

PR 2007/1 - Income tax: Agriwealth 31 March 2007 Radiata Pine Project



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Product Ruling

Income tax: Agriwealth 31 March 2007 Radiata Pine Project

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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. 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.

Terms of use of this Product Ruling

This Product Ruling has been given on the basis that the entity(s) who applied for the Product 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 Product Ruling.

What this Ruling is about

1. This Product Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified in the Ruling section (below) apply to the defined class of entities, who take part in the scheme to which this Ruling relates. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated. In this Product Ruling this scheme is referred to as the 'Agriwealth 31 March 2007 Radiata Pine Project' or simply as 'the Project'.

Class of entities

2. This part of the Product Ruling specifies which entities can rely on the tax benefits set out in the Ruling section of this Product Ruling and which entities cannot rely on those tax benefits.

3. The class of entities who can rely on those tax benefits are referred to as Growers. Growers will be those entities that are accepted to participate in the scheme specified below on or after the date this Product Ruling is made and who have executed the relevant Project Agreements set out in paragraph 29 of this Ruling on or before 31 March 2007. They must 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.

4. The class of entities who can rely on the tax benefits set out in the Ruling section of this Product Ruling does **not** include entities who:

- do not acquire a minimum of two Timberlots in the Project (refer to paragraph 41 of this Ruling);
- intend to terminate their involvement in the scheme prior to its completion, or who otherwise do not intend to derive assessable income from it;
- are accepted into this Project before the date of this Ruling or after 31 March 2007;
- participate in the scheme through offers made other than through the Information Memorandum;
- have their application conditionally accepted by Stanford Australia Finance Limited subject to finance for the payment of the application fee, where the finance has not been approved by the lender or the funds have not been made available to Stanford Australia Finance Limited by 31 March 2007; or
- enter into finance schemes with financiers associated with Stanford Australia Finance Limited or United Pacific Finance Pty Limited.

Qualifications

5. The class of entities defined in this Product Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 29 to 71 of this Ruling.

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

- this Product 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 Product Ruling may be withdrawn or modified.

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Date of effect

8. This Product Ruling applies prospectively from 24 January 2007, the date this Product Ruling is made. It therefore applies only to the specified class of entities that enter into the scheme from 24 January 2007 until 31 March 2007, being the closing date for entry into the scheme. This Product Ruling provides advice on the availability of tax benefits to the specified class of entities for the income years up to 30 June 2009.

9. However the Product Ruling only applies to the extent that:

- there is no change in the scheme or in the entity's involvement in the scheme;
- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

10. 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)).

11. 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.

12. 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).

Changes in the Law

13. Although this Product Ruling deals with the laws enacted at the time it was issued, later amendments to the law may impact on this Product Ruling. Any such changes will take precedence over the application of this Product Ruling and, to the extent of those amendments this Product Ruling will be superseded.

14. Entities who are considering participating in the scheme 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

15. 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 participants are fully informed of any legislative changes after the Product Ruling is issued.

Goods and Services Tax

16. All fees and expenditure referred to in this Product 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.

Ruling

Application of this Ruling

17. Subject to the stated qualifications, this part of the Product Ruling sets out in detail the taxation obligations and benefits for a Grower in the defined class of entities who enters into the scheme described at paragraphs 29 to 71 of this Ruling.

18. The Grower's participation in the Project must constitute the carrying on of business of a primary production. Provided the Project is carried out as described below, the Grower's business of primary production will commence at the time of execution of their Forestry Management Agreement and Timberlot Agreement.

The Simplified Tax System (STS)

Division 328

19. 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 was an 'STS taxpayer' prior to 1 July 2005 and 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*.

