



# ***PR 2006/119 - Income tax: Olive Growers Australia Project 2005/2006 - Applicant Group 2***

 This cover sheet is provided for information only. It does not form part of *PR 2006/119 - Income tax: Olive Growers Australia Project 2005/2006 - Applicant Group 2*

 This document has changed over time. This is a consolidated version of the ruling which was published on *19 July 2006*



## Product Ruling

### Income tax: Olive Growers Australia Project 2005/2006 – Applicant Group 2

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**ⓘ This publication provides you with the following level of protection:**

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

## 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 scheme is carried out in accordance with the information we have been given, and have described below in the **Scheme** part of this document.

If the scheme 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 scheme 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 scheme has been implemented as described below and to ensure that the participants in the scheme 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 entity(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 relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates. In this Ruling, this scheme is sometimes referred to as the Olive Growers Australia Project 2005/2006 or simply as 'the Project'.

### Relevant provision(s)

2. The relevant provisions 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;
  - section 108-5 of the ITAA 1997;
  - Division 110 of the ITAA 1997;
  - Division 328 of the ITAA 1997;
  - Division 328 of the *Income Tax (Transitional Provisions) Act 1997*;
  - section 82KL of the *Income Tax Assessment Act 1936* (ITAA 1936);
  - section 82KZME of the ITAA 1936;
  - section 82KZMF of the ITAA 1936; and
  - Part IVA of the ITAA 1936.

All legislative references in this Ruling are to the ITAA 1997 unless otherwise indicated.

### 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 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 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. Entities 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 entities in schemes such as this. In keeping with that intention the Tax Office suggests that promoters and advisers ensure that entities are fully informed of any legislative changes after the Ruling is issued.

**Class of entities**

7. The class of entities to whom this Ruling applies consists of the entities who are more specifically identified in the ruling part of this Product Ruling, refer to paragraphs 73 to 75 of this Ruling, and who enter into the scheme specified below on or after the date this Ruling is made. They will have a purpose of staying in the scheme until it is completed (that is, being a party to the relevant Agreements until their term expires) and deriving assessable income from this involvement. In this Ruling, these entities are referred to as 'Growers'.

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

- intend to terminate their involvement in the scheme prior to its completion or who otherwise do not intend to derive assessable income from it;
- have entered into the scheme specified below before the date of this Ruling or after 30 November 2006; or
- subscribe to **and are allocated only one interest** in the Project.

## Qualifications

9. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 17 to 72 of this Ruling.

10. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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## Date of effect

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12. This Ruling applies prospectively from 19 July 2006, 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. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

13. If this Product Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

14. If this Product Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Product Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

15. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

## **Withdrawal**

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16. This Product Ruling is withdrawn and ceases to have effect after 30 June 2009. The Ruling continues to apply, in respect of the relevant provisions ruled upon, to all entities within the specified class who enter into the scheme specified below. Thus, the Ruling continues to apply to those entities, even following its withdrawal, who entered into the specified scheme prior to withdrawal of the Ruling. This is subject to there being no change in the scheme or in the entities involvement in the scheme.

## **Scheme**

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

- Application for Product Ruling as constituted by documents provided on 14 November 2005, and additional correspondence dated 28 February 2006, 14 March 2006, 28 March 2006, 31 March 2006, 5 April 2006, 26 April 2006 and 27 April 2006;
- Draft Prospectus and Product Disclosure Statement of the Olive Growers Australia Project 2005/2006 received 26 April 2006;
- Draft Supplementary Prospectus and Product Disclosure Statement of the Olive Growers Australia Project 2005/2006 received 26 June 2006;
- Draft **Constitution** of the Olive Growers Australia Project 2005/2006 received 5 April 2006;
- **Draft Licence Agreement No. 1 (Commencement Date to 30 June 2011)** of the Olive Growers Australia Project 2005/2006, between Olive Growers Australia Ltd ('Licensor') and the Grower received 14 November 2005;
- **Draft Licence Agreement No. 2 (1 July 2011 to 30 June 2016)** of the Olive Growers Australia Project 2005/2006, between Olive Growers Australia Ltd and the Grower received 14 November 2005;

- **Draft Licence Agreement No. 3 (1 July 2016 to 30 June 2021)** of the Olive Growers Australia Project 2005/2006, between Olive Growers Australia Ltd and the Grower received 14 November 2005;
- **Draft Licence Agreement No. 4 (1 July 2021 to 30 June 2026)** of the Olive Growers Australia Project 2005/2006, between Olive Growers Australia Ltd and the Grower received 14 November 2005;
- Draft Memorandum Of lease between Carcuma Land Holdings Limited ('Landholder') and Olive Growers Australia Ltd ('Lessee') received 27 April 2006;
- **Draft Management Agreement** of the Olive Growers Australia Project 2005/2006 between Olive growers Australia Ltd ('Responsible Entity') and the Grower received 5 April 2006;
- Compliance Plan for the Olive Growers Australia Project 2005/2006 received 14 November 2005;
- **Terms Payment Agreement** for the Olive Growers Australia Project 2005/2006 received 27 April 2006;
- Viticultural Report for the Olive Growers Australia Project 2005/2006 received 14 November 2005; and
- Draft Olive Orchard Management Agreement of the Olive Growers Australia Project 2005/2006, between the Responsible Entity and Olive Grove Management Pty Ltd ('Vineyard Manager') received 14 March 2006.

