



PR 2005/46 - Income tax: Australian Bight Abalone Project

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 This document has changed over time. This is a consolidated version of the ruling which was published on *21 September 2005*



Product Ruling

Income tax: Australian Bight Abalone Project

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Potential participants may wish to refer to the Tax Office website at **www.ato.gov.au** or contact the Tax Office directly to confirm the currency of this Product Ruling or any other Product Ruling that the Tax Office has issued.

Preamble

*The number, subject heading, **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

The Tax Office **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 and how the product fits an existing portfolio. 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 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, 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 Tax Office will be undertaking review activities to confirm the arrangement has been implemented as described below and to ensure that the participants in the arrangement include in their income tax returns income derived in those future years.

Terms of use of this Product Ruling

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

What this Product Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates.

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 of the ITAA 1997;
 - section 17-5 of the ITAA 1997;
 - Division 27 of the ITAA 1997;
 - Division 35 of the ITAA 1997;
 - Division 40 of the ITAA 1997;
 - Division 70 of the ITAA 1997;
 - Division 328 of the ITAA 1997;
 - section 82KL of the *Income Tax Assessment Act 1936* (ITAA 1936);
 - section 82KZL of the ITAA 1936;
 - sections 82KZME and 82KZMF of the ITAA 1936; and
 - Part IVA of the 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. 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 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 those persons who enter into the arrangement described below on or after the date this Ruling is made. They will have a purpose of staying in the arrangement until it is completed (that is, being a party to the relevant agreement until their term expires), and deriving assessable income from this involvement as set out in the description of the arrangement. In this Ruling, each of these persons, referred to as 'Growers', will be wholesale clients for the purpose of the *Corporations Act 2001* or will have accepted an offer which qualifies as a small scale offer for the purpose of the *Corporations Act 2001*.

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 harvest, market and sell their Abalone Produce;
- choose to prepay fees payable under the arrangement;
or
- enter into this arrangement after 15 June 2005.

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

11. This Ruling applies prospectively from 6 April 2005, 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 21 September 2005, applies on and from 1 July 2005.

Withdrawal

13. This Product Ruling is withdrawn and ceases to have effect after 30 June 2008. The Ruling continues to apply, in respect of the tax law(s) ruled upon, to all persons within the specified class who enter into the arrangement specified below. Thus, the Ruling continues to apply to those persons, even following its withdrawal, who entered into the specified arrangement prior to withdrawal of the Ruling. This is subject to there being no change in the arrangement or in the persons' involvement in the arrangement.

Arrangement

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

- Application for a Product Ruling received by the Tax Office on 17 December 2004 as constituted by documents provided on 17 December 2004, 13, 19 and 28 January 2005, 1, 14 and 15 February 2005, 14, 17, 24, 29 and 30 March 2005 and additional correspondence dated 20 December 2004, 13 and 20 January 2005, 1, 7 and 15 February 2005, 14, 17, 24, 29 and 30 March 2005;
- Correspondence from the Tax Office to the Applicant dated 13, 17 and 19 January 2005, 10 February 2005 and 16 March 2005;
- Correspondence from Primary Industries and Resources SA dated 14 January 2005 and 8 February 2005;
- Draft undated **Information Memorandum** received by the Tax Office on 24 March 2005;
- Draft undated **Application Form** received by the Tax Office on 15 February 2005;
- Draft undated **Constitution** received by the Tax Office on 30 March 2005;
- Draft undated **Aquaculture and Cage Rental Agreement** between Australian Bight Infrastructure Pty Ltd (Marine Lease Owner), Australian Bight Abalone Limited (Responsible Entity) and the Grower received by the Tax Office on 30 March 2005;
- Draft undated **Management Agreement** between Australian Bight Abalone Management Pty Limited (Manager), the Responsible Entity and the Grower received by the Tax Office on 30 March 2005;
- Draft undated **Compliance Plan** received by the Tax Office on 15 February 2005; and
- Independent Biologists Report dated 14 December 2004 and received by the Tax Office on 15 February 2005.

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

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

16. In accordance with the above documents, a Grower who participates in the arrangement must be a wholesale client or have accepted an offer that is a small scale offering. **This Ruling does not apply unless:**

- the Grower is a wholesale client as defined in section 761G of the *Corporations Act 2001*; or
- not being a retail client, the Grower has accepted a 'personal offer' of a small scale offering for the purpose of the *Corporations Act 2001*.

17. Each of these categories is explained in paragraphs 86 to 92 in the Explanation area of this Product Ruling.

18. 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

19. The salient features of the Australian Bight Abalone Project are as follows:

Location	Waldegrave Island, near Elliston on the Eyre Peninsula, South Australia.
Type of business each participant is carrying on	Commercial Aquaculture of Greenlip Abalone.
Maximum number of Interests offered	120
Minimum Subscription	15 Interests
Size of a minimum allocation	One Interest (which is the equivalent of 60 Abalone Baskets).
The term of the Project	7 years from the date of commencement.
Initial cost per Interest	\$53,195
Ongoing costs	RE Fee Cage Rental Fee Annual Management Fee Harvest Fee Seeding & Settling Fee Sales Incentive Fee

20. A Grower will acquire 60 Abalone Baskets and 10,000 Abalone Spat per each Interest they are allocated in the Project. Each in-sea cage will hold 300 Abalone Baskets. The Project will not proceed until the minimum subscription level of 15 Interests is achieved. Once the minimum subscription is achieved further Interests will only be allocated in multiples of 5 Interests to ensure there will be 300 Abalone Baskets per in-sea cage. No applications for Interests in the Project will be accepted after 15 June 2005.

