



PR 2006/97 - Income tax: Primary Yield Tomato Project - Pre 30 June 2006

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 This document has changed over time. This is a consolidated version of the ruling which was published on *24 May 2006*



Product Ruling

Income tax: Primary Yield Tomato Project – Pre 30 June 2006

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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

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates. In this Ruling this arrangement is referred to as the 'Primary Yield Tomato Project' 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;
 - section 25-25 of the ITAA 1997;
 - Division 27 of the ITAA 1997;
 - Division 35 of the ITAA 1997;
 - Subdivision 61-J 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 82KZL of the ITAA 1936;
 - sections 82KZME and 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 (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 entities

7. The class of entities to whom this Ruling applies consists of the entities more specifically identified in the Ruling part of this Product Ruling 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;
- entities who participate in the Primary Yield Tomato Project (the Project) through offers made other than through the Product Disclosure Statement;
- entities who are accepted to participate in the Project after 15 June 2006;
- entities whose 'Initial Tomato Management Services', including the preparation of the 'Grower's Lots' and the 'Planting Services', have not been provided by the Manager on or before 30 June 2006;
- entities who finance their participation in the Project with loans other than from Primary Yield Finance Pty Ltd, or other than an Instalment Agreement with as described at paragraphs 46 to 51 of this Ruling; or
- Environinvest Limited or its associates.

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 53.

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

12. This Ruling applies prospectively from 24 May 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

16. This Product Ruling is withdrawn and ceases to have effect after 30 June 2008. 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 entity's involvement in the scheme.

Scheme

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

- Application for a Product Ruling as constituted by documents received on 21 December 2005 and additional correspondence received from the applicant's representative dated 3 and 24 February 2006, 8, 19, 20, 23 and 31 March 2006, 6, 10, 11, 12, 21, 24, 27 and 28 April 2006, 1, 4, 12, 15, and 16 May 2006;
- **Product Disclosure Statement** ('PDS') for the Project received 16 May 2006;
- Draft **Supplementary PDS** for the Project received 15 May 2006;
- Draft **Constitution** for the Project received 21 December 2005;
- Draft Compliance Plan for the Project received 21 December 2005;
- Draft **Management Agreement** between the Environinvest Ltd (as Manager) and a Grower for Primary Yield Tomato Project received 15 May 2006;
- Draft Head Lease between the Lessor and Environinvest Ltd ('the Lessee') received 15 May 2006;
- Draft **Grower Lease** between Environinvest ('the Lessor') and a Grower for Primary Yield Tomato Project received 15 May 2006;
- Draft Heads of Agreement between Environinvest Ltd (as Manager) and the services provider for Primary Yield Tomato Project received 21 December 2005;

- Draft Operations Management Agreement between Environinvest Ltd (as Manager) and the services provider for Primary Yield Tomato Project received 6 April 2006;
- Draft **Instalment Agreement** between Environinvest Ltd (as Manager) and a Grower for Primary Yield Tomato Project received 21 December 2005; and
- Draft **Finance Application** between Primary Yield Finance Pty Ltd and a Grower for Primary Yield Tomato Project received 21 December 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.

18. The documents highlighted are those that a Grower may enter into. For the purposes of describing the scheme 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 scheme. The effect of these agreements is summarised as follows.

19. 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

20. The main features of the Project are as follows:

Location	Guyra, New South Wales
Type of business to be carried on by each participant	Commercial growing and cultivation of tomato plants for the purpose of harvesting and selling the tomatoes.
Number of hectares offered for cultivation	5 hectares
Size of each interest	1 square metre
Minimum allocation	50 Lots
Minimum subscription	2 Growers and 100 Lots
Number of plants per hectare	30,000
Term of the Project	6 years
Initial cost	\$92.40 per Lot
Initial cost per hectare	\$924,000
Ongoing costs	Management Fees; and Rent.
Other costs	Packing Fees; Sales Management Fees; and Out of Pocket Expenses.

21. The Project will be registered as a managed investment scheme under the *Corporations Act 2001*. Environinvest has been issued with an Australian Financial Service Licence and will be the Responsible Entity for the Project.

22. An offer to participate in the Project will be made through the PDS. The offer will invite participants to subscribe for a minimum of 50 'Lots' in the Project.