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

18. The documents highlighted are those that the Growers enter into. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or an associate of the Grower will be a party to that are part of the scheme to which this Ruling applies.

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

**Overview**

20. The scheme is called 'Olive Growers Australia Project 2005/2006' and is summarised as follows:

Location	Coonalpyn, South East of South Australia
Type of business	Olive Grove
Name of development	Olive Growers Australia Project 2005/2006
Size of each lot	0.05 hectare
Number of lots available	5,694
Minimum subscription	100 lots
The term of the Project	Expires on 30 June 2026
Initial cost per lot	\$2,420 plus a Licence Fee of \$11.45 per month.
Initial costs per hectare	\$48,400
Subscription for one 'B' class share in Landholder	\$1 of the cost of \$1,000 for one share in Carcuma Land Holdings Limited paid on application, the balance of \$999 is payable on 1 July 2011
Ongoing costs	Annual management fees, annual licence fees, olive orchard operating costs, harvesting costs, processing costs and insurance costs

**The Project**

21. The Olive Growers Australia Project 2005/2006 is registered as a Managed Investment Scheme under the *Corporations Act 2001*. The Responsible Entity for the Project is Olive Growers Australia Ltd. Under the combined Prospectus and Product Disclosure Statement ('PDS'), Olive Growers Australia Ltd proposes to offer 5,694 interests called Groves of 0.05 hectares each.

22. The Project Land is situated at Coonalpyn in the south east of South Australia. The Project Land is owned by Carcuma Land Holdings Limited (the 'Landholder') and will be leased by the Responsible Entity.

23. The Landholder may purchase additional land for the Project. The Responsible Entity is able to accept oversubscriptions to the extent of the additional land available. Additional land will only be purchased if it has similar characteristics to the land already acquired for this Project and it is approved by the Horticultural Consultant as being suitable for the establishment of a commercial Olive Grove.

24. The Responsible Entity will plant approximately 21 trees per Grove (420 per hectare). Water for irrigation of the Olive Groves will be supplied from underground aquifers.

25. An interest in the Project is offered under a combined Prospectus and PDS. The minimum subscription for the Project is 100 Olive Groves. Each Applicant may subscribe for a minimum of one Olive Grove and one 'B' class share in the Landholder. It should be noted however that this Ruling only applies to Growers who are allotted more than one Olive Grove.

26. There will be two classes of Growers in the Project, determined by the date of application:

- Applicant Group 1 – Growers who apply on or before 1 June 2006; and
- Applicant Group 2 – Growers who apply on or after the date of this Ruling and on or before 30 November 2006.

This Ruling does not apply to Applicant Group 1 Growers. Product Ruling PR 2006/83 may apply to Applicant Group 1 Growers.

27. Each Grower is required to subscribe for a minimum of one 'B' Class Share in the Landholder, Carcuma Land Holdings Limited, for each interest subscribed to in the Project. The cost of the share is \$1,000, with \$1 payable on application and \$999 payable on 1 July 2011.

28. Upon Application, the Grower will grant a Power of Attorney enabling the Responsible Entity to execute:

- the Licence Agreements between the Responsible Entity and the Grower;
- the Management Agreement between the Responsible Entity and the Grower; and
- the application for shares in the Landholder.

29. Under each Licence Agreement, the Responsible Entity agrees to licence to the Grower an identifiable area of land (a 'Grower's Olive Grove') for the purpose of cultivating olive trees, harvesting olives and producing olive oil until the Project is terminated on 30 June 2026. Each Licence Agreement is for a term of five years.

30. Under the Management Agreement, the Grower appoints the Responsible Entity to establish, maintain and manage the Grower's Olive Grove. The Grower also appoints the Responsible Entity to harvest, process, market and sell the Olive Oil produced.

31. The Responsible Entity will enter into an Olive Orchard Management Agreement with Olive Grove Management Pty Ltd (the 'Olive Orchard Manager') to perform the initial and ongoing services and carryout the harvesting services as required under the Management Agreement.

**Constitution**

32. The Constitution establishes the Project and operates as a deed binding on the Growers and the Responsible Entity. The Constitution sets out the terms and conditions under which Olive Growers Australia Ltd agrees to act as the Responsible Entity and thereby manage the Project. Growers are bound by the Constitution by virtue of their participation in the Project.

33. All Project Property, as defined in clause 1 of the Constitution, will be held by the Responsible Entity acting as Custodian. Project Property includes the Application Fees paid by Growers and Gross Proceeds pending distribution to Growers. The Responsible Entity will deposit all the Application Fees into a trust account (clause 7.11).

34. All Gross Proceeds will be payable to the Responsible Entity. Gross Proceeds includes all interest and accretions received by the Responsible Entity from Authorised Investments and all moneys received from the sale of the Olive Oil (clause 1 of the Constitution). The Responsible Entity must deposit the full amount of Gross Proceeds into a Gross Proceeds Account (clause 13).

35. The balance of Gross Proceeds, after payment to the Responsible Entity of fees, costs and expenses, will be distributed to the Growers within 28 days of receipt of the Gross Proceeds. The amount each Grower receives will be based on the number of Olive Groves licensed to the Grower as a proportion of the total number of Groves licensed under the Project. However, in the event of a partial or total destruction of the trees or olives on the Grower's Olive Grove, the Grower's Proportion will be reduced accordingly (clause 13.3.6).