21. A Grower will be involved in the Project for a term of 7 years which allows for two growth cycles of 3 years each plus a 12 month sales period.

Project Entities

22. Australian Bight Abalone Limited is the Responsible Entity for the Project and holder of Australian Financial Securities Licence Number 282113. The Responsible Entity is the holding company of both the Marine Lease Owner and the Manager and will enter into the Aquaculture & Cage Rental Agreement and the Management Agreement on behalf of each Grower.

23. Australian Bight Infrastructure Pty Ltd (Marine Lease Owner) is the holder of a Marine Lease and attached aquaculture licence issued by the department of Primary Industries and Resources of South Australia. The aquaculture licence enables the aquaculture licence holder to carry out aquaculture activities on the leased site. The Marine Lease Owner is the owner of in-sea cages. Under the Aquaculture & Cage Rental Agreement each Grower will be granted aquaculture rights which include the right to use the in-sea cages.

24. Australian Bight Abalone Management Pty Ltd will be the Manager for the Project and will provide aquaculture services for each Grower under the terms of the Management Agreement. A Grower will purchase the Abalone Baskets and Abalone Spat from the Manager.

Aquaculture Licence

25. In South Australia under the *Aquaculture Act 2001*, a person must not carry on aquaculture except as authorised by an aquaculture licence. The department of Primary Industries and Resources South Australia (PIRSA) has advised the Tax Office that Growers participating in the Australian Bight Abalone Project are not required to hold an aquaculture licence under the terms of the *Aquaculture Act 2001*.

Application for Interests

26. To participate in the Project an applicant needs to complete and sign the Application Form attached to the Information Memorandum. A signed Application Form gives the Responsible Entity a Limited Power of Attorney to execute the Aquaculture & Cage Rental Agreement and Management Agreement on behalf of a Grower.

27. The Application Form, along with the Application Fee of \$53,195 per Interest applied for, needs to be received by the Responsible Entity. The Responsible Entity will not execute the Aquaculture & Cage Rental Agreement or the Management Agreement until the Application Fee has been cleared. The latest date this can occur is 15 June 2005 (clauses 3.6 and 3.7 of the Constitution).

28. Applications will not be accepted before the minimum subscription level of 15 Interests has been achieved or where there are insufficient Abalone Baskets, Abalone Spat and/or in-sea cages available. Applications will not be accepted after 15 June 2005.

29. Each in-sea cage and Abalone Basket used in the Project will be numbered. The in-sea cages will have a four digit number identifying the lease site and the in-sea cage number. Each Abalone Basket will have a seven digit number identifying the lease site, in-sea cage and basket number. The Responsible Entity will record each Grower's Abalone Basket numbers in the Growers register as per clause 17.1 of the Constitution.

30. All Growers who acquire an Interest in the Project will pool their Abalone Produce (Pooled Growers) unless they make an election in writing on application that they wish to personally harvest, market and sell their Abalone Produce. This Product Ruling has no application to Growers who elect to harvest, market and sell their Abalone Produce.

Constitution

31. Under clause 1.1 the Responsible Entity is appointed to act as agent, attorney and/or trustee in relation to the Project. The Responsible Entity will establish a bank account into which Application Fees and harvest proceeds from the sale of Abalone will be deposited (clauses 2.5 and 8.1).

32. All amounts payable by a Grower under the Aquaculture & Cage Rental Agreement, the Management Agreement and the Constitution must be paid to the Responsible Entity (clause 6.1). The Responsible Entity will make payments of amounts owing by a Grower under the Aquaculture & Cage Rental Agreement and Management Agreement and the Constitution from the bank account prior to distribution of harvest proceeds to a Grower (clause 8.2). Harvest proceeds are to be paid to a Grower no later than 30 days from the receipt of funds from the sale of a Grower's Abalone (clause 8.2.1).

33. Under clause 23.1 the Responsible Entity is entitled to a fee of \$120 per Interest per annum plus CPI from 30 June 2005 (RE Fee) for services provided under the Constitution. The RE Fee from the date of acceptance to 30 June 2005 is \$120 per Interest and is incorporated into the Application Fee (refer to the table at paragraph 46). The RE Fee for later years is only payable after invoicing. Invoicing will occur in the year ending 30 June 2009 for the income years ending 30 June 2006, 2007 and 2008, and in the year ending 30 June 2012 for the income years ending 30 June 2009, 2010, 2011 and 2012.

Aquaculture & Cage Rental Agreement

34. Under clause 1 of this agreement the Marine Lease Owner grants a Grower the following aquaculture rights:

- (a) the right to enter the Marine Lease area subject to the terms of the Management Agreement;
- (b) the right to settle, maintain and harvest Abalone in the Marine Lease area subject to the terms of the Management Agreement;
- (c) the right to use such works and facilities provided to the Grower by the Marine Lease Owner as may be necessary or convenient to enable the Grower to settle, maintain and harvest Abalone in the Marine Lease area;
- (d) the right of use of the in-sea cage(s); and
- (e) the ownership of the Abalone Baskets.

