML, as agent for the Growers, has agreed to sell to IOPL all of the processed oil from the Project. IOPL markets its processed olive oil through Origin Olives Australia Pty Ltd ('OOA') under the Viva brand name. The Project will be a preferred supplier of olive oil, subordinate only to processed olive oil supplied by existing Barkworth Olive Projects (clause 1).

54. The sale and purchase of the processed olive oil will commence from the commercial production period, being the year ending 30 June 2007, and continue for the term of the Project (clause 2).

**Water Supply**

55. The Water Supply Agreement is between BLCL who will own the Project land and BOGL who holds the water licences. BOGL has agreed to supply BLCL with adequate water in order for BLCL to comply with its obligations under the Licence Agreements. The Water Supply Agreement commences on the earlier of the date the agreement is signed by both parties or the commencement of the first Licence Agreement for the Project. The agreement will end 20 years after it commences (clause 4).

**Finance**

56. Growers can fund their involvement in the Project themselves or borrow from an independent lender. Barkworth Finances Pty Ltd, and its associates, will neither offer finance nor promote any 'preferred financiers' to Growers.

57. This Ruling does not apply if the finance arrangement entered into by the Grower includes or has any of the following features:

- a finance arrangement entered with the Responsible Entity or any associate of the Responsible Entity; or
- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL or the funding arrangements transform the Project into a 'scheme' to which Part IVA may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project are involved or become involved in the provision of finance to Growers for the Project.

## **Ruling**

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### **Application of this Ruling**

58. This Product Ruling applies to a Grower who is accepted to participate in the Project on or before 15 June 2004 and the Grower has executed the Licence Agreement and the Management Agreement on the date of acceptance. The Grower's participation in the Project must constitute the carrying on of a business of primary production.

59. This Ruling does **not** apply to Growers who:

- are excluded from the Ruling as described in the Class of Persons or the Arrangement sections of this Product Ruling; or
- are accepted to participate in the Project on or after 16 June 2004.

### **The Simplified Tax System ('STS')**

#### ***Division 328***

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

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

### **Qualification**

61. 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.

**Assessable Income*****Section 6-5 and section 328-105***

62. 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.

63. A Grower who is not an 'STS taxpayer' recognises ordinary income from carrying on the business of cultivating olive trees and harvesting the olives for the production and sale of olive oil at the time that income is derived.

64. A Grower who is an 'STS taxpayer' recognises ordinary income from carrying on the business of cultivating olive trees and harvesting the olives for the production and sale of olive oil at the time that income is received (paragraph 328-105(1)(a)).

**Deductions for management fees and licence fees*****Section 8-1 and 328-105***

65. A Grower may claim, on a per Grovelot basis, tax deductions for the following revenue expenses.

<b>Fee Type</b>	<b>30/6/2004</b>	<b>30/6/2005</b>	<b>30/6/2006</b>
Management fee	\$4,994 – See Notes (i) & (ii)	\$2,266 – See Notes (i) & (ii)	\$2,266 – See Notes (i) & (ii)
Licence fee	See Notes (i) & (iii)	\$233.75 – See Notes (i) & (ii)	\$233.75 – See Notes (i) & (ii)
Interest	See Note (iv)	See Note (iv)	See Note (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 management fees shown in the Management Agreement and the licence fee, for the years ending 30 June 2005 and 30 June 2006, shown in the Licence Agreement are deductible under section 8-1 in full in the year that they are incurred (where the Grower is not an 'STS taxpayer') or, under paragraph 328-105(1)(b)

- in the year in which they are paid (where the Grower is an 'STS taxpayer');
- (iii) The deduction for the licence fee payable for the year ended 30 June 2004 is \$19.50 per month for each month or part month that the Grower holds a licence over the land. This means that the full \$233.75 payable for the year ended 30 June 2004, will not be deductible. See paragraphs 93 and 94;
  - (iv) This Ruling does not apply to Growers who choose to prepay fees for management services or licence fees (see paragraph 96). Amounts that are prepaid for a period that extends beyond the income year in which the expenditure is incurred may be subject to the prepayment provisions in sections 82KZME to 82KZMF of the ITAA 1936. Any Grower who prepays such amounts may request a private ruling on the taxation consequences of their participation in the Project; and
  - (v) The deductibility or otherwise of interest arising from loan agreements entered into with financiers is outside the scope of this Ruling. Growers who borrow from lenders may request a private ruling on the deductibility of the interest incurred.