**Compliance Plan**

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

**Lease**

37. Under a Memorandum of Lease, Carcuma Land Holdings Limited (the 'Lessor') will lease the Project Land to the Responsible Entity. The Lessor agrees the Responsible Entity may licence the land or portions of the land for use in the Project without the consent of the Lessor. Also, the Lessor agrees to provide, at the Lessor's cost, an adequate water supply to enable the Responsible Entity to irrigate the olive groves on the leased land.

## **Licence Agreements**

38. The Responsible Entity, as Licensor, grants a licence to the Grower for a portion of the Project Land, being the Grower's Olive Grove, for the purpose of establishing and maintaining an olive orchard to subsequently harvest olives and sell the Olive Oil. The terms and conditions under which the licence of the Olive Grove is granted to the Grower are contained in the Licence Agreements.

39. Each Grower will enter into four consecutive Licence Agreements with the Licensor, as follows:

- the first Licence Agreement takes effect from the Commencement Date until 30 June 2011;
- the second Licence Agreement will be in effect from 1 July 2011 to 30 June 2016;
- the third Licence Agreement will be in effect from 1 July 2016 to 30 June 2021; and
- the fourth Licence Agreement will be in effect from 1 July 2021 to 30 June 2026.

40. In consideration for the grant of the licence, the Grower agrees to pay a Licence Fee annually. The amount of the Licence Fee is \$11.45 per month or part of a month payable on application for the year ended 30 June 2007. From 1 July 2007, the Licence Fee is \$137.50 per year, payable in advance on 1 July of each Financial Year of the first Licence Agreement.

41. For each Financial Year commencing 1 July 2011, the Licence Fee will be the amount of 4.95% of the Growers Proportion of the Gross Proceeds.

## **Management Agreement**

42. Each Grower enters into a Management Agreement with the Responsible Entity, contracting the Responsible Entity to establish, manage and maintain the Grower's Olive Grove in accordance with good horticultural practices.

43. During the Establishment Period, the Responsible Entity will carry out the following activities to establish the olive orchard on behalf of the Grower:

- preparing that part of the Grower's Olive Grove which can be used to satisfactorily grow olive trees, obtaining healthy olive trees for planting and planting them on the Grower's Olive Grove (in accordance with good horticultural practices);
- spacing, posting and protecting each olive tree on the Grower's Olive Grove in accordance with good horticultural practices so that olives can be harvested commercially; and
- installing the appropriate irrigation equipment.

44. The Establishment Period for Growers in Applicant Group 2 is the period from the Commencement Date to 31 December 2006 (clause 30 Management Agreement).

45. In the ongoing period commencing on 1 January 2007, the Responsible Entity will provide the following ongoing olive orchard maintenance and management services for the term of the Project:

- pruning the olive trees by such methods as the Responsible Entity reasonably determines;
- as permitted by Law, eradicate vermin which have or may cause damage to the Olive Trees or the Grower's Olive Grove and put in place measures to control such vermin;
- operating the irrigation system in order to irrigate the Grower's Olive Grove;
- fertilising the Grower's Olive Grove as required to maintain satisfactory rates of growth and productivity of the Olive Trees;
- destroy any of the Olive Trees, or the Olives, that have contracted an exotic, noxious or incurable disease;
- protecting the Olive Trees from insect infestation and competition from competing growth using good horticultural practices, including but not limited to applying herbicides to the Grower's Olive Trees and spraying under the Olive Trees;
- monitor the condition of and if necessary repair the tree support, tree protection and irrigation equipment on the Grower's Olive Grove;
- regularly inspect the Olive trees;
- replace any of the Olive Trees in need of replacement after the Establishment Period; and
- any other service or thing, which, in the reasonable opinion of the Responsible Entity, is incidental and/or ancillary to the conduct of the Grower's business.

46. The Responsible Entity will send a report to the Grower within 90 days of the end of each financial year containing information on matters considered material to the Grower's Business, including harvest and sales results, the Proceeds of Sale and the condition of the Grower's Olive Grove.

47. In addition, the Responsible Entity must ensure that insurance policies are taken out to cover the destruction or loss of Olive Trees and the Olives and Olive Oil as well as a public liability insurance policy. Each Grower will pay the Grower's Proportion of the Insurance Premiums or the premiums will be reimbursed to the Responsible Entity from the Grower's Proportion of the Gross Proceeds of the Project (clause 11 of the Management Agreement and clauses 9.7 and 13.3 of the Constitution).

### ***Harvesting***

48. Under the Management Agreement, the Responsible Entity must harvest all of the mature Olives grown on the Grower's Olive Grove (clause 5). The Responsible Entity will determine when the harvest will commence by assessing the maturity of the Olives in accordance with good viticultural practices.

49. The Responsible Entity will determine how and where the olives are to be stored and harvesting may be done mechanically or by hand or a combination of both.

50. The costs of providing the harvesting services will be met from the Grower's payment of Harvesting Costs (clauses 9 and 12) which will be deducted from the Grower's Proportion of the Gross Proceeds.

### ***Processing***

51. Under the Management Agreement, the Responsible Entity will crush and process the Olives that have been harvested to extract Olive Oil (clause 5).

52. The Responsible Entity may process the Olives itself or engage a contractor or other person to do so on its behalf.

53. Until sold, the Responsible Entity will use reasonable endeavours to store the Olive Oil extracted from the Olives during processing in such a manner that its quality is maintained.