23. To participate in the Project a participant must complete the 'Application and Power of Attorney Form' in the PDS and pay the 'Initial Management Fee'. The 'Initial Management Fee' will be held by the Responsible Entity initially in the 'Project Account' as bare Trustee for the 'Applicant' and will be released to the Responsible Entity in accordance with clause 8 of the Constitution when certain specified criteria have been met.

24. Growers will enter into a Grower Lease with Environinvest. The Grower Lease will comprise contractual rights in relation to parcels of land of one square metre called a 'Lot'. Each Grower will lease a minimum of 50 'Lots'.

25. The Grower Lease gives Growers the right to use their 'Lots' during the term of the Project to carry on their 'Business' of planting, tending, growing and caring for their 'Tomato Plants' and the harvesting of their 'Tomatoes'.

26. Under the Management Agreement each Grower will engage Environinvest to manage their 'Business' during the term of the Project.

27. For the purposes of this Ruling, Growers whose applications are accepted on or before 15 June 2006 will become 'Pre 30 June 2006 Growers'. This Ruling only applies to 'Pre 30 June 2006 Growers'. **Note that a separate Product Ruling will issue for 'Post 30 June Growers' who are accepted into the Project from 1 July 2006 to 31 August 2006.**

Constitution

28. The Constitution for the Project sets out the general functions, powers and duties under which the Responsible Entity agrees to act for the Growers and to manage the Project. The Grower Lease and the Management Agreement are Schedules to the Constitution. These Agreements will be executed on behalf of each Grower who has signed the 'Application and Power of Attorney Form' attached to the PDS and who is accepted into the Project. After acceptance and execution of the Agreements, Growers are bound by the Constitution, the Management Agreement and the Grower Lease. The Responsible Entity will keep a register of all Growers that are accepted to participate in the Project.

29. Among the other things, the Constitution sets out details summarised as follows:

- appointment of the Responsible Entity as the Grower's irrevocable agent, representative and attorney (clause 3);
- procedures relating to applications for interests in the Project and the 'Application Moneys' (clause 7);
- procedures relating to the issue of interests and the transfer of 'Application Moneys' (clause 8);
- execution of the 'Project Documents' by the Responsible Entity (clause 9) and the issue to each Grower of a 'Certificate' setting out details of the Grower, their interest in the Project, and the number of 'Grower's Lots' subscribed for by the Grower (clause 10);
- the Responsible Entity's powers and duties (clause 14);
- the setting up and maintenance of a Register of Growers (clause 15);
- procedures relating to the collection of all proceeds, deductions from the proceeds, and distribution of the proceeds (clause 19);
- resolution of complaints made by the Growers in relation to the Project or the Responsible Entity (clauses 20 and 21);
- assignment of a Grower's interest (clause 24);
- retirement and removal of the Responsible Entity (clause 26);
- procedures for calling a meeting of Growers (clause 29); and
- events and procedures for winding up the Project (clause 33).

Acceptance of Applications

30. In order to acquire an interest in the Project, the Grower must make an application in a form approved by the Responsible Entity accompanied by payment of the 'Application Money'. Payment of the 'Application Money' must be made by cheque or money order, credit or debit card facility, an 'Instalment Agreement, an approved finance arrangement, or a combination of these payment methods.

Compliance Plan

31. As required by the *Corporations Act 2001*, Environinvest has prepared a Compliance Plan. The purpose of the Compliance Plan is to ensure that Environinvest manages the Project in accordance with its obligations and responsibilities contained in the Constitution and that the interests of Growers are protected.

Head Lease

32. The Responsible Entity will enter into a Head Lease Agreement with the Lessor in respect of the 'Land', including the 'Glasshouse', required for the Project.

Grower Lease

33. Each Grower will execute a Grower Lease with the Responsible Entity. The Responsible Entity will grant to the Grower the right to exclusively possess, occupy, use and enjoy the 'Grower's Lots', together with all improvements (including the 'Tomato Plants'), for cultivating, planting, tending, growing, caring for, and the harvesting of and selling the Tomatoes for a commercial profit (clauses 2 and 3).

34. The Grower Lease sets out the rights and obligations of the parties to the Agreement. The Grower Lease operates on and from the 'Commencement Date' until terminated in accordance with the terms of clause 2.2.