35. In consideration for granting the above aquaculture rights the Marine Lease Owner will be entitled to a fee of \$1. This fee is included in the Application Fee (Initial Management Fee) paid to the Responsible Entity (clauses 3.1 and 3.1.1). The Marine Lease Owner will also be entitled to a Cage Rental Fee which will be calculated at \$500 per Interest per annum plus CPI from 30 June 2005. The Cage Rental Fee from the date of acceptance to 30 June 2005 is \$125 per Interest. A Cage Rental Fee of \$125 is incorporated into the Application Fee (refer to the table at paragraph 46). The Cage Rental Fee for later years is only payable after invoicing. Invoicing will occur in the year ending 30 June 2009 for the income years ending 30 June 2006, 2007 and 2008, and in the year ending 30 June 2012 for the income years ending 30 June 2009, 2010, 2011 and 2012.

36. Under clause 4 a Grower owns all of the Abalone in their Abalone Baskets and is entitled to all harvest proceeds from the sale of Abalone from their Abalone Baskets. Upon termination of this agreement or the Management Agreement the ownership of the Abalone Baskets will revert to the Marine Lease Owner on payment of \$1 per Abalone Basket (clause 8.1 and 8.1.1).

37. The Grower must promptly repair any damage caused directly by the Grower, or any of its employees, agents or contractors, to any infrastructure owned by the Marine Lease Owner (clause 6.4). Following the final harvest the Grower must rehabilitate the Marine Lease site (clause 9.1 and 9.2). The cost of rehabilitation is included in the final Harvest Fee.

38. The Grower is entitled to re-establish Abalone in the Grower's Abalone Baskets following a harvest, other than the final harvest (clause 9.4). Under the arrangement it is proposed to have a harvest in year 4 (year ending 30 June 2009) of the Project and a final harvest in year 7 (year ending 30 June 2012) of the Project.

39. The agreement can be terminated where either party breaches any of its obligations under the agreement unless the breach has, in certain circumstances, been rectified. Either party may terminate the agreement if the other party undergoes a specified insolvency event. The Marine Lease Owner may terminate the agreement if the Manager terminates the Management Agreement (clause 10).

Management Agreement

40. Under clause 1.1 a Grower engages the Manager as an independent contractor to perform the aquaculture services. The aquaculture services to be provided by the Manager and the Annual Management Fees payable to the Manager are detailed in Schedules 3 and 4 of the agreement (refer paragraphs 46 to 57).

41. A Grower acknowledges that the Manager has the exclusive right to carry out all of the aquaculture rights set out in the Aquaculture & Cage Rental Agreement on the Grower's behalf (clause 2.4). A Grower has the right to give general direction to the Manager including dates of harvest of the Grower's Abalone Produce and the right to receive quarterly progress reports from the Manager (clauses 2.10 and 2.11).

42. A Grower is entitled to all proceeds from the sale of produce net of all costs owing by the Grower under the Management Agreement, the Aquaculture & Cage Rental Agreement and the Constitution (clause 6.12).

43. A Pooled Grower's entitlement to Abalone Produce from the Project as a whole will be calculated by reference to the weight of the Abalone harvested by the Grower compared with the overall weight of the Abalone harvested from all Pooled Growers in the Project (clause 6.7.3). A Pooled Grower's share of Project costs will be calculated pro rata by reference to the number of the Pooled Grower's Abalone Baskets compared with the overall number of Pooled Growers' Abalone Baskets for the Project (clause 6.12).

44. Under clause 1.3 a Grower is able to remove the Manager. To do so they need to provide the Marine Lease Owner with evidence of a valid contractual relationship for the provision of aquaculture services to the Grower by a party suitably licensed by PIRSA. The Grower may appoint a new manager in accordance with clause 1.4.

45. The agreement ends after the final harvest, marketing and sale of all Abalone Produce together with the completion of the rehabilitation work. The agreement must end within 10 years after its commencement (clause 3.1). The agreement can be terminated where either party breaches any of its obligations under the agreement unless the breach has, in certain circumstances, been rectified. Either party may terminate the agreement if the other party undergoes a specified insolvency event. The Manager or Responsible Entity may terminate the agreement if the scheme or the Aquaculture & Cage Rental Agreement is terminated by the Marine Lease Owner or Responsible Entity. The Manager may terminate the agreement where all, or substantially all, of the Abalone in the Abalone Baskets is destroyed (clause 12).

Initial Establishment Services and Initial Management Fee

46. The Initial Establishment Services are to be completed on or before 30 June 2005. The Initial Management Fee for the provision of the Initial Establishment Services is \$53,195 per Interest. This amount is the Application Fee which is payable on application for each Interest in the Project. A breakdown of the costs attributed to the Application Fee is detailed in the table below.

