



# ***PR 2007/53 - Income tax: Media Funds Management Pty Limited: Film Fund No. 2 of 2007 - 'The Last Stand'***

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 This document has changed over time. This is a consolidated version of the ruling which was published on *6 June 2007*



## Product Ruling

### Income tax: Media Funds Management Pty Limited: Film Fund No. 2 of 2007 – ‘The Last Stand’

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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**

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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**

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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

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1. This 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 1936* (ITAA 1936) unless otherwise indicated. In this Product Ruling this scheme is referred to as 'The Last Stand', 'the scheme', 'the Project' or simply as 'the Film'.

### 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. In this Product Ruling, those entities that can rely on the tax benefits set out in this Ruling are referred to as Investors.

3. The class of entities who can rely on those tax benefits consists of entities that are accepted to participate in the scheme specified below on or after the date this Product Ruling is made and which execute relevant Project Agreements mentioned in paragraph 29 of this Ruling on or before 30 June 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:

- 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 Product Ruling or after 30 June 2007;
- are not a wholesale client for the purposes of section 761G of the *Corporations Act 2001*;
- participate in the scheme through offers made other than through the Information Memorandum for the Film; or
- are non-residents of Australia for the purposes of the ITAA 1936 or the *Income Tax Assessment Act 1997* (ITAA 1997).

**Superannuation Industry (Supervision) Act 1993**

5. This Product Ruling does not address the provisions of the *Superannuation Industry (Supervision) Act 1993* (SISA 1993). The Tax Office gives no assurance that the product is an appropriate investment for a superannuation fund. The trustees of superannuation funds are advised that no consideration has been given in this Product Ruling as to whether investment in this product may contravene the provisions of SISA 1993.

**Qualifications**

6. 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 84 of this Ruling.

7. 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 Ruling may be withdrawn or modified.

8. This work is copyright. Apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to:

Commonwealth Copyright Administration  
Attorney General's Department  
Robert Garran Offices  
National Circuit  
Barton ACT 2600

or posted at: <http://www.ag.gov.au/cca>

**Date of effect**

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9. This Product Ruling applies prospectively from 6 June 2007, the date this Product Ruling is made. It therefore applies to the specified class of entities that enter into the scheme from 6 June 2007 until 30 June 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 up to 30 June 2009.

10. 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.

11. 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)).

12. 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.

13. 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

14. Although this Product Ruling deals with the laws enacted at the time it was issued, later amendments may impact on this Product Ruling. Any such changes will take precedence over the application of this Product Ruling and, to that extent, this Product Ruling will have no effect.

15. 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

16. 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

17. All amounts and percentages referred to in this Product Ruling exclude the Goods and Services Tax (GST), unless otherwise specified. The transactions in respect of this scheme will, where appropriate, ordinarily have GST implications. Those GST implications are outside the scope of this Product Ruling. Parties to this Product Ruling should seek independent advice in respect of GST. Parties to this Ruling can also submit an application for a private binding ruling from the Tax Office in respect of the application of the GST law to their particular circumstances.

## Ruling

### Division 10BA

18. A deduction is available to an Investor in the Film under Division 10BA of Part III (Division 10BA) for 93.5% of their Capital Contribution.

19. A deduction is not available unless each of the following occur on or before 30 June 2007:

- the production budget of \$12,950,000 has been achieved;
- each Investor's Investment Application Deed has been executed; and
- the Joint Venture Deed has been executed.

20. Upon completion of the Film, after the audit has been carried out by an independent auditor, Division 10BA deductions will be withdrawn from Investors to the extent that their investment moneys were spent on non-deductible expenses, in excess of those stated above (section 124ZAG).

### Sections 8-1 and 25-25 of the ITAA 1997 and section 124ZAO of the ITAA 1936

21. An Investor may claim tax deductions for the following fees and expenses in relation to their Film investment as set out in the Table below.