### ***Sale of Olive Oil***

54. The Grower unconditionally appoints the Responsible Entity as its sole and exclusive agent to market and sell the Olive Oil, for the term of the Project (clause 6). The Olives from each Olive Grove in the Project will be pooled and sold by the Responsible Entity on behalf of the Growers. The Responsible Entity will use all reasonable endeavours to sell the Olive Oil at a price equivalent to the price likely to be paid for Olive Oil of the same type and quality at the time of sale.

**Olive Orchard Management Agreement**

55. Under the Olive Orchard Management Agreement, the Responsible Entity will engage the Olive Orchard Manager, Olive Grove Management Pty Ltd, to establish the Growers' Olive Groves and to manage and maintain the Olive Groves on the terms and conditions contained in the Agreement. The Olive Orchard Manager will be subject to the direction of the Responsible Entity in all matters relating to the Olive Orchard Management Agreement.

56. The Olive Grove Manager will perform services including planting and the installation of irrigation during the Establishment Period. After the Establishment Period the Olive Grove Manager will provide Ongoing Services and Harvesting Services in relation to the Olive Groves.

**Fees**

57. Under the Management Agreement and the Licence Agreements, the Grower is required to pay the following:

- initial fees on application;
- Olive Orchard Operating Costs;
- annual Management Fees;
- insurance costs;
- Harvesting Costs;
- Processing Costs; and
- Licence Fees.

From 1 July 2009, all the fees, other than Licence Fees will be deducted from Gross Proceeds.

***Initial Fees on application***

58. For each Grower, an initial fee of \$2,420 is payable on application for the following services to be provided in the Establishment Period:

- initial planting and preparation (\$299);
- spacing, posting and protection (\$35);
- installing irrigation (\$137); and
- all other maintenance and management services (\$1,949).

59. A Licence Fee of \$11.45 for each month, or part thereof, is also payable on application for the period from the Commencement Date to 30 June 2007.

## ***Olive Orchard Operating Costs***

60. A Grower is required to pay Olive Orchard Operating Costs as follows:

- \$627, payable on application for the financial year ending 30 June 2007;
- \$440, payable on 1 July 2007 for the financial year ending 30 June 2008; and
- \$440, payable on 1 July 2008 for the financial year ending 30 June 2009.

61. From 1 July 2009, Olive Orchard Operating Costs will be the actual direct costs incurred by the Olive Orchard Manager (on behalf of the Responsible Entity) in maintaining and managing the Grower's Olive Grove. The Olive Orchard Operating Costs will be payable on 1 July in each financial year.

## ***Annual Management Fees***

62. From 1 July 2009, and on 1 July of each succeeding financial year until the end of the Project, the Management Fee will be an amount equal to 8.25% of the Grower's Proportion of the Gross Proceeds for that year.

## ***Insurance Costs***

63. The Grower's Proportion of the cost of insurance taken out by the Responsible Entity on behalf of the Growers will be reimbursable to the Responsible Entity from the Grower's Proportion of the Gross Proceeds.

## ***Harvesting Costs***

64. Harvesting Costs will be deducted from the Grower's Proportion of the Gross Proceeds commencing on 1 July immediately following the first harvest and thereafter on 1 July immediately following each succeeding harvest. Harvesting Costs is defined in the Management Agreement as meaning any costs or expenses incurred by the Responsible Entity when harvesting (clause 30).

## ***Processing Costs***

65. Processing Costs will be deducted from the Grower's Proportion of the Gross Proceeds commencing on 1 July of the year of the first harvest and thereafter on 1 July of each harvest year. Processing Costs is defined in the Management Agreement as meaning any costs or expenses incurred by the Responsible Entity when crushing and processing the Olives to extract Olive Oil (clause 30).

***Licence Fees***

66. For the Financial Year beginning 1 July 2007 and the following Three (3) Financial Years, a Licence Fee of \$137.50 is payable in advance on 1 July of each Financial Year. For the Financial Year beginning 1 July 2011 and each succeeding Financial Year, the Licence Fee payable by all Growers will be an amount equal to 4.95% of the Grower's Proportion of the Gross Proceeds for the period commencing on 1 July of each Financial Year.

***Ongoing Fees***

67. The Gross Proceeds from the sale of the Olive Oil will be paid into a Gross Proceeds Account to be established by the Responsible Entity. From 1 July 2009, Management Fees, Harvesting costs, Processing costs, Insurance Premiums and Olive Orchard Operating Costs are due and payable and will be deducted from the Grower's Proportion of the Gross Proceeds before the proceeds are distributed to the Grower.

***Shares***

68. Each Grower must also subscribe for a minimum of one share in the Landholder, Carcuma Land Holdings Limited, for each Olive Grove. The cost of each share is \$1,000 of which \$1 is payable on application and \$999 on 1 July 2011.

***Finance***

69. Growers may fund their involvement in the Project themselves, borrow from an independent lender or enter into a Terms Payment arrangement with Olive Growers Australia Ltd.

***Terms Payment Agreement***

70. The Responsible Entity will offer a Terms Payment Option under which Growers will be able to pay their Initial fees by monthly instalments.

71. Where a Grower enters into a Terms Payment Option, the full amount of the Initial Fee must be paid to the Responsible Entity within a 12 month period. The instalments that must be made to the Responsible Entity under this arrangement are as follows:

- 11 monthly instalments of \$201.66; and
- 1 final monthly payment of \$201.74.

72. 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 of the ITAA 1936 or the funding arrangements transform the Project into a 'scheme' to which Part IVA of the ITAA 1936 may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project, other than Olive Growers Australia Ltd under the Terms Payment Option, are involved or become involved in the provision of finance to Growers for the Project.