Application Fee	Amount
Provision of 10,000 Abalone Spat settled on hatchery tray	\$1,128
Biologist controlled grading and removal of runts	\$4,785
Biologist controlled transportation of Spat and tray to jetty site and vessel	\$600
Provision of 60 Abalone Baskets per Interest (post algae growth state)	\$43,890
Attachment of tray to Abalone Basket	\$800
Transport of tray to in-sea cage site	\$500
Insertion/attachment of Abalone Basket to in-sea cage	\$1,146
Re-insertion/re-attachment of Abalone Baskets as required	\$100
Payment of \$1.00 to the Marine Lease Owner for the granting of rights under the Growers Aquaculture & Cage Rental Agreement	\$1
RE Fee from acceptance to 30 June 2005	\$120
Cage Rental Fee from acceptance to 30 June 2005	\$125
Application Fee (Initial Management Fee)	\$53,195

Annual Aquaculture Services and Annual Management Fee

47. The Annual Aquaculture Services are the following services to be performed annually or monthly:

- Managing and maintaining the Abalone Baskets (monthly);
- Testing for disease (monthly) or as necessary;
- Quality control (monthly);
- Internal audit of operations (annual);
- Corporate services comprising: research, administration, investment relations, and projections (constant);
- Inventory assessment (annual); and
- Maintenance of related infrastructure (as necessary).

48. The Annual Management Fee for the Annual Aquaculture Services is \$1,875 per Interest. This amount is to be indexed by the CPI from 30 June 2005. The Annual Management Fee is payable from harvest proceeds and only after invoicing (deferred management fee). Invoicing will occur in the year ending 30 June 2009 for the income years ending 30 June 2006, 2007 and 2008, and in the year ending 30 June 2012 for the income years ending 30 June 2009, 2010, 2011 and 2012.

49. In the case there is no harvest or harvest proceeds do not meet the deferred management fee plus the Harvest Fee, the Grower shall be liable for the higher of the harvest proceeds or a maximum contribution of \$2,500 in satisfaction for the full amount of deferred management fees and Harvest Fee (Schedule 4 clause 5.4 of the Management Agreement). However where a Grower receives a payment in relation to an insurance policy covering the Abalone Produce for any amount, the Grower will be liable to pay all deferred management fees and Harvest Fees and clause 5.4 will not apply to that Grower (Schedule 4 clause 5.6 of the Management Agreement).

Harvest Aquaculture Services and Harvest Fee

50. The Harvest Aquaculture Services occur twice in the life of the Project (year 4 and year 7) and are to be performed on harvest of the Abalone Produce as follows:

- In respect of Pooled Growers, arrange for the harvesting of Abalone Produce at first harvest, and final harvest. Harvesting preparation, supervision and all ancillary activities necessary for harvest will be performed to ensure that these operations extract Abalone and Abalone Produce with minimal damage to the Growers Abalone Baskets;

- Assistance to a Pooled Grower to secure markets for Abalone and Abalone Produce. There is no obligation on the Manager to purchase or guarantee the purchase or sale of the Abalone or Abalone Produce; and
- Rehabilitation of the Marine Lease after final harvest, comprising such that the sea bed is in a clean and tidy condition as required under the Marine Lease conditions imposed by terms of the Marine Lease.

51. The Harvest Fee for the provision of the Harvest Aquaculture Services is \$5,965 per Interest, indexed by CPI from 30 June 2005. The Harvest Fee is payable only after harvest from the harvest proceeds. The Harvest Fee is payable twice in the life of the Project (year ending 30 June 2009 and year ending 30 June 2012).

52. In the case there is no harvest or harvest proceeds do not meet the deferred management fees plus the Harvest Fee, the Grower shall be liable in total for a contribution of \$2,500 in satisfaction for the full amount of deferred management fees and Harvest Fee (Schedule 4 clause 6.3 of the Management Agreement). However where a Grower receives a payment in relation to an insurance policy covering the Abalone Produce for any amount, the Grower will be liable to pay all deferred management fees and Harvest Fees and clause 6.3 will not apply to that Grower (Schedule 4 clause 6.4 of the Management Agreement).

Re-Seeding Aquaculture Services and Seeding & Settling Fee

53. Re-Seeding Aquaculture Services occur once in the life of the Project immediately following the first harvest of Abalone Produce and include the following:

- Provision of 10,000 Abalone Spat settled on hatchery tray;
- Biologist controlled grading and removal of runts;
- Biologist controlled transportation of Spat and tray to jetty site and vessel;
- Cleaning and re-preparation of 60 Abalone Baskets per Interest (post algae growth state);
- Attachment of tray to Abalone Basket;
- Transport of tray to in-sea cage site;
- Insertion/attachment of Abalone Basket to in-sea cage; and
- Re-insertion/re-attachment of Abalone Baskets as required.

54. The Seeding & Settling Fee for the provision of the Re-Seeding Aquaculture Services is \$9,305 per Interest and is payable from harvest proceeds after the Re-Seeding Aquaculture Services have been provided by the Manager. This fee is not CPI indexed. Where harvest proceeds are insufficient to cover the deferred management fees and Harvest Fee the Grower will remain liable for payment of the Seeding & Settling Fee.

Sales Incentive Fee and other costs

55. A Sales Incentive Fee is payable when the Growers average sale price per kilogram for each harvest exceeds \$43.00. The Sales Incentive Fee equates to 50% of the sale price per kilogram received in excess of \$43.00 per kilogram in each harvest.