## **Deductions for horticultural plants**

### ***Division 40***

66. Each Grower will also be entitled to tax deductions relating to the olive trees planted on the Grovelot. 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.

67. An olive tree is considered to be a 'horticultural plant' as defined in subsection 40-520(2). A Grower holds a licence to cultivate olive trees on a designated area of land called a Grovelot for the growing of olives for commercial gain. As a Grower holds the Grovelot under a licence, 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.

68. The deduction is determined using the formula in section 40-545. Olive trees have an 'effective life' of greater than 30 years and, 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).

BOML will notify Growers when their olive trees enter their first commercial season and the amount that may be claimed.

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

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

69. For a Grower who is an individual and who enters the Project by 15 June 2004 in the year ended 30 June 2004 the rule in section 35-10 may apply to the business activity comprised by their involvement in this Project.

70. Under paragraph 35-55(1)(b) the Commissioner will decide for these Growers that the rule in section 35-10 does not apply to this activity for the income years ending **30 June 2004 to 30 June 2007** provided that the Project is carried out in the manner described in this Ruling.

71. 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 103 in the Explanation 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)).

72. 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.

73. Growers are reminded of the important statement made on Page 1 of this Product Ruling. Therefore, Growers should not see the Commissioner’s decision to exercise the discretion in paragraph 35-55(1)(b) as an indication that the Tax Office sanctions or guarantees the Project or the product to be commercially viable. An assessment of the Project or the product from this perspective has not been made.

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

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

- expenditure by a Grower does not fall within the scope of sections 82KZME - 82KZMF;
- 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.

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**Explanation**

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

75. For the amounts set out in paragraphs 65 to 68 above to constitute allowable deductions the Grower's activities of cultivating olive trees and harvesting the olives for the production and sale of olive oil as a participant in the Barkworth Olives Project No 8 must amount to the carrying on of a business of primary production.

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

77. For schemes such as that of the Barkworth Olives Project No 8, 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) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

78. Generally, a Grower will be carrying on a business of cultivating olive trees and harvesting the olives for the production and sale of olive oil, and hence primary production, if:

- the Grower has an identifiable interest in the land (by lease) or rights over the land (by licence) on which the Grower's olive trees are established;

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- the Grower has a right to harvest and sell the olives and olive oil produce from those olive trees;
- the cultivating of the olive trees and harvesting the olives for the production and sale of olive oil are carried out on the Grower's behalf;
- the activities of the Grower are typical of those associated with a business of cultivating olive trees and harvesting the olives for the production and sale of olive oil; and
- the weight and influence of general indicators point to the carrying on of a business.

79. In this Project, each Grower enters into a Licence Agreement and a Management Agreement.

80. Under the Licence Agreement, each individual Grower will have rights over a specific and identifiable area of 0.256 hectares or more of land. The Licence Agreement provides the Grower with an ongoing interest in the specific trees on the licenced area for the term of the Project. Under the licence, the Grower must use the land in question for the purpose of carrying out activities of cultivating olive trees and harvesting the olives for the production and sale of olive oil and for no other purpose. The licence allows BOML to come onto the land to carry out its obligations under the Management Agreement.

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

82. BOML is also engaged to harvest the olives grown on the Grower's Grovelot for the production and sale of olive oil on the Grower's behalf.

83. 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.

84. 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 olive oil 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.

85. The pooling of olives and olive oil produce from trees grown on the Grower's Grovelot with the olives and olive oil produce of other Growers is consistent with general horticultural practices. Each Grower's proportionate share of the sale proceeds of the pooled olives and olive oil products will reflect the proportion of the trees contributed from their Grovelot.