## Ruling

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### Application of this Ruling

73. This Ruling applies only to Growers who:

- are accepted to participate in the Project during the period from the date of this Ruling to 30 November 2006 (Applicant Group 2);
- have executed a Licence Agreement and a Management Agreement during this period; and
- have subscribed to two or more Interests in the Project.

74. A Grower's participation in the Project must constitute the carrying on of a business of primary production. A Grower is not eligible to claim any tax deductions until their application to enter the Project is accepted and the Project has commenced.

75. This Ruling does not apply to:

- Growers in Applicant Group 2, whose application has been conditionally accepted by the Responsible Entity subject to finance, where finance has not been approved by the lender and the funds have not been made available to the Responsible Entity by 30 November 2006;
- Growers who are accepted to participate in the Project before the date of this Ruling or after 30 November 2006; and
- Growers who subscribe to and are allocated only one Interest in the Project.

### **Minimum subscription**

76. 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 Prospectus and PDS, a Grower's application will not be accepted and the Project will not proceed until the minimum subscription of 100 interests is achieved.

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

#### **Division 328**

77. To be an 'STS taxpayer', a Grower must be eligible to be an 'STS taxpayer' and must have elected to be an 'STS taxpayer' (Division 328 of the ITAA 1997). For a Grower participating in the Project, the recognition of income and the timing of tax deductions is different depending on whether the Grower who was an 'STS taxpayer' prior to 1 July 2005 continues to use the cash accounting method (called the 'STS accounting method') – see sections 328-120 and 328-125 of the *Income Tax (Transitional Provisions) Act 1997*.

78. For such Growers, a reference in this Ruling to an amount being deductible when 'incurred' will mean that amount is deductible when paid and a reference to an amount being included in assessable income when 'derived' will mean that amount is included in assessable income when received.

### **25% entrepreneurs tax offset**

#### **Subdivision 61-J**

79. For the first income year starting on or after 1 July 2005, Subdivision 61-J provides a tax offset of up to 25% of income tax liability related to the business income of a business in the STS with annual group turnover of less than \$75,000. Entitlement to the offset varies depending on the type of entity and is therefore outside the scope of this Ruling.

**Assessable income****Section 6-5**

80. 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.

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

**Deductions for Management Fees, Olive Orchard Operating Expenses and Licence Fees****Sections 8-1**

82. A Grower may claim tax deductions for the following revenue expenses on a per Olive Grove basis:

<b>Fee Type</b>	<b>ITAA 1997 section</b>	<b>Year ended 30 June 2007</b>	<b>Year ended 30 June 2008</b>	<b>Year ended 30 June 2009</b>
<b>Management Fees</b>	8-1	\$1,322 See Notes (i) & (ii)	Nil	Nil
<b>Licence Fees</b>	8-1	See Notes (i), (ii) & (iii)	\$137.50 See Notes (i), (ii) & (iv)	\$137.50 See Notes (i), (ii) & (iv)
<b>Olive Orchard Operating Costs</b>	8-1	\$627 See Notes (i) & (ii)	\$440 See Notes (i), (ii) & (iv)	\$440 See Notes (i), (ii) & (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 (for example, input tax credits): Division 27.
- (ii) The Initial Management Fee, Olive Orchard Operating Expenses and Licence Fees are deductible under section 8-1 in full in the year that they are incurred.
- (iii) The Licence Fee included in the initial fees on application is \$11.45 per month or part thereof, for the period from the Commencement Date to 30 June 2007 for Applicant Group 2. The Licence fee is deductible in the income year in which it is incurred.

**Deductions for capital expenditure (non-STS taxpayers)****Division 40**

83. A Grower who is not an 'STS taxpayer' will be entitled to tax deductions relating to posts, irrigation and the establishment and decline in value of the Olive Trees. All deductions shown in the following Table are determined under Division 40.

<b>Fee Type</b>	<b>ITAA 1997 section</b>	<b>Year ended 30 June 2007</b>	<b>Year ended 30 June 2008</b>	<b>Year ended 30 June 2009</b>
<b>Posts/stakes</b>	40-25	Must be calculated See Notes (v) & (vi)	Must be calculated See Notes (v) & (vi)	Must be calculated See Notes (v) & (vi)
<b>Irrigation</b>	40-515	\$45.67 See Notes (v) & (vii)	\$45.67 See Notes (v) & (vii)	\$45.67 See Notes (v) & (vii)
<b>Establishment of Olive trees</b>	40-515	Nil	Nil	Must be calculated See Notes (v) & (viii)

**Notes:**

- (iv) If the Grower is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (v) Posts and Stakes meet the definition of a 'depreciating asset' in section 40-30 and therefore each Grower's interest in the posts and stakes is a 'depreciating asset'. The 'cost' of the asset is the amount paid by the Grower. The decline in value of the asset is calculated using the formula in either subsection 40-70(1) ('diminishing value method') or subsection 40-75(1) ('prime cost method'). Both formulas rely on the 'effective life' of the posts.

There has not been any determination of the 'effective life' of posts and stakes by the Commissioner. Therefore, Growers must self-assess the 'effective life' of posts and stakes (section 40-105). For Growers who are accepted into the Project during the period from the date of this Ruling to 30 November 2006, the posts and stakes will be installed and first used during the year ended 30 June 2007.