56. The Manager may charge a fee where it is required to do any work of an emergency or other necessary nature not otherwise covered by the Management Agreement (clause 4.5). The Manager and Growers may agree from time to time for the Manager to provide services in addition to the aquaculture services listed above (clause 4.8). For Pooled Growers the fees for emergency and additional services will be calculated by reference to the number of Abalone Baskets owned by a Pooled Grower compared with the overall number of Abalone Baskets of all Pooled Growers.

57. The Manager and the Responsible Entity have a lien on the Abalone Produce and harvest proceeds in respect of all amounts payable to the Manager or Responsible Entity by a Grower which are due and unpaid. The Manager or the Responsible Entity may sell any property on which they have a lien (clauses 8.8 to 8.12).

Finance

58. Growers can fund their investment in the Project themselves or borrow from an independent lender.

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

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL or the funding arrangements transform the Project into a 'scheme' to which Part IVA may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;

- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project are involved or become involved in the provision of finance to Growers for the Project.

Ruling

Application of this Ruling

60. This Ruling only applies to Growers who:

- are accepted to participate in the Project and their Application Fee of \$53,195 per Interest applied for has been received on or before 15 June 2005;
- have executed an Aquaculture & Cage Rental Agreement and a Management Agreement by 15 June 2005;
- do not elect to harvest, market and sell their own Abalone Produce; and
- are either a wholesale client (section 761G of the *Corporations Act 2001*) or have accepted a 'personal offer' of a small scale offering (section 1012E of the *Corporations Act 2001*).

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

Minimum Subscription

61. 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. Under the terms of the Constitution a Grower's application will not be accepted and the Project will not proceed unless the minimum subscription of 15 interests is reached on or before 15 June 2005.

The Simplified Tax System ('STS') – Division 328

62. To be an 'STS taxpayer' a Grower must be eligible to be an 'STS taxpayer' and must have elected to be an 'STS taxpayer'. 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 under the STS where the Grower uses the cash accounting method.

Qualification

63. 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 – sections 6-5 and 328-105

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

65. A Grower will recognise ordinary income from carrying on the business of aquaculture at the time that income is derived when they are:

- not an 'STS taxpayer', or
- an 'STS taxpayer' using the accruals accounting method for the 2005-06 and later income years.

66. A Grower who is an 'STS taxpayer' using the cash accounting method will recognise ordinary income from carrying on their business of aquaculture in the income year in which that income is received.

Trading Stock**Sections 70-35 and 70-45**

67. During the term of the Project, a Grower will hold Abalone that will constitute trading stock on hand. The Initial management fee and the Seeding and Settling Fee include an amount of \$1,128 per Interest for the provision of 10,000 Abalone Spat. Section 70-35 requires the Grower to include the value of the trading stock in working out assessable income and deductions.

68. 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.

69. 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.

70. Under section 70-45, the Grower can elect to value trading stock on hand at the end of the income year at cost, market selling value or replacement value. Where the Grower elects to value the trading stock at the end of the income year at cost, 'cost' would include only those expenses incurred until the Abalone became trading stock of the Grower.

71. During the term of the Project, the Manager will provide sufficient information to enable the Grower to determine the value of the trading stock on hand at the end of the relevant income year.

Section 328-285

72. Section 70-35 requires the Grower to include the value of the trading stock in working out assessable income and deductions, unless the Grower who is an 'STS taxpayer' is able to choose not to apply this section as the conditions in subsection 328-285(1) are met.

73. Subsection 328-285(1) provides if the difference between the value of all the Grower's trading stock at the start of an income year and a reasonable estimate of the trading stock at the end of the income year is less than \$5,000, an 'STS taxpayer' does not have to account for that difference under the ordinary trading stock rules in sections 70-35 and 70-45. The value of all the trading stock on hand at the end of the year will instead be considered equal to the trading stock on hand at the start of the year.

Deductions for Initial Management Fee, RE Fee, Cage Rental Fee, Annual Management Fee, Harvest Fee and Seeding & Settling Fee – sections 8-1 and 328-105

74. A Grower may claim tax deductions for the following expenses per Interest in the Project:

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Fee Type	ITAA 1997 Section	Year ended 30 June 2005	Year ended 30 June 2006	Year ended 30 June 2007
Initial Management Fee (excluding Abalone Spat & Abalone Baskets)	8-1 & 328-105	\$7,932 See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)
Provision of 10,000 Abalone Spat	8-1, 70-15, 70-35 & 328-285	Amount must be calculated – See Notes (i) & (iv)	Nil See Notes (i) & (iv)	Nil See Notes (i) & (iv))
RE Fee	8-1 & 328-105	\$120 See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)
Cage Rental Fee	8-1 & 328-105	\$125 See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)
Annual Management Fee	8-1 & 328-105	Nil See Notes (i), (ii) & (iii)	Nil See Notes (i), (ii) & (iii)	Nil See Notes (i), (ii) & (iii)
Harvest Fee	8-1 & 328-105	Nil See Notes (i), (ii) & (iii)	Nil See Notes (i), (ii) & (iii)	Nil See Notes (i), (ii) & (iii)
Seeding and Settling Fee	8-1 & 328-105	Nil See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)	Nil See Notes (i), (ii), (iii) & (iv)
Abalone Baskets	Div 40 & Subdiv 328-D	See paragraphs 75 to 82	See paragraphs 75 to 82	See paragraphs 75 to 82