86. BOML's services are also consistent with general horticultural practices. They are of the type ordinarily found in horticultural ventures that would commonly be said to be businesses. While the size of a Grovelot is relatively small, it is of a size and scale to allow it to be commercially viable.

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

88. The activities of cultivating olive trees and harvesting the olives for the production and sale of olive oil, 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 Grower's activities of cultivating olive trees and harvesting the olives for the production and sale of olive oil in the Barkworth Olives Project No 8 will constitute the carrying on of a business.

## **The Simplified Tax System**

### ***Division 328***

89. 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.

90. 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***

91. 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.

92. The management fee and, subject to paragraphs 93 and 94, the licence fees will relate to the gaining of income from the Grower's business of cultivating olive trees and harvesting the olives for the production and sale of olive oil (see above), and hence have a sufficient connection to the operations by which income (from the harvesting and sale of olives and olive oil produce) is to be gained from this business. They will thus be deductible under the first limb of section 8-1. Further, no 'non-income producing' purpose in incurring the fee is identifiable from the arrangement. The fee appears to be reasonable. Subject to paragraphs 93 and 94, there is no capital component of this fee. The tests of deductibility under the first limb of section 8-1 are met. Subject to paragraphs 93 and 94, the exclusions do not apply.

93. One of the exclusions under section 8-1 relates to expenditure that is capital, or is capital in nature. Any part of the expenditure of a Grower entering into a horticulture business which is attributable to acquiring an asset or advantage of an enduring kind is generally capital or capital in nature and hence will not be deductible under section 8-1.

94. The Commissioner is of the view that, a portion of the initial licence fee payable by a Grower, accepted into the Project on or before the 15 June 2004, will be capital expenditure. Therefore, the amount allowed as a deduction under section 8-1 for the initial licence fee of \$233.75 per Grovelot will be calculated on a pro-rata monthly basis of \$19.50 for each month or part month that the Grower holds a licence over an established Grovelot.

### **Interest deductibility**

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

95. 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.

### **Prepayment provisions**

#### ***Sections 82KZL to 82KZMF***

96. 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.

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

97. Under the Arrangement to which this Product Ruling applies management fees and licence fees are incurred annually. Accordingly, the prepayment provisions in sections 82KZME and 82KZMF have no application to this Arrangement. A Grower who is an 'STS taxpayer' can, therefore, claim a deduction for each of the relevant amounts in the income year in which the amount is paid. A Grower who is not an 'STS taxpayer' can claim a deduction for each of the relevant amounts in the income year in which the fee is incurred.

98. However, sections 82KZME and 82KZMF may have relevance if a Grower in this Project prepays all or some of the expenditure payable under the Management Agreement or Licence Agreement. Where such a prepayment is made these prepayment provisions will also apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes them from the operation of section 82KZMF.

99. As noted in the Ruling section above, Growers who prepay fees are not covered by this Product Ruling and may instead request a private ruling on the tax consequences of their participation in this Project.

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

#### ***Division 35***

100. 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 incurred by an individual (including an individual in a general law partnership) from certain business activities will not be allowable in an income year unless:

- the 'Exception' in subsection 35-10(4) applies;
- one of four objective tests in sections 35-30, 35-35, 35-40 or 35-45 is satisfied; or
- if one of the objective tests is not satisfied, the Commissioner exercises the discretion in section 35-55.

101. 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.

102. 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.

103. 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 'Participant

Growers' who participate in the Project they are beyond the scope of this Product Ruling and are not considered further.

104. 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).

105. 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 one Grovelot in the Project is unlikely to pass one of the objective tests until the income year ended 30 June 2010. Growers who acquire more than one Grovelot in the Project may however, find that their activity meets one of the tests in an earlier income year.

106. 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.