For a Grower who purchases only two Olive Groves in this Project, as required under this Ruling, their interest in the posts and stakes will be a 'low cost asset' that is, an asset costing less than \$1,000. A 'low-cost asset' 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 posts and stakes would also have to be allocated to that pool. Otherwise, the Grower must decide whether to create a 'low-value pool'.

If the asset is allocated to a 'low-value pool', the capital expenditure on the posts and stakes will be deducted under the diminishing value methodology of the pool based on a rate of 18.75% in the year the posts and stakes are first used and a rate of 37.5% in subsequent years (section 40-440). If the posts and stakes are not allocated to a 'low-value pool', they can be written off based on the 'effective life' of the asset.

- (vi) An irrigation system, dam or bore is a 'water facility' as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. A deduction for water facilities is available under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one third of the capital expenditure incurred by each Grower on the installation of the 'water facility' in the year in which it is incurred and one third in each of the next 2 years of income (section 40-540).
- (vii) The olive trees meet the definition of 'horticultural plant' in subsection 40-525(2). As Growers hold the land under a licence, the condition in item 3 of subsection 40-525(2) is met and a deduction for the decline in value of 'horticultural plants' is available under paragraph 40-515(1)(b).

The deduction for the olive trees is determined using the formula in section 40-545 and is based on the capital expenditure incurred by the Grower that is attributable to their establishment. As the olive trees have an 'effective life' of 30 years or more, for the purposes of section 40-545, this results in a straight-line write-off at a rate of 7% per annum. The deduction is allowable when the olive trees enter their first commercial season (section 40-530, item 2). The Project Manager will inform Growers of when the olive trees enter their first commercial season.

**Deductions for capital expenditure (STS taxpayers)*****Division 328 and Subdivision 40-F***

84. A Grower who is an 'STS taxpayer' will also be entitled to tax deductions relating to posts/stakes, irrigation and the establishment and decline in value of the olive trees.

85. Posts and stakes meet the definition of a 'depreciating asset' and deductions relating to the 'cost' of posts and stakes must be determined under Division 328. 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.

86. An 'STS taxpayer' may claim deductions in relation to irrigation under Subdivision 40-F because irrigation meets the definition of a 'water facility'. As expenditure on irrigation would also meet the definition of a 'depreciating asset', an 'STS taxpayer' may choose to claim a deduction under Division 328.

87. Deductions for the olive trees must be determined under Subdivision 40-F.

88. The deductions shown in the following Table are on a per Olive Grove basis and assumes the Grower has chosen to claim deductions for expenditure on irrigation under Division 328. If the expenditure is claimed under Subdivision 40-F, the deduction is determined as for Non-STS Taxpayers (see the table at paragraph 83 of this Ruling).

<b>Fee Type</b>	<b>ITAA 1997</b>	<b>Year ended 30 June 2007</b>	<b>Year ended 30 June 2008</b>	<b>Year ended 30 June 2009</b>
<b>Posts/stakes</b>	Subdiv 328-D	\$35 See Notes (ix) & (x)	Nil See Notes (ix) & (x)	Nil See Notes (ix) & (x)
<b>Irrigation</b>	Subdiv 328-D	\$137 See Notes (ix) & (xi)	Nil See Notes (ix) & (xi)	Nil See Notes (ix) & (xi)
<b>Establishment of Olive trees</b>	40-515	Nil	Nil	Must be calculated See Notes (ix) & (xii)

## Notes:

- (viii) If the Grower is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (ix) Posts and stakes meet the definition of a 'depreciating asset' in section 40-30. Where a Grower acquires the minimum allocation of two Olive Groves required under this Ruling, the Grower's interest in the posts and stakes is a 'low-cost asset' as defined in subsection 40-425(2). 'Low cost assets' cannot be allocated to a 'general STS pool' (section 328-180).

A deduction equal to the amount of the Grower's expenditure for the posts and stakes is available in the income year in which they are used or 'installed ready for use'. This is 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.

Where a Grower acquires **multiple Interests**, the Grower's interest in the posts and stakes may not be a 'low cost asset' as the cost may be \$1,000 or greater. For these Growers, their interest in the posts and stakes is a 'depreciating asset' that can be allocated to a 'general STS pool'. The 'cost' of the asset is the amount paid by each Grower.

For posts and stakes allocated to a 'general STS pool' the tax deduction allowable is determined in the year ended 30 June 2007 by multiplying the 'cost' of the interest by half the 'general STS pool rate, that is, by 15%.

Each Grower's interest in the posts and stakes is allocated to their 'general STS pool' at the end of the financial year ended 30 June 2007 and that part of the 'cost' not deducted in the first year is added to the pool balance. In subsequent years, the full pool rate of 30% will apply.

- (x) Any irrigation system, dam or bore is a 'water facility' as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. If the expenditure is on a 'depreciating asset' (the underlying asset), the Grower may choose to claim a deduction under either Division 328 or Subdivision 40-F.

For the purposes of Division 328, each Grower's interest in the underlying asset is itself deemed to be a 'depreciating asset'. If the 'cost' apportionable to that deemed 'depreciating asset' is less than \$1,000, the deemed asset is treated as a 'low-cost asset' and that amount is deductible in full when the underlying asset is first used or 'held' ready for use. This is provided the Grower is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income.

If the deemed asset is not treated as a 'low-cost asset', the tax deduction allowable in the year ended 30 June 2007 is determined by multiplying its 'cost' by half the relevant STS pool rate. At the end of the year, it is allocated to the relevant STS pool and in subsequent years the full pool rate will apply.