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 (for example, input tax credits): Division 27. See Example at paragraph 128.
- (ii) The Initial Management Fee (excluding the Abalone Spat & Abalone Baskets), RE Fee, Cage Rental Fee, Annual Management Fee, Harvest Fee and the Seeding and Settling Fee (excluding the Abalone Spat) shown in the Constitution, Aquaculture & Cage Rental Agreement and the Management Agreement are deductible under section 8-1, to the extent they are not capital in nature, in the year that they are incurred, (where the Grower is not an 'STS taxpayer') or in the

year in which they are paid (where the Grower is an 'STS taxpayer'). If an amount shown is not fully paid in the year in which it is incurred by a Grower who is an 'STS taxpayer' then the amount is only deductible to the extent to which it has been paid, or has been paid for the Grower. The RE Fee and Cage Rental Fee from 1 July 2005 and the Annual Management Fee, although calculated annually, are not incurred until they are invoiced following the sale of the Abalone by the Manager. The actual amount incurred and payable in respect to the Annual Management Fee and Harvest Fee will depend on the amount of harvest proceeds.

- (iii) This Ruling does not apply to Growers who choose to prepay the Initial Management fee, RE Fee, Cage Rental Fee, Annual Management fee, Harvest Fee or Seeding & Settling Fee. 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 section 82KZME and section 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.
- (iv) The 10,000 Abalone Spat acquired per Interest is the cost of acquiring juvenile Abalone which is the trading stock of the Grower. The timing of the deduction for the outgoing is the year the Abalone becomes part of the Grower's trading stock (section 70-15). Section 70-35 adjusts the amount of the deduction by comparison of the value of the trading stock at the start of the income year with the value of the trading stock on hand at the end of the income year. A Grower who is an 'STS taxpayer' can choose not to account for differences in trading stock under section 70-35, if the conditions in subsection 328-285(1) are met (see paragraph 67 to 73).

Deductions for Capital Expenditure (Non-STs taxpayers) – Division 40

75. A Grower who is not an 'STS taxpayer' will also be entitled to tax deductions relating to Abalone Baskets, determined under Division 40.

76. The Initial Management Fee of \$53,195 per Interest includes \$43,890 for the purchase of 60 Abalone Baskets. Each Abalone Basket is a 'depreciating asset'. The 'cost' of the asset is the amount paid by each Grower, which is \$731.50 per Abalone Basket. The decline in value of the asset is calculated using the formula in either subsection 40-70(1) ('diminishing value method'), subsection 40-75(1) ('prime cost method') or section 40-440 ('low value pool'). If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (for example, input tax credits): Division 27. See Example at paragraph 128.

77. Both the diminishing value method and prime cost method formulas rely on the 'effective life' of the Abalone Basket. As there has been no determination of the 'effective life' of an Abalone Basket by the Commissioner, Growers must self-assess an 'effective life' (section 40-105). The Abalone Baskets will be placed in an in-sea cage and first used during the year ended 30 June 2005. The Manager will advise Growers when that occurs to enable Growers to calculate the deduction for the decline in value.

78. Each Grower holds an interest in each of their Abalone Baskets which are a 'low-cost asset' and can be allocated to a 'low-value pool'. Once any 'low-cost asset' of a Grower is allocated to a 'low-value pool', all other 'low-cost assets' the Grower starts to 'hold' in that year or a later year must be allocated to that pool. If the Grower has already allocated an asset to a 'low-value pool', the Abalone Basket assets must also be allocated to that pool. Otherwise, the Grower must decide whether to create a 'low-value pool'. If the assets are allocated to a 'low-value pool', the capital expenditure on the Abalone Baskets will be deducted under the diminishing value methodology of the pool based on a rate of 18.75% in the year the Abalone Baskets are first used and a rate of 37.5% in subsequent years (section 40-440).

Deductions for Capital Expenditure (STS taxpayers) – Subdivision 328-D

79. A Grower who is an 'STS taxpayer' will also be entitled to tax deductions relating to Abalone Baskets. Deductions relating to the 'cost' of Abalone Baskets must be determined under Division 328.

80. Under Division 328, if the 'cost' of a 'depreciating asset' at the end of the income year is less than \$1,000 (a 'low-cost asset'), it can be claimed as an immediate deduction when first used or 'installed ready for use'. This is so provided the Grower is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income.

81. An Abalone basket is a 'depreciating asset'. Each Grower holds an interest in each of their Abalone Baskets which are a 'low-cost asset' as defined in subsection 40-525(2). It cannot be allocated to a 'general STS pool' (section 328-180). A deduction equal to the amount of the Grower's expenditure for the Abalone Baskets is available in the income year in which they are used or 'installed ready for use'. The Abalone Baskets will be placed in an in-sea cage and first used during the year ended 30 June 2005.

82. If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (for example, input tax credits): Division 27. See Example at paragraph 128.

Interest

83. The deductibility or otherwise of interest incurred by Growers who finance their participation in the Project through a loan facility with a bank or other financier is outside the scope of this Ruling. However, all Growers who borrow funds in order to participate in the Project should read the discussion of the prepayment rules in paragraphs 110 to 114 as those rules may be applicable if interest is prepaid.