20. For these Growers only, 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

21. 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 and section 17-5

22. 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 fees for Initial Establishment Services, Planting Services, Borrowing Expenses, Interest and Rental Fees***Section 8-1, section 25-25 and Division 27 of the ITAA 1997 and section 82KZMG of the Income Tax Assessment Act 1936***

23. A Grower may claim tax deductions for the following fees and expenses on a per Timberlot basis, as set out in the Table below.

| Fee Type | Year ending 30 June 2007 | Year ending 30 June 2008 | Year ending 30 June 2009 |
|--|-------------------------------------|-------------------------------------|-------------------------------------|
| Initial Establishment Services | \$8,490 See Notes (i) & (ii) | | |
| Planting Services | \$840 See Notes (i) & (ii)) | | |
| Interest on loans with United Pacific Finance Pty Limited | As incurred See Note (iii) | As incurred See Note (iii) | As incurred See Note (iii) |
| Loan application fee | Must be calculated See Note (iv) | Must be calculated See Note (iv) | Must be calculated See Note (iv) |

Notes:

- (i) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (ii) Under section 82KZMG of the *Income Tax Assessment Act 1936* (ITAA 1936) the Initial Establishment Services and Planting Services Fees are expenditure for 'seasonally dependent agronomic activities' (see paragraphs 88 to 90 of this Ruling) and is deductible in the income year in which it is incurred.
- (iii) The deductibility or otherwise of interest arising from agreements entered into with financiers other than United Pacific Finance Pty Limited, is outside the scope of this Ruling. Prepayments of interest to any lender, including United Pacific Finance Pty Limited, are also not covered by this Product Ruling. Growers who enter into agreements with other financiers and/or prepay interest may request a private ruling on the deductibility of the interest incurred.

- (iv) The loan application fee payable to United Pacific Finance Pty Limited is a borrowing expense and is deductible under section 25-25. It is incurred for borrowing money that is used or is 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 United Pacific Finance Pty Limited 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

24. A Grower who is an individual accepted into the Project in the year ended 30 June 2007 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 Growers for the income years ended **30 June 2007 to 30 June 2032**. 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.

Prepayment provisions and anti-avoidance provisions

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

25. For a Grower who commences participation in the Project and incurs expenditure as required by Forestry Management Agreement and Timberlot Agreement, the following provisions of the ITAA 1936 have application as indicated:

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

Units in the Land Trust

Part 3-1 of the ITAA 1997 and Division 6 of Part III of the ITAA 1936

26. Growers may also acquire Units in the Land Trust. The Units are CGT Assets (section 108-5) and the amounts payable for the Units upon subscription constitute an outgoing of capital and are not allowable as a deduction.

27. The amount paid for each Unit will represent the first element of the cost base of the Units (subsection 110-25(2)). The disposal of the Units by the Unit Holder will be a CGT Event and may give rise to a capital gain or loss.

28. Distributions to the Unit Holder by the Trustee of the Land Trust may be income distributions that are included in the assessable income of a Grower who is a Unit holder in accordance with Division 6 of Part III of the ITAA 1936 or may be non assessable amounts that give rise to CGT Event E4 (section 104-70 of the ITAA 1997).

Scheme

29. The scheme that is the subject of this Ruling is identified and described in the following documents:

- Application for a Product Ruling considered valid on 11 August 2006 as constituted by documents provided on 31 July 2006, 10 August 2006, 11 August 2006, 5 September 2006, 17 October 2006, 19 October 2006, 24 October 2006, 30 October 2006, 6 November 2006 and 12 January 2007 and additional correspondence received from the Applicant dated 25 September 2006, 26 September 2006, 27 September 2006, 18 October 2006, 24 October 2006, 26 October 2006, 27 October 2006, 30 October 2006 and 6 November 2006;
- Draft Information Memorandum ('IM'), received on 17 October 2006;
- Draft **Constitution AgriWealth 31 March 2007 Radiata Pine Plantation Investment** received on 17 October 2006;
- Draft **Forestry Management Agreement** between Stanford Finance Australia Limited ('Stanford'), AgriWealth Pty Limited ('AgriWealth') and the Grower received on 12 January 2007;
- Draft Forestry Management Agreement between Stanford and AgriWealth received on 17 October 2006;
- Draft Agreement for Lease between Stanford and AgriWealth received on 17 October 2006;

- Draft Lease Agreement between Stanford and AgriWealth received on 12 December 2006;
- Forestry Management Contract AgriWealth 2006 Softwood Project ('Forests NSW Agreement') between AgriWealth and Forestry Commission of New South Wales dated 21 June 2006;
- Draft **Constitution for AgriWealth 31 March 2007 Radiata Pine Land Trust** received on 17 October 2006;
- Draft **Timberlot Agreement** between Stanford, AgriWealth and the Grower undated, received on 17 October 2006;
- Draft **Finance Facilities** documents from Stanford received on 17 October 2006; and
- Draft **Finance Facilities** documents from United Pacific Finance Pty Limited ('United') received on 10 August 2006.