35. The Grower Lease also:

- provides that each Grower owns the 'Tomatoes' and the 'Tomato Plants' on their 'Lots' during the term of the Lease (clause 4);
- requires that the Grower pays Rent and other fees during the term of the Lease (clause 5);
- sets out the Grower's and the Lessor's covenants (clauses 6 and 7);
- provides for termination in the case of default (clause 13) and sets out dispute resolution procedures (clause 15).

Heads of Agreement and Operations Management Agreement

36. The Responsible Entity has entered into a Heads of Agreement for the execution of an Operations Management Agreement with the 'Services' provider to undertake the day to day management of the Project.

Management Agreement

37. Under the Management Agreement the Grower appoints the 'Manager' as an independent contractor to manage the Grower's 'Business' and to carry out the management services and, as the Grower's sole agent, to procure the sale of the 'Grower's Tomatoes' (clause 2). This Agreement commences on the date the Responsible Entity accepts the Grower application under the PDS and continues until termination under clause 3.

38. On or after the 'Commencement Date' the Manager will commence the provision of the 'Initial Tomato Management Services', including the preparation of the 'Grower's Lots' and the 'Planting Services', and will use all reasonable endeavours to complete the 'Initial Services' before the end of the 'Application Year' (clause 4(a)). This Product Ruling will not apply if the 'Initial Tomato Management Services' are not completed by the Manager for a Grower on or before 30 June 2006.

39. After the completion of the 'Initial Tomato Management Services' the Manager will commence the provision of the 'Services' and will provide the 'Services' until the termination of the Project (clause 4(b)).

40. The 'Services' include 'Planting Services', 'Maintenance Services', 'Harvesting Services', 'Packing Services' and 'Sales Management Services'.

Pooling of 'Tomatoes' and 'Grower's Entitlement' to 'Net Harvest Proceeds'

41. Each 'Grower's Tomatoes' will be pooled with the 'Tomatoes' of other Growers in the Project and the Grower will be entitled to a proportionate share of the net proceeds of sale of the total tomatoes produced by all Growers in the 2006 Project. The Management Agreement sets out provisions relating to the 'Grower's Entitlement' to 'Harvest Proceeds' (clause 6).

42. This Product Ruling only applies where the following principles apply to the pooling and distribution arrangements:

- only Growers who have contributed tomatoes to the sales pool in a 'Subsequent Year' are entitled to benefit from distributions of 'Harvest Proceeds' from the pool; and
- any pooled 'Crops must consist only of 'Crops' or 'Insurance Proceeds' contributed by Growers of the same Project 'Class'.

Fees

43. Under the terms of the Management Agreement (clause 5) and the Grower Lease (clause 5) a Grower will make payments as described below:

Initial Management Fees

- for the period from Commencement Date until 30 June 2006, \$92.40 per 'Lot', payable on or before the Commencement Date (Item 4 of the Schedule).

Management Fees

- for the period 1 July 2006 to 30 June 2007 and each 'Subsequent Year', a fixed management fee of \$27.50 per 'Lot' (indexed for CPI beginning from the year ended 30 June 2008), plus an amount equal to 36.66% of the 'Grower's Entitlement' to 'Harvest Proceeds', payable each 30 June (Item 5 of the Schedule).

Sales Management Fees

- for the period 1 July 2007 to 30 June 2008 and each subsequent year, an amount equal to 11% of the 'Grower's Entitlement' to 'Harvest Proceeds', payable each 30 June (Item 6 of the Schedule).

Packing Fees

- for the period 1 July 2006 to 30 June 2007 and each 'Subsequent Year', a fixed packing fee of \$4.10 (indexed for CPI beginning from the year ended 30 June 2008) per 5kg box used to pack the 'Grower's Interest' in the harvest, payable each 30 June.

Out of Pocket Expenses

- for the period 1 July 2007 to 30 June 2008 and each subsequent year, an amount equal to the Grower's share of the total Out of Pocket Expenses (if any) incurred or estimated to be incurred by the Manager, payable within 15 Business Days of the date of a 'Notice'.

Grower Lease (Rent)

- for the period 1 July 2006 to 30 June 2007 and each 'Subsequent Year', a fixed rent of \$24.20 (indexed for CPI beginning from the year ended 30 June 2008), payable each 30 June.