If the expenditure is not on a 'depreciating asset', or if the Grower chooses to use Subdivision 40-F, the deductions are claimed under Subdivision 40-F, paragraph 40-515(1)(a). The deduction is equal to one third of the capital expenditure incurred by each Grower on the installation of the 'water facility', in the year in which it is incurred and one third in each of the next 2 years of income (section 40-540).

- (xi) The olive trees meet the definition of 'horticultural plant' in subsection 40-525(2). As Growers hold the land under a licence, the condition in item 3 of subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value.

The deduction for the olive trees is determined using the formula in section 40-545 and is based on the capital expenditure incurred by the Grower that is attributable to their establishment. As the olive trees have an 'effective life' of 30 years or more, 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 (subsection 40-530(2)). The Project Manager will inform Growers of when the olive trees enter their first commercial season.

## **Shares**

89. The shares in Carcuma Land Holdings Limited are CGT assets (section 108-5) and the amounts paid by a Grower to acquire the shares are an outgoing of capital and not allowable as a deduction.

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

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

### **Trading stock**

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

91. A Grower who is not an 'STS taxpayer' will, in some years, hold Olive Oil 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.

92. 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***

93. A Grower who is an 'STS taxpayer' may, in some years, hold Olive Oil 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)).

94. 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)).

### ***Interest***

95. 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 115 to 122 of this Ruling as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant loan agreement or is at the Grower's choice.

**Division 35 – deferral of losses from non-commercial business activities*****Section 35-55 – Commissioner's discretion***

96. A Grower who is an individual accepted into the Project 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 the income years ending **30 June 2007 to 30 June 2011** for Applicant Group 2 Growers. 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.

**Section 82KL and Part IVA**

97. 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:

- 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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**Commissioner of Taxation**19 July 2006

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## Appendix 1 – Explanation

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❶ ***This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.***

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

98. For the expenditure referred to in the Tables above to constitute allowable deductions the Grower's horticulture activities as a participant in the Olive Growers Australia Project 2005/2006 must amount to the carrying on of a business of primary production. These horticulture activities will fall within the definitions of 'horticulture' and 'commercial horticulture' in section 40-535.

99. For schemes such as that of the Olive Growers Australia Project 2005/2006, 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.

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

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

101. In this Project, each Grower enters into a Management Agreement and four Licence Agreements.

102. Under the Licence Agreements, each individual Grower will have rights over a specific and identifiable area of land. The Licence Agreements provide the Grower with an ongoing interest in the specific Olive Trees on the licenced area for the term of the Project. Under the licences the Grower must use the land in question for the purpose of carrying out horticultural activities and for no other purpose. The licences allow the Responsible Entity to come onto the land to carry out its obligations under the Management Agreement.

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

104. In establishing the Olive Groves, the Grower engages the Responsible Entity to purchase and install posts, stakes and irrigation and to acquire and plant olive trees on the Grower's Olive Groves. During the term of the Project, these assets will be used wholly to carry out the Grower's horticulture activities. The Responsible Entity is also engaged to harvest and process the olives and sell, on the Grower's behalf, the olive oil produced from the Grower's Olive Groves.

105. 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.

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

107. The pooling of olives grown on the Grower's Olive Groves with the olives of other Growers is consistent with general horticulture practices. Each Grower's proportionate share of the sale proceeds of Olive Oil from the pooled olives will reflect the proportion of the Olive Oil contributed from their Olive Groves.

108. The Responsible Entity's services and the installation of assets on the Grower's behalf are also consistent with general horticultural practices. The assets are of the type ordinarily used in carrying on a business of horticulture. While the size of the Olive Groves are relatively small, they are of a size and scale to allow them to be commercially viable.

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

110. The horticulture activities, and hence the fees associated with their procurement, are consistent with an intention to commence regular activities that have an 'air of permanence' about them. For the purposes of this Ruling, the Growers' horticulture activities in the Olive Growers Australia Project 2005/2006 will constitute the carrying on of a business.

## **The Simplified Tax System**

### ***Division 328***

111. 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.

112. 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 project fees**

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

113. Consideration of whether the Management Fees, Olive Orchard Operating Expenses and Licence Fees (the 'project 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.

114. The project fees associated with the horticulture activities will relate to the gaining of income from the Grower's business of horticulture, and hence have a sufficient connection to the operations by which income (from the regular sale of olive oil) 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 fees is identifiable from the arrangement. The project fees appear to be reasonable. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

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

115. 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 or the licensing 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.

116. For this Project only section 82KZL of the ITAA 1936 (an interpretative provision) and sections 82KZME and 82KZMF of the ITAA 1936 are relevant. Where the requirements of sections 82KZME and 82KZMF are met, taxpayers determine deductions for prepaid expenditure under section 82KZMF using the formula in subsection 82KZMF(1). These provisions also apply to STS taxpayers because there is no specific exclusion contained in section 82KZME that excludes STS taxpayers from the operation of section 82KZMF.

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

117. Where the requirements of subsections 82KZME(2) and (3) of the ITAA 1936 are met, the formula in subsection 82KZMF(1) of the ITAA 1936 (see paragraph 121 of this Ruling) will apply to apportion expenditure that is otherwise deductible under section 8-1 of the ITAA 1997. The requirements of subsection 82KZME(2) will be met if expenditure is incurred by a taxpayer in return for the doing of a thing that is not to be wholly done within the year the expenditure is made. The year in which such expenditure is incurred is called the 'expenditure year' (subsection 82KZME(1)).