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

30. The documents highlighted are those that a Grower/Investor 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/Investor, or any associate of a Grower/Investor, will be a party to, which are a part of the scheme. The effect of these agreements is summarised as follows.

31. 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

32. Following is a summary of the scheme:

| | |
|---|---|
| Location | Tumut, Tumbarumba region of NSW |
| Plantation Investment | |
| Type of business to be carried on by each participant | Commercial growing and cultivation of <i>Pinus radiata</i> trees for the purpose of harvesting and selling the timber |
| Number of hectares offered for cultivation | Approximately 200 hectares |

| | |
|---|--|
| Minimum Subscription | No minimum applies |
| Size of each Timberlot | 0.5 plantable hectare |
| Minimum allocation per Grower | 2 Timberlots |
| Number of trees per Timberlot | 500 <i>Pinus radiata</i> |
| Term of the Project | Approximately 26 years with an option to extend up to 5 years |
| Initial minimum Establishment Services Fee and Planting Services fee cost | \$18,660 for 2 Timberlots |
| Ongoing costs per Timberlot | Interim and Final Management Fees, Rent, Tree Insurance, Cost of harvesting and transporting timber, land rehabilitation |
| Land Trust Investment | |
| Minimum Subscription | No minimum applies |
| Minimum Trust Unit allocation per Unit Holder | 2 Units |
| Initial minimum cost | \$4,650 for 2 Units |
| Cost per Unit | \$2,325 |
| Ongoing costs | NIL |

The Project

33. Under the IM applicants are invited to participate in the AgriWealth 31 March 2007 Radiata Pine Project. Growers enter into a Forestry Management Agreement with Stanford as the Manager ('Manager'). The Manager operates in its role under its Australian Financial Services Licence number 226895.

34. Growers will enter into a Timberlot Agreement with AgriWealth as Grantor. Under the Timberlot Agreement Growers will be allocated a specific parcel of land which is evidenced by holding a Forestry Right Interest ('FRI').

35. The Forestry Commission of New South Wales ('Forests NSW') has been contracted to provide the silvicultural services over the life of the Project. Forests NSW is responsible for identifying suitable land, land preparation, planting, forest maintenance and harvesting.
36. A Timberlot is equivalent to a 0.5 plantable hectare. The initial cost per Timberlot is \$8,490 for Initial Establishment Services and \$840 for Planting Services. Growers must subscribe for a minimum of two (2) Timberlots.
37. There is no minimum subscription for this Project.
38. There will be 500 trees per Timberlot planted within 12 months from 1 June 2007. There is a guaranteed average survival rate of 425 trees per Timberlot across the plantation for the first 12 months after planting.
39. The allotment date is at the Manager's discretion but no later than 31 March 2007.
40. As well as entering a Forestry Investment Growers or other entities may choose to participate in an investment with the AgriWealth 31 March 2007 Radiata Pine Land Trust ('Land Trust') which has been established to be the ultimate owner of the plantation land. Under the IM applicants are invited to subscribe for Units in the Land Trust at a cost of \$2,325 per Unit with a minimum subscription of 2 Units. It is not compulsory for a Grower to subscribe for Units in the Land Trust.
41. This Ruling applies to Growers who acquire two or more Timberlots only or to those Growers who acquire two or more Timberlots and Units in the Land Trust. This Ruling does not apply for investors who do not acquire Timberlots.

Constitution AgriWealth 31 March 2007 Radiata Pine Plantation Investment ('Plantation Constitution')

42. The Plantation Constitution establishes the Project and operates as a deed binding on all of the Project's Growers (clause 1.3 of the Plantation Constitution). The Plantation Constitution sets out the terms and conditions under which Stanford agrees to act as Manager. Growers are bound by the Plantation Constitution by virtue of their participation in the Project. The Manager is required to establish and maintain a register of Growers (clause 16 of the Plantation Constitution).
43. Under the terms of the Plantation Constitution, until an application is accepted, all application money received is to be placed into a bank account in the name of the Manager and held in accordance with the requirements of the *Corporations Act 2001* (clause 2.5.1 of the Plantation Constitution). After acceptance the money is held by the Manager as an agent, for and on behalf of, each applicant (clause 2.5.2 of the Plantation Constitution).