Finance

44. A Grower who does not pay the 'Initial Management Fee' in full upon application and who does not receive an approval to pay its fees under the Instalment Agreement (see below), can borrow from Primary Yield Finance, or from an independent lender external to the Project. **A Grower who funds its participation in the Project through loans with Environinvest Ltd is not covered by this Product Ruling and is not entitled to the tax benefits set out in this Product Ruling.**

45. Only the Instalment Agreement Arrangement set out in paragraphs 50 to 51 and finance arrangements with Primary Yield Finance Pty Ltd that do not differ from the arrangement described in paragraphs 46 to 49 are covered by this Product Ruling. No other finance arrangements are covered by this Product Ruling. A Grower who enters into a finance arrangement with an independent lender external to the Project may request a private ruling on the deductibility or otherwise of interest incurred under finance arrangements not covered by this Product Ruling.

Finance offered by Primary Yield Finance Pty Ltd

46. Subject to the terms and conditions of the 'Loan Agreement' a Grower (called 'the Borrower' in the Primary Yield Finance Pty Ltd Loan Application Form and Loan Agreement) can borrow from Primary Yield Finance (as the 'Lender').

47. Subject to Primary Yield Finance accepting the 'Borrower's' application, the 'Borrower' will be bound by the terms and conditions of the Loan Agreement upon signing the Loan Application Form and Loan Agreement and after the Loan Application Form and Loan Agreement are executed.

48. Although details of Loan Agreements with Primary Yield Finance may vary at the discretion of the Lender, Growers are not covered by this Product Ruling where they enter into a Loan Agreement with Primary Yield Finance which includes any of the following features:

- the 'Term' of the loan exceeds 4 years;
- repayments of the 'Loan' are not made by equal repayments of principal and interest made monthly in arrears; or
- the 'Loan' includes any interest only period.

49. Common features of the Loan Application Form and Loan Agreement offered by Primary Yield Finance require that:

- the Grower's application to participate in the Project has been accepted by Environinvest;
- the Grower pays a 'Loan Establishment Fee' of \$250;

- Primary Yield Finance will take security over the Growers 'Allotments' and 'Tomato Plants';
- additional interest will be charged at the Commonwealth Bank 55 Day Interest Free Standard VISA Credit Card Rate on overdue amounts due and payable; and
- Growers agree to make equal repayments monthly in arrears of the 'Instalment Amount', which is stipulated in Item 10 of the Schedule, on each 'Date of Payment' over the 'Term' of the 'Loan' as detailed in the Schedule.

Instalment Agreements with Environinvest Ltd

50. Where Environinvest accepts that the 'Initial Management Fee' can be paid under the Instalment Agreement, the Grower must complete an Instalment Agreement. Environinvest reserves the right to either accept or reject the application.

51. If the Instalment Agreement is accepted by Environinvest, the Grower will be required to pay their 'Application Money' on the date and the amount specified in Item 7 of the Schedule in the Instalment Agreement, or as otherwise agreed by the Grower and the Manager from time to time provided that the 'Application Money' must be paid in full within 12 months of the 'Commencement Date' by the 'Final Repayment Date'.

Other qualifications relating to finance arrangements

52. Other than where the 'Application Money' is paid under an Instalment Agreement, Growers cannot rely on any part of this Ruling if the 'Application Money', is not paid in full on or before 15 June 2006 by the Grower or, on the Grower's behalf, by a lending institution. Where an application is accepted by Environinvest, and that application is subject to finance approval by any lending institution, Growers cannot rely on this Ruling if written evidence of that approval has not been given to Environinvest by the relevant lending institution on or before 15 June 2006.

53. 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 Primary Yield Pty Ltd, are involved or become involved in the provision of finance to Growers for the Project.

Ruling

Application of this Ruling

54. Subject to paragraph 8, this Ruling applies only to Growers who are accepted to participate in the Project on or before 15 June 2006 and who have executed a Management Agreement and a Grower Lease on or before that date. The Grower's participation in the Project must constitute the carrying on of a business of primary production. This Ruling will not apply unless the 'Initial Tomato Management Services', including the preparation of the 'Grower's Lots' and the 'Planting Services' have been provided to the Grower by the Manager on or before 30 June 2006.

Minimum subscription

55. 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, a Grower's application will not be accepted and the Project will not proceed until the minimum subscription of 100 Grower's Lots is achieved.

The Simplified Tax System (STS)

Division 328

56. 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 38 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*.

57. 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

58. For the first income year starting on or after 1 July 2005, Subdivision 61-J provides for 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

59. 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.