107. The first arm of the discretion in paragraph 35-55(1)(a) relates to 'special circumstances' applicable to the business activity, and has no relevance for the purposes of this Product Ruling. However, the second arm of the discretion in paragraph 35-55(1)(b) may be exercised by the Commissioner where:

- (i) the business activity has started to be carried on;
- (ii) because of its nature, it has not satisfied one of the objective tests; and
- (iii) there is an objective expectation that the business activity of an individual taxpayer will either pass one of the objective tests or produce a taxation profit within a period that is commercially viable for the industry concerned.

108. Information provided with the application for this Product Ruling indicates that a Grower who acquires an Interest in the Project is expected to be carrying on a business activity that will either pass one of the objective tests, or produce a taxation profit, for the year ended 30 June 2008. The Commissioner will decide for such a Grower that it would be reasonable to exercise the second arm of the discretion until the year ended 30 June 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 paragraphs 69 & 70), in the manner described in the Arrangement (see paragraphs 14 to 57). 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 expert and additional expert and scientific evidence provided by BOML with the application; 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 BOML.

### **Section 82KL – recouped expenditure**

111. 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 anti-avoidance provisions**

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 Barkworth Olives Project No 8 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 65 to 68, that would not have been obtained but for the scheme. However, it is not possible to conclude the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

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 olives and olive oil 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**

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 2003 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 1/1/2004 to 30/6/2004	\$4,400*
Carrying out of upgrade of power for your vineyard as quoted	<u>\$2,200*</u>
Total due and payable by 1 January 2004 (includes GST of \$600)	<u>\$6 600</u>

\*Taxable supply

Susan pays the invoice by the due date and calculates her input tax credit on the management fee (to be claimed through her Business Activity Statement) as:

$$1/11 \times \$4400 = \$400.$$

Hence her outgoing for the management fee is effectively \$4400 *less* \$400, or \$4000.

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

$$1/11 \times \$2200 = \$200.$$

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

In preparing her income tax return for the year ended 30 June 2004, 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).

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**Commissioner of Taxation**

24 March 2004

<i>Previous draft:</i>	- ITAA 1936 177D(b)
Not previously issued in draft form	- ITAA 1997 6-5 - ITAA 1997 8-1
<i>Related Rulings/Determinations:</i>	- ITAA 1997 17-5
TR 92/1; TR 92/20; TD 93/34;	- ITAA 1997 Div 27
TR 97/11; TR 97/16; TR 98/22;	- ITAA 1997 Div 35
TR 2000/8; PR 1999/95	- ITAA 1997 35-10 - ITAA 1997 35-10(2) - ITAA 1997 35-10(3)
<i>Other Rulings/Determinations:</i>	- ITAA 1997 35-10(4)
TR 2001/14	- ITAA 1997 35-30 - ITAA 1997 35-35
<i>Subject references:</i>	- ITAA 1997 35-40
- carrying on a business	- ITAA 1997 35-45
- commencement of business	- ITAA 1997 35-55
- fee expenses	- ITAA 1997 35-55(1)
- interest expenses	- ITAA 1997 35-55(1)(a)
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- producing assessable income	- ITAA 1997 40-520(2)
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- schemes and shams	- ITAA 1997 40-545
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- tax avoidance	- ITAA 1997 Subdiv 328-F - ITAA 1997 Subdiv 328-G - ITAA 1997 328-105
<i>Legislative references:</i>	- ITAA 1997 328-105(1)(a)
- TAA 1953 Part IVAAA	- ITAA 1997 328-105(1)(b)
- ITAA 1936 Div 3 Subdiv H Pt III	- Copyright Act 1968
- ITAA 1936 82KL	- Corporations Act 2001
- ITAA 1936 82KZL	- New South Wales Real Property Act
- ITAA 1936 82KZME	
- ITAA 1936 82KZMF	
- ITAA 1936 Pt IVA	<i>Case references:</i>
- ITAA 1936 177A	- FCT v. Lau (1984) 6 FCR 202;
- ITAA 1936 177C	84 ATC 4929; (1984) 16 ATR 55
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