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

Section 35-55 – Commissioner's discretion

84. A Grower who is an individual accepted into the Project by 15 June 2005 may have losses arising from their participation in the Project that would be deferred to a later income year under section 35-10. Subject to the Project being carried out in the manner described above, the Commissioner will exercise the discretion in paragraph 35-55(1)(b) for these Growers for the income years ending **30 June 2005 to 30 June 2008, 30 June 2010 and 30 June 2011**. This conditional exercise of the discretion will allow those losses to be offset against the Grower's other assessable income in the income year in which the losses arise.

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

85. For a Grower who participates in the Project and incurs expenditure as required by the Constitution, Aquaculture & Cage Rental Agreement and Management 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 and 82KZMF (but see paragraphs 110 to 114);

- 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

Corporations Act 2001

86. For this Ruling to apply, an offer for an interest in the project must:

- have been made to, and accepted by a Grower, who qualifies as a wholesale client as defined in section 761G of the *Corporations Act 2001*; or
- be an offer which qualifies as a small scale offering as defined in section 1012E of the *Corporations Act 2001*.

Small scale offers and offers to wholesale clients do not require a prospectus or product disclosure statement.

87. A Grower in the Project may be a person who is a wholesale client within the definition in section 761G. A person will be a wholesale client where the persons satisfies one of the following tests:

- the 'product value test' (paragraph 761G(7)(a));
- the 'individual wealth test' (paragraph 761G(7)(c)); or
- the 'professional investor test' (paragraph 761G(7)(d)).

88. A participant in a managed investment scheme, referred to below as 'the person' or 'the person to whom the offer is made', will satisfy the 'product value test' where:

- the minimum amount payable for the interests in the project on acceptance of the offer by the person to whom the offer is made is at least \$500,000; or
- the amount payable for the interests in the project on acceptance by the person to whom the offer is made and the amounts previously paid by the person for interests in the project of the same class that are held by the person add up to at least \$500,000.

89. A participant in a managed investment scheme, referred to below as 'the person' or 'the person to whom the offer is made', will satisfy the 'individual wealth test' where, it appears from a certificate given by a qualified accountant no more than 6 months before the offer is made, that the person to whom the offer is made:

- has net assets of at least \$2.5 million; or
- has a gross income for each of the last 2 financial years of at least \$250,000 a year.

90. A participant in a managed investment scheme, referred to below as 'the person' or 'the person to whom the offer is made', will satisfy the 'professional investor test' where:

- the person is a financial services licensee; or
- the person controls at least \$10 million for the purposes of investment in securities.

91. Alternatively, under section 1012E, a Grower may participate in the project by accepting a 'personal offer' for an interest in the project. Offers made under section 1012E cannot be accepted by more than 20 investors in any 12 month period and these investors, in aggregate, must not invest more than \$2 million dollars (subsection 1012E(2)).

92. An offer will be a 'personal offer' where it can only be accepted by the person to whom it is made, and it is made to a person who is likely to be interested in the offer because of previous contact, or professional or other connection with the person making the offer, or because they have indicated that they are interested in offers of that kind (subsection 1012E(5)).

Is the Grower carrying on a business?

93. For the amounts set out in the Ruling section above to constitute allowable deductions, the Grower's aquaculture activities, as a participant in the Australian Bight Abalone Project, must amount to the carrying on of a business of primary production.

94. Where there is a business, or a future business, the gross proceeds from the sale of the Abalone 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.

95. For schemes such as the Australian Bight Abalone 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 *Commissioner of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

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

- the Grower purchases identifiable Abalone Baskets in which Abalone owned by the Grower will be cultivated and grown;
- the Grower has the right to harvest and sell the Abalone from those Abalone Baskets;

- the aquaculture activities are carried out on the Grower's behalf;
- the aquaculture activities of the Grower are typical of those associated with an aquaculture business; and
- the weight and influence of general indicators point to the carrying on of a business.

97. In this Project, each Grower enters into an Aquaculture & Cage Rental Agreement and a Management Agreement. Under the Management Agreement each individual Grower will have ownership over a specific and identifiable number of Abalone Baskets. The Management Agreement provides the Grower with an ongoing interest in the specific Abalone in the Abalone Baskets for the term of the Project. Under the Management Agreement the Grower must use the aquaculture lease and in-sea cage(s) in question for the purpose of carrying out aquaculture activities, and for no other purpose. The Management Agreement allows the Manager to utilise the Abalone Baskets to carry out its obligations under the Management Agreement.

98. Under the Management Agreement the Manager is engaged by the Grower to establish and maintain an Abalone farm in the Grower's identifiable area using the Growers Abalone Baskets during the term of the Project. The Manager has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the Abalone farm on the Grower's behalf.

99. The Manager is also engaged to harvest, market and sell, on the Grower's behalf, the Abalone grown on the Grower's Abalone farm.

100. 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.

101. 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 Abalone that will return a before-tax profit, that is a profit in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

102. A Pooled Grower's entitlement to Abalone Produce from the Project as a whole will be calculated by reference to the weight of the Abalone harvested by the Pooled Grower compared with the overall weight of the Abalone harvested from all Pooled Growers in the Project. A Pooled Grower's share of Project costs will be calculated pro rata by reference to the number of the Pooled Grower's Abalone Baskets compared with the overall number of Pooled Growers' Abalone Baskets for the Project. This pooling is consistent with general aquaculture practices.