Deductions for Management Fees, Grower Lease, Interest and 'Loan Application Fee'

Section 8-1 and section 25-25

60. A Grower may claim tax deductions for each Lot under section 8-1 and section 25-25 for the fees and expenses set out in the Table.

Fee Type	Year ended 30 June 2006	Year ended 30 June 2007	Year ended 30 June 2008
Initial Management Fees	\$92.40 See Notes (i) & (ii)	Nil	Nil
Management Fees	Nil	Amount incurred See Notes (i), (ii) & (iii)	Amount incurred See Notes (i), (ii) & (iii)
Sales Management Fees	Nil	Amount incurred See Notes (i), (ii) & (iii)	Amount incurred See Notes (i), (ii) & (iii)

Packing Fees	Nil	Amount incurred See Notes (i), (ii) & (iii)	Amount incurred See Notes (i), (ii) & (iii)
Out of Pocket Fees	Nil	Amount incurred See Notes (i), (ii) & (iii)	Amount incurred See Notes (i), (ii) & (iii)
Grower Lease (Rent)	Nil	\$24.20 See Notes (i), (ii) & (iii)	Amount incurred See Notes (i), (ii) & (iii)
Interest on loans with Primary Yield Finance Pty Ltd	Nil	As incurred See Notes (iii) & (iv)	As incurred See Notes (iii) & (iv)
Loan Application Fee for loans with Primary Yield Finance Pty Ltd	Must be calculated See Note (v)	Must be calculated See Note (v)	Must be calculated See Note (v)

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 (Division 27).
- (ii) The 'Initial Management Fee' of \$92.40 per Lot, the 'Management Fees' for 'Subsequent Years', the Sales Management Fees, the Packing Fees, any share of Out of Pocket Expenses and the Rent are deductible in the income year that the relevant fee is incurred.
- (iii) This Ruling does not apply to Growers who choose to prepay fees or who choose, or who are required to prepay interest under a loan agreement (see paragraph 84). Subject to certain exclusions, amounts that are prepaid for a period that extends beyond the income year in which the expenditure is incurred may be subject to the prepayment provisions in sections 82KZME and 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 deductibility or otherwise of interest arising from loan agreements entered into with financiers other than Primary Yield Finance Pty Ltd, the internal financier, is outside the scope of this Ruling.

- (v) The Loan Application Fee payable to Primary Yield Finance Pty Ltd is a borrowing expense and is deductible under section 25-25. It is incurred for borrowing moneys that are used or are to be used during that income year solely for income producing purposes. The deduction is spread over the period of the loan or 5 years, whichever is the shorter. The deductibility or otherwise of borrowing costs arising from loan agreements entered into with financiers other than Primary Yield Finance Pty Ltd is outside the scope of this Ruling.

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

Section 35-55 – exercise of Commissioner’s discretion

61. A Grower who is an individual accepted into the Project by 15 June 2006 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 year ending **30 June 2006**. 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 loss arises.

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

62. For a Grower who participates in the Project and incurs expenditure as required by the Management Agreement and the Grower Lease 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 paragraph 84);
- 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.

Appendix 1 – Explanation

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?

63. For the amounts set out in the Tables above to constitute allowable deductions the Grower's horticultural activities as a participant in the Primary Yield Tomato Project must amount to the carrying on of a business of primary production.

64. Where there is a business, or a future business, the gross proceeds from the sale of the 'Tomatoes' 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.

65. For schemes such as that of the Primary Yield Tomato 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 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.

66. 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 rights over land (by licence) on which the 'Tomato Plants' are established;
- the Grower has a right to harvest and sell the 'Tomatoes' from those plants;
- the horticultural activities are carried out on the Grower's behalf;
- the horticultural 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.

67. In this Project, each Grower enters into a Management Agreement and a Grower Lease.

68. Under the Grower Lease each individual Grower will have rights over a specific and identifiable area of 1 square metre of 'Land' which includes the 'Glasshouse'. The Grower Lease provides the Grower with an ongoing interest in the specific plants on the leased area for the term of the Project. Under the Grower Lease the Grower must use the 'Land' in question for the purpose of carrying out horticulture activities, and for no other purpose. The Grower Lease allows the Project Manager to come onto the land to carry out its obligations under the Management Agreement.