Fee Type	Year ending 30 June 2007	Year ending 30 June 2008	Year ending 30 June 2009
<b>Management Fee</b>	Nil See Notes (i) & (ii)	Nil See Notes (i) & (ii)	Subject to Film income See Notes (i) & (ii)
<b>Annual Management Fee</b>	Nil See Notes (i) & (ii)	Nil See Notes (i) & (ii)	Subject to Film income See Notes (i) & (ii)
<b>Interest on funds borrowed from United</b>	Nil See Notes (i), (ii) & (iii)	Nil See Notes (i), (ii) & (iii)	Subject to Film income See Notes (i) & (ii)
<b>Establishment Fee paid to United</b>	Nil See Notes (i) & (iv)	Nil See Notes (i) & (iv)	Subject to Film income See Notes (i) & (iv)

**Notes:**

- (i) With the exception of deductions claimable under Division 10BA, section 124ZAO will operate to limit the amount of any deduction otherwise allowable in relation to the Film and in gaining or producing assessable income to which section 26AG relates. The deduction allowable in a year of income will be limited to the amount of film income which is derived from the Film (subsection 124ZAO(2)) in that year. Any excess deductions may be carried forward indefinitely and offset against future income from the Film (subsection 124ZAO(3)). Section 124ZAO will apply in relation to deductions in respect of the Management Fee, the Annual Management Fee, any interest on finance obtained from United Pacific Finance Pty Ltd (United) and the United loan Establishment Fee.
- (ii) Subject to section 124ZAO of the ITAA 1936, the Management Fee, the Annual Management Fee and any interest on finance obtained from United, are deductible in terms of section 8-1 of the ITAA 1997.
- (iii) The deductibility or otherwise of interest arising from agreements entered into with financiers other than United is outside the scope of this Ruling. Prepayments of interest to any lender, including United, are not covered by this Product Ruling. Investors who enter into agreements with other financiers and/or prepay interest may request a private ruling on the deductibility of the interest incurred.
- (iv) Subject to section 124ZAO of the ITAA 1936, the Establishment Fee of \$1,375 payable to United is a borrowing expense and is deductible under section 25-25 of the ITAA 1997. 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 is outside the scope of this Ruling.

**Partnership and section 26AG**

22. For the year ending 30 June 2007 and subsequent years of income, Investors who initially acquire 100% of the Copyright in the Film will comprise a tax law partnership for the purposes of Division 5 of Part III of the ITAA 1936 (see definition of 'partnership' in section 995-1 of the ITAA 1997). All amounts received by the Partnership as consideration for the use of, or the right to use, the Investors' Copyright interests are assessable income of the Partnership under section 26AG in the income year in which they are received. The partners will receive income jointly from the commercial exploitation of their Copyright interest in the Film. However, pursuant to subsection 26AG(9) of the ITAA 1936, any income received by a Partnership from the use of, or the right to use, the Copyright is taken to have been derived by the partners. No such income is taken into account for the purposes of calculating the net income or loss of the Partnership of any year of income and, if this is the only income derived by the Partnership, it will not be necessary to lodge partnership income tax returns. Any income derived will be taken to be the income of each Investor in proportion to their share in the partnership.

23. Consideration receivable by an Investor in a Film, from the disposal of the Investor's Copyright interest in the Film, will be assessable income of the Investor in the income year in which the Copyright interest is disposed of and will be an amount equal to the specified price, or the amount determined by the Commissioner where there is no specified price (paragraph 26AG(1)(e) and subsection 26AG(3)).

**Division 35**

24. Division 35 of the ITAA 1997 will not apply to defer the deductions otherwise allowable.

**Section 79D**

25. Section 79D does not apply to deny or defer the deductions otherwise allowable.

**Section 82KL**

26. Section 82KL will not be applied to deny deductions otherwise allowable.

**Part IVA**

27. Part IVA will not apply to deny deductibility or to accelerate assessability of the above amounts.



## Assumptions

28. This Ruling is made subject to the following assumptions:

- (a) the Investor was a resident of Australia for tax purposes at the time the money was expended (subparagraph 124ZAFA(1)(b)(i));
- (b) the investment moneys will be paid to the Production Company by way of contribution to the cost of producing the Film under a contract entered into on or before the end of the financial year in which the capital moneys are to be expended by the Division 10BA