44. In summary, the Plantation Constitution sets out provisions relating to:

- applications to be on the form attached to the IM (clause 2.1);
- appointment of the Manager as the Grower's irrevocable agent, representative and attorney to enter into the Grower's Timberlot Agreement and Management Agreement on behalf of the Grower (clause 3.6);
- the effect of an applicant's application being accepted by the Manager (clause 3.5);
- preparation and execution of the Timberlot Agreement and Forestry Management Agreement by the Manager and the Grantor (clause 3.5);
- the Manager's duties, powers and obligations (clause 9);
- the right of the Manager to be paid certain expenses (clause 22); and
- termination of the Scheme (clause 25.1).

Constitution AgriWealth 31 March 2007 Radiata Pine Land Trust ('Land Trust Constitution') (Optional)

45. A Grower or another entity may subscribe for Units in the Land Trust that will acquire the land on which the Project will be carried out.

46. The Land Trust will be an unregistered managed investment scheme under Chapter 5C of the Corporations Act. Stanford will act as the trustee for the Land Trust.

47. The subscription price for the Land Trust is \$2,325 per Unit and is payable on 2 April 2007.

Timberlot Agreement

48. An interest in the land will be provided to Growers via the Timberlot Agreement between the Grantor and the Grower. The provisions of the agreement are incidental to a FRI with the intent that all the provisions are forestry covenants within the meaning of section 87A of the *Conveyancing Act 1919* (NSW) (clause 1.1 of the Timberlot Agreement).

49. The Grantor is entitled to a Rental Fee equal to 11% of the net harvest proceeds to which the Grower is entitled from the Final Harvest (clause 3.2 of the Timberlot Agreement).

50. The Rental Fee will be calculated on the amount of any insurance proceeds received by the Grower in respect of a partial or total loss or destruction of the plantation produce on their Timberlot. The Rental Fee levied in relation to the insurance proceeds will be payable at the time the insurance proceeds are received.

51. Where no insurance proceeds are received by a Grower, in the event of a partial or total loss or destruction of the plantation produce, the Rental Fee will be calculated on the amount of Discounted Harvest Proceeds (to be assessed by an independent forester at the time of the loss or destruction).

52. The Grower must use the Timberlots only for approved purposes and must establish, maintain, manage and harvest the plantation in accordance with sound forestry practice (clause 6.1 of the Timberlot Agreement).

53. The Timberlot Agreement will grant the Grower the right to maintain, manage and harvest a crop of trees on the Timberlot (clause 5.1.1 of the Timberlot Agreement). The Grower may also construct roads, tracks, bridges and other facilities on the land with the written consent of the Landowner (clause 5.3 of the Timberlot Agreement). The Timberlot Agreement will give the Grower ownership of all trees on their Timberlots and all plantation produce from the land (clause 4.1 of the Timberlot Agreement).

54. The Grower must bear the harvesting costs (clause 9.6 of the Timberlot Agreement).

55. The Grower is responsible for rehabilitating the Timberlot following final harvest (clause 9.1 of the Timberlot Agreement).

56. The Grantor must not do anything on the Timberlots or on the adjacent land which would materially or adversely affect the plantation (clause 7.8 of the Timberlot Agreement).

Forestry Management Agreement

57. The Grower engages Stanford to act as Manager to perform forestry services in respect of the Timberlots. Growers are required to pay \$8,490 per Timberlot (\$16,980 per minimum investment) for Initial Establishment Services and will pay \$840 per Timberlot (\$1,680 per minimum investment) for Planting Services.

58. The Initial Establishment Services are for seasonally dependent agronomic activities to be conducted on or prior to 31 March 2008. The Services include (schedule 1 clause 24 of the Forestry Management Agreement):

- site preparation within the approved Code of Practice, comprising, ripping & mounding cultivation, where appropriate, control of competing vegetation and control of noxious weeds and animals; and
- provision of cuttings or seedlings equivalent to GF19+ wherever growing conditions are suitable or such other quality stock cuttings or seedlings approved by the Manager in accordance with the Plantation Establishment and Management Plan. Density of planting is to be consistent with the desired silvicultural outcome (usually 1,000 stems per hectare).