69. Under the Management Agreement the 'Manager' is engaged by the Grower to establish and maintain the 'Tomato Plants' on the Grower's identifiable area of 'Land' during the term of the Project. The Project Manager has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the 'Tomato Plants' on the Grower's behalf.

70. The 'Manager' is also engaged to harvest and sell, on the Grower's behalf, the 'Tomatoes' grown on the Grower's 'Tomato Plants'.

71. 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.

72. 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 'Tomatoes' that will return a before-tax profit, i.e. a profit in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

73. The pooling of 'Tomatoes' grown on the Grower's 'Tomato Plants' with the 'Tomatoes' of other Growers is consistent with general horticultural practices. Each Grower's proportionate share of the sale proceeds of the pooled 'Tomatoes' will reflect the proportion of the 'Tomato Plants' contributed from their 'Grower Lots'.

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

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

76. 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' horticultural activities in the Primary Yield Tomato Project will constitute the carrying on of a business.

The Simplified Tax System

Division 328

77. 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.

78. The question of whether a Grower is eligible to be an 'STS taxpayer' is outside the scope of this Product Ruling (but refer to Taxation Ruling TR 2002/6 and Taxation Ruling TR 2002/11). Therefore, any Grower who relies on those parts of this Ruling that refer to the STS will be assumed to have correctly determined whether or not they are eligible to be an 'STS taxpayer'.

Deductibility of management fees and lease fees

Section 8-1

79. Consideration of whether the management fees and lease 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.

80. The Management Fees, Rent and other fees associated with the horticulture activities will relate to the gaining of income from the Grower's business of horticulture (see above), and hence have a sufficient connection to the operations by which income (from the harvesting and sale of the 'Tomatoes') is to be gained from this business. They will thus be deductible under the first limb of section 8-1. Further, no 'non-income producing' purpose in incurring the fee is identifiable from the scheme. The fee appears to be reasonable. There is no capital component of the Initial Management Fee or the other fees. The expenditure incurred to acquire and plant the 'Tomato Plants' is in the nature of an ordinary expense of operating the horticultural business. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

Interest deductibility**Section 8-1**

(i) A Growers who use Primary Yield Finance Pty Ltd as the finance provider

81. A Grower may finance their participation in the Project through a loan facility with Primary Yield Finance Pty Ltd. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of the Management Fees, Rent and other fees.

82. The interest incurred for the year ended 30 June 2006 and in subsequent years of income will be in respect of a loan to finance the Grower's business operations – the cultivation and growing of the 'Tomato Plants' and the lease of the 'Land' on which the 'Tomato Plants' will have been planted – that will continue to be directly connected with the gaining of 'business income' from the Project. Such interest will, therefore, have a sufficient connection with the gaining of assessable income to be deductible under section 8-1.

(ii) Growers who DO NOT use Primary Yield Finance Pty Ltd as the finance provider

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

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

84. 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 leasing of land) that will not be wholly done within the same year of income as the year in which the expenditure is incurred. If expenditure is incurred to cover the provision of services to be provided within the same year, then it is not expenditure to which the prepayment rules apply.

Application of the prepayment provisions to this Project

85. Under the Scheme to which this Product Ruling applies 'Management Fees', Rent and other fees are incurred annually and the interest payable to Primary Yield Finance Pty Ltd is incurred monthly in arrears. Accordingly, the prepayment provisions in sections 82KZME and 82KZMF of the ITAA 1936 have no application to this Scheme

86. However, sections 82KZME and 82KZMF of the ITAA 1936 may have relevance if a Grower in this Project prepays all or some of the expenditure payable under the Management Agreement and/or the Grower Lease, or prepays interest under a loan agreement (including loan agreements with lenders other than Primary Yield Finance Pty Ltd). Where such a prepayment is made these prepayment provisions will also apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes them from the operation of section 82KZMF.

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

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

Section 35-55 – exercise of Commissioner's discretion

88. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income year **30 June 2006** 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 the income year ended 30 June 2006:

- 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 horticulture 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.

89. 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

90. 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

91. 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).

92. The Primary Yield Tomato 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 60 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.

93. 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 'Tomatoes'. 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.

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 97/11; TR 98/22; TR 2000/8;
TR 2001/14; TR 2002/6;
TR 2002/11

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
- tax shelters project
- taxation administration

Legislative references:

- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
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- ITAA 1936 82KZME
- ITAA 1936 82KZMF
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)
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