103. The Manager's services are also consistent with general aquaculture practices. They are of the type ordinarily found in aquaculture ventures that would commonly be said to be businesses. While the size of the Grower's Abalone farm is relatively small, it is of a size and scale to allow it to be commercially viable.

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

105. The aquaculture 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 Grower's aquaculture activities in the Australian Bight Abalone Project will constitute the carrying on of a business.

The Simplified Tax System – Division 328

106. 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.

107. 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'.

Deductions for Initial Management Fee, RE Fee, Cage Rental Fee, Annual Management Fee, Harvest Fee and Seeding & Settling Fee – section 8-1

108. Consideration of whether the fees payable under the Constitution, Aquaculture & Cage Rental Agreement and Management Agreement 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.

109. The Initial Management Fee, RE Fee, Cage Rental Fee, Annual Management Fee, Harvest Fee and Seeding & Settling Fee associated with the aquaculture activities will relate to the gaining of income from the Grower's business of aquaculture (see above), and hence have a sufficient connection to the operations by which income (from the harvesting and sale of Abalone) is to be gained from this business. They will thus be deductible under the first limb of section 8-1 (excluding that part of the Initial Management Fee and Seeding and Settling Fee which relates to the acquisition of Abalone Baskets and Abalone Spat) to the extent they are not capital in nature. Further, no 'non-income producing' purpose in incurring the fees is identifiable from the arrangement. The fees appear to be reasonable. There is however a capital component in the Initial Management Fee as the cost of acquiring the Abalone Baskets are costs of a capital nature that are not deductible under section 8-1.

Prepayment provisions

Sections 82KZL to 82KZMF

110. 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 (for example the performance of management services) 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.

111. For this Project, only section 82KZL (an interpretative provision) and sections 82KZME and 82KZMF are relevant. Where the requirements of sections 82KZME and 82KZMF are met, taxpayers determine deductions for prepaid expenditure under section 82KZMF using the formula in subsection 82KZMF(1). These provisions also apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes 'STS taxpayers' from the operation of section 82KZMF.

Application of prepayment provisions to this Project

112. Under the Arrangement to which this Product Ruling applies the fees payable under the Constitution, Aquaculture & Cage Rental Agreement and Management Agreement are incurred on acceptance into the Project and following the sale of the Abalone Produce. 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 an immediate 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 an immediate deduction for each of the relevant amounts in the income year in which the fee is incurred.

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

114. As noted in the Ruling section above, Growers who prepay the 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.

Expenditure of a capital nature – Division 40 and Division 328

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

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

117. The tax treatment of capital expenditure has been dealt with in a representative way in paragraphs 75 to 82.

Treatment of trading stock***Section 70-35***

118. A Grower who is not an 'STS taxpayer' may, in some years, hold Abalone 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.

119. 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.

Section 328-285

120. A Grower who is an 'STS taxpayer' may, in some years, hold Abalone 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) of the ITAA 1997).

121. 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) of the ITAA 1997).

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

122. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income years **30 June 2005 to 30 June 2008, 30 June 2010 and 30 June 2011** the Commissioner has applied the principles set out in Taxation Ruling TR 2001/14 Income tax: Division 35 – non-commercial business losses. Accordingly, based on the evidence supplied, the Commissioner has determined that for those income years ended 30 June 2005 to 30 June 2008, 30 June 2010 and 30 June 2011:

- it is because of its nature the business activity of a Grower will not satisfy one of the four tests in Division 35;
- there is an objective expectation that within a period that is commercially viable for the aquaculture industry, a Grower's business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit; and
- a Grower who would otherwise be required to defer a loss arising from their participation in the Project under subsection 35-10(2) until a later income year is able to offset that loss against their other assessable income.

123. The exercise of the Commissioner's discretion under paragraph 35-55(1)(b) is conditional on the Project being carried on in the manner described in this Ruling during the income years specified. If the Project is carried out in a materially different way to that described in the Ruling a Grower will need to apply for a private ruling on the application of section 35-55 to those changed circumstances.

Section 82KL – recouped expenditure

124. The operation of section 82KL depends, among other things, on the identification of a certain quantum of ‘additional benefits(s)’. Insufficient ‘additional benefits’ will be provided to trigger the application of section 82KL. It will not apply to deny the deduction otherwise allowable under section 8-1.

Part IVA – general tax avoidance provisions

125. 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).

126. The Australian Bight Abalone 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 paragraph 74 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.

127. 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 Abalone. 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**

128. 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	\$2,200*
Total due and payable by 1 January 2004 (includes GST of \$600)	\$6,600

*Taxable supply

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

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

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 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

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Previous draft:

Not previously issued as a draft

- tax shelters project
- taxation administration
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Related Rulings/Determinations:

PR 1999/95; TD 93/34; TR 92/1;
TR 92/20; TR 97/11; TR 97/16;
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*Legislative references:**Subject references:*

- carrying on a business
- commencement of business
- fee expenses
- interest expenses
- management fees
- non-commercial losses
- producing assessable income
- product rulings
- public rulings
- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters

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