59. Planting Services are for seasonally dependent agronomic activities to be conducted between 1 June 2007 and 31 May 2008. Services include (schedule 1 clause 25 of the Forestry Management Agreement):

- planting GF19+ equivalent (or such other quality stock approved by the Manager) cuttings or seedlings in accordance with the Plantation Establishment and Management Plan; and
- application of fertiliser if considered necessary by the Manager, including the application of boron.

60. The Manager is appointed to market and deal with the plantation produce at each thinning and final harvest. Ongoing forestry services will be performed at all times prior to final harvest. Ongoing Services include (schedule 1 clause 26 of the Forestry Management Agreement):

- managing and maintaining the plantation;
- hazard reduction activities;
- quality control and internal audit of operations;
- assessments and reports on growth and performance as necessary;
- inventory assessments targeted at ages 1 or 2 years, at age 5 years where necessary, age 10 years and harvest;
- maintenance and repair of roads, firebreaks, gates and related infrastructure and fences;
- identification of fire prevention and risk reduction parameters; and
- rehabilitation of plantation land after final harvest.

61. Growers have appointed the Manager to act as their agent to market the plantation produce. Growers authorise the Manager to consolidate and mix the plantation produce of their Timberlot with that of other growers (clause 6.10.2 of the Forestry Management Agreement).

62. Growers are entitled to all the proceeds from sale of the plantation produce net of all costs of harvesting and transportation (clause 6.2 of the Forestry Management Agreement).

63. A Grower's share of produce will be calculated by reference to the size of the Grower's Timberlot land compared to the overall size of the plantation land of all Growers adjusted for any Grower who has suffered a loss or destruction of plantation produce on their Timberlots (clause 9 of the Forestry Management Agreement).

64. Growers who have suffered a loss or destruction of plantation produce will have their share of pooled plantation produce reduced by the pro rata amount of plantation produce lost or destroyed from their Timberlots (clause 9 of the Forestry Management Agreement).

Forests NSW Agreement

65. Forests NSW have been contracted to provide the silvicultural services for the term of the Project and to act as marketing agent for the Project.

Fees

66. The following fees, per **Timberlot**, are set out in the Forestry Management Agreement and Timberlot Agreement:

- \$8,490 for 'Initial Establishment Services' to be performed on or before 31 March 2008, payable on 2 April 2007;
- \$840 for 'Planting Services' to be performed during the period 1 June 2007 to 31 May 2008, payable on 29 June 2007;
- First Interim Management fee of 11% of the net harvest proceeds from the First Thinning, payable at the time of First Thinning, approximately year 13;
- Second Interim Management fee of 11% of the net harvest proceeds from the Second Thinning, payable at the time of Second Thinning, approximately year 20;
- Final Management fee of 11% of the net harvest proceeds from the Final Harvest or \$1,650 (adjusted for annual CPI movements) per Timberlot whichever is the greater, payable at the time of Final Harvest; and
- Rental Fee per Timberlot equal to 11% of net Final Harvest proceeds, payable at the time of Final Harvest.

Finance

67. Growers can fund their involvement in the Project themselves, by entering into a Terms Payment Agreement with Stanford, borrowing from United or by borrowing from an independent lender. Finance provided by United is on a full recourse basis and on arm's length commercial terms.

68. Details of the Terms Payment Agreement offered to Growers by Stanford are set out in the Finance Facility (AgriWealth 31 March 2007 Radiata Pine Project) documents. The Terms Payment Agreement is summarised as follows:

- Stanford will offer a terms payment option to Growers that are individuals for up to 100% of the Grower's Initial Establishment Services Fee and Planting Services Fee. Stanford will not offer a terms payment option to Growers that are companies or trustees. No terms payment option will be offered in relation to subscription for Units in the Land Trust;

- Stanford will pay stamp duty and registration fees in relation to the Terms Payment Agreement document;
- the Terms Payment Agreement is for a period of 1 year;
- no interest is payable pursuant to the Terms Payment Agreement;
- the amount is payable over 12 months from each due date by way of equal monthly instalments;
- Stanford may obtain security for the Terms Payment Agreement by a mortgage over the Grower's Timberlots.