118. The requirements of subsection 82KZME(3) of the ITAA 1936 will be met where the agreement (or arrangement) has the following characteristics:

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

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

119. For the purpose of these provisions, the agreement referred to includes all activities that relate to the agreement (subsection 82KZME(4) of the ITAA 1936. This has particular relevance for a Grower in this Project who, in order to participate in the Project may borrow funds from a financier. Although undertaken with an unrelated party, that financing would be an element of the arrangement. The funds borrowed and the interest deductions are directly related to the activities under the arrangement. If a Grower prepays interest under such financing arrangements, the deductions allowable will be subject to apportionment under section 82KZMF of the ITAA 1936.

120. There are a number of exceptions to these rules, but for Growers participating in this Project, only the 'excluded expenditure' exception in subsection 82KZME(7) of the ITAA 1936 is relevant. 'Excluded expenditure' is defined in subsection 82KZL(1) of the ITAA 1936. However, for the purposes of Growers in this Project, 'excluded expenditure' is prepaid expenditure incurred under the scheme that is less than \$1,000. Such expenditure is immediately deductible.

121. Where the requirements of section 82KZME of the ITAA 1936 are met, section 82KZMF of the ITAA 1936 applies to apportion relevant prepaid expenditure. Section 82KZMF uses the formula below, to apportion prepaid expenditure and allow a deduction over the period that the benefits are provided.

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

122. In the formula, 'eligible service period' (defined in subsection 82KZL(1) of the ITAA 1936) means the period during which the thing under the agreement is to be done. The eligible service period begins on the day on which the thing under the agreement commences to be done or on the day on which the expenditure is incurred, whichever is the later, and ends on the last day on which the thing under the agreement ceases to be done, up to a maximum of 10 years.

*Application of the prepayment provisions to this Project*

123. In this Project, an initial management fee of \$1,949 and rent of \$11.45 per month per Allotment will be incurred on the execution of the Management Agreement and the Licence Agreement. The management fee and rent are charged for providing management services or leasing of land to a Grower by 30 June of the year of the Management Agreement and Licence Agreement coming into effect. Under these agreements, further annual expenditure is required each year during the term of the Project for the provision of management services and lease of land until 30 June in those years.

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

125. There is also no evidence that might suggest the management services covered by the fee could not be provided within the relevant expenditure year. Thus, for the purposes of this Ruling, it can be accepted that no part of the initial management fee, and the fees for subsequent years, is for the Project Manager doing 'things' that are not to be wholly done within the expenditure year. Under the Licence, rent is payable for the lease of the land during the expenditure year.

126. On this basis, provided a Grower incurs expenditure as required under the Project agreements, as set out in paragraph 82 of this Ruling, then the basic precondition in subsection 82KZME(2) of the ITAA 1936 is not satisfied and, in these circumstances, section 82KZMF of the ITAA 1936 will have no application.

*Growers who choose to pay fees for a period in excess of that required by the Project's agreements*

127. Where a Grower chooses to prepay fees under the agreements for a period beyond the income year in which the expenditure is incurred, the prepayment provisions (see paragraphs 115 to 122 of this Ruling) will apply to determine the amount and timing of the deductions regardless of whether the Grower is an STS taxpayer or not. These provisions apply to STS taxpayers because there is no specific exclusion contained in section 82KZME of the ITAA 1936 that excludes STS taxpayers from the operation of section 82KZMF of the ITAA 1936.

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

129. However, as noted above, prepaid fees of less than \$1,000 incurred in an expenditure year will be 'excluded expenditure' and will be not subject to apportionment under section 82KZMF of the ITAA 1936.

## **Expenditure of a capital nature**

### ***Division 40 and Division 328***

130. 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 posts, stakes, irrigation and the establishment of the Olive Trees is of a capital nature. This expenditure falls for consideration under Division 40 or Division 328.

131. 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'.

132. The tax treatment of capital expenditure has been dealt with in a representative way in paragraphs 83 and 88 of this Ruling.

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

133. The Commissioner has applied the principles set out in Taxation Ruling TR 2001/14 Income tax: Division 35 – non-commercial business losses in deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income years ending **30 June 2007 to 30 June 2011** (Applicant Group 2).

134. Accordingly, based on the evidence supplied, the Commissioner has determined that for those income years ended 30 June 2007 up to and including 30 June 2011:

- it is because of its nature the business activity of a Grower that 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 olive 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.

135. 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**

136. The operation of section 82KL of the ITAA 1936 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 of the ITAA 1997.

**Part IVA – general tax avoidance provisions**

137. For Part IVA of the ITAA 1936 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).

138. The Olive Growers Australia Project 2005/2006 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 82, 83 and 88 of this Ruling 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.

139. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting and sale of their Olive Oil. 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) of the ITAA 1936, it cannot be concluded, on the information available, that participants will enter into the scheme for the dominant purpose of obtaining a tax benefit.

## **Appendix 2 – Detailed contents list**

140. The following is a detailed contents list for this Product Ruling:

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TR 97/11; TR 98/22; TR 2000/8;  
TR 2001/14

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- fee expenses
- horticulture
- irrigation expenses
- management fees expenses
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- primary production
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- primary production income
- producing assessable income
- product rulings
- public rulings
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- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters
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