69. Details of the loans offered to Growers by United are set out in the United Finance Facility (AgriWealth 31 March 2007 Radiata Pine Project) documents. The United documents are summarised as follows:

- United will lend up to 100% of the Grower's Initial Establishment Services Fee and Planting Services Fee and the cost of subscription for Units in the Land Trust;
- Growers will pay stamp duty and registration fees in relation to the document;
- Growers will pay a loan application fee of \$250 plus 0.5% of the amount borrowed to fund the Initial Establishment Services Fee and the Planting Services Fee up to a maximum of \$1,250;
- the 'Loan Terms' are for periods of 10 years, 12 years or 15 years;
- the loans attach a fixed interest rate with a current indicative interest rate of 10.5% per annum payable monthly in arrears (however under the 10 year loan facility interest may be charged at a variable rate);
- the 10 year and 12 year loans are repayable as to interest only during the first 3 years of the loans. Thereafter, the 10 year and 12 year loans are repayable over the remaining term of the loans by way of equal monthly repayments of principal and interest. Under the 10 year variable rate loan, a borrower can repay part or all of the outstanding loan balance without penalty at each 90 day interest reset date. An administration fee may apply should an early repayment be exercised;
- the 15 year loan is repayable over the term of the loan by way of equal monthly repayments of principal and interest;

- United will obtain security for the finance facilities by a mortgage over the Grower's Timberlots and/or Units in the Land Trust; and
- where the Grower/Unit Holder is a corporate borrower, unless otherwise advised by United, the directors of the entity will be required to personally guarantee the finance facilities.

70. Growers cannot rely on this Product Ruling if they enter into a finance agreement with United that materially differs from that set out in the information provided to the Tax Office with the application for this Product Ruling.

71. 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 schemes or other collateral agreements in relation to the loans 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 arrangement transform the Project into a 'scheme' to which Part IVA of the ITAA 1936 may apply;
- the loans or rates of interest are 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 United, are involved or become involved in the provision of finance to Growers for the Project.

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?

72. For the amounts set out in paragraph 23 of this Ruling to constitute allowable deductions the Grower's afforestation activities as a participant in the Agriwealth 31 March 2007 Radiata Pine Project must amount to the carrying on of a business of primary production.

73. Two Taxation Rulings are relevant in determining whether a Grower will be carrying on a business of primary production.

74. The general indicators used by the Courts are set out in Taxation Ruling TR 97/11 Income tax: am I carrying on a business of primary production?

75. Taxation Ruling TR 2000/8 Income tax: investment schemes, particularly paragraph 89, is more specific to arrangements such as the Agriwealth 31 March 2007 Radiata Pine Project. As Taxation Ruling TR 2000/8 sets out, the relevant principles have been established in court decisions such as *Commissioner of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

76. Having applied these principles to the arrangement set out above, a Grower in the Agriwealth 31 March 2007 Radiata Pine Project is accepted to be carrying on a business of growing and harvesting Radiata Pine for sale.

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. Changes to the STS rules apply from 1 July 2005. 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 the fees for Initial Establishment Services, Planting Services, and interest on loans with United Pacific Finance Pty Limited***Section 8-1***

79. The fees for Initial Establishment Services, Planting Services, and interest on loans with United Pacific Finance Pty Limited are deductible under section 8-1 (see paragraphs 43 and 44 of TR 2000/8). A 'non-income producing' purpose (see paragraphs 47 and 48 of TR 2000/8) is not identifiable in the arrangement and there is no capital component evident in the fees for Initial Establishment Services or Planting Services (see paragraphs 49 to 51 of TR 2000/8).

80. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply. Subject to the prepayment provisions (see paragraphs 83 to 90 of this Ruling) a deduction for these amounts can be claimed in the year in which they are incurred (Note: The meaning of incurred is explained in Taxation Ruling TR 97/7).

81. Some Growers may finance their participation in the Project through a Loan Agreement with United Pacific Finance Pty Limited. Applying the same principles as that used for the fees for Initial Establishment Services and Planting Services, interest incurred under such a loan has sufficient connection with the gaining of assessable income to be deductible under section 8-1.

82. Other than where the prepayment provisions apply (see paragraphs 83 to 90 of this Ruling), a Grower can claim a deduction for such interest in the year in which it is incurred.

Prepayment provisions***Sections 82KZL to 82KZMG***

83. 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 income year, then it is not expenditure to which the prepayment rules apply.

84. For this Project, the only prepayment provisions that are relevant are section 82KZL of the ITAA 1936 (an interpretive provision) and section 82KZMG of the ITAA 1936 (an operative provision). References to sections 82KZME and 82KZMF of the ITAA 1936 are made only in respect their interaction with section 82KZMG and to confirm that these provisions have no application to expenditure incurred by Growers who participate in the scheme set out in this Ruling.

Application of the prepayment provisions to this Project

Sections 82KZME and 82KZMF

85. Other than the fees for Initial Establishment Services and Planting Services (see below) the fees payable under the scheme to which this Product Ruling applies are payable out of harvest proceeds and the interest payable to United Pacific 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 expenditure incurred by Growers under this scheme.

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

87. As noted in the Ruling part above, Growers who prepay 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.

Section 82KZMG

88. Expenditure that meets the requirements of section 82KZMG of the ITAA 1936 is excluded from the application of the prepayment rules in sections 82KZME and 82KZMF of the ITAA 1936 that would otherwise apply. Section 82KZMG provides a '12 month rule' that, in effect, facilitates an immediate deduction for certain prepaid expenditure incurred under a plantation forestry managed agreement. The 12 month rule applies to expenditure for 'seasonally dependent agronomic activities' that will be carried out during the establishment period of a particular planting of trees. Seasonally dependent agronomic activities are explained in Taxation Determination TD 2003/12. Whilst the establishment period itself may exceed 12 months, each seasonally dependent agronomic activity must be completed within 12 months of commencement of its eligible service period (as defined in subsection 82KZL(1) of the ITAA 1936), and by the end of the following income year.

89. Under the Forestry Management Agreement each Grower incurs an Initial Establishment Services Fee of \$8,490 and a Planting Services Fee of \$840 per Timberlot for 'seasonally dependent agronomic activities' that will be carried out during the 'establishment period' of the Trees.

90. The expenditure for 'seasonally dependent agronomic activities' meets all other requirements of section 82KZMG and, therefore, a deduction is allowable in the income year ended 30 June 2007 for the full amount of expenditure incurred by the Grower for the Initial Establishment Services Fee and the Planting Services Fee.

Division 35 – deferral of losses from non-commercial business activities and the Commissioner's discretion

Sections 35-10 and 35-55

91. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for income years ending 30 June 2007 to 30 June 2032, the Commissioner has applied the principles set out in Taxation Ruling TR 2001/14 Income tax: Division 35 – non-commercial business losses. Accordingly, based on the evidence supplied, the Commissioner has determined that for those income years:

- it is because of its nature the business activity of a Grower will not satisfy one of the four tests in Division 35; and
- there is an objective expectation that within a period that is commercially viable for the afforestation industry, a Grower's business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

92. 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.

93. 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

94. 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 of the ITAA 1936. It will not apply to deny the deduction otherwise allowable under section 8-1 of the ITAA 1997.

Part IVA – general tax avoidance provisions

95. 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).

96. The Agriwealth 31 March 2007 Radiata Pine 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 23 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.

97. 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 timber. 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 97/7; TR 97/11; TR 98/22;
TR 2000/8; TR 2001/14;
TR 2002/6; TR 2002/11;
TD 2003/12

Subject references:

- advance deductions and expenses for certain forestry expenses
- carrying on a business
- commencement of a business
- fee expenses
- forestry agreement
- interest expenses
- management fees
- non-commercial losses
- producing assessable income
- product rulings
- public rulings
- seasonally dependent agronomic activities
- 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 82KZL(1)
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC

- ITAA 1936 82KZMD
- ITAA 1936 82KZME
- ITAA 1936 82KZMF
- ITAA 1936 82KZMG
- ITAA 1936 Pt III Div 6
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
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- ITAA 1997 35-10
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- ITAA 1997 Subdiv 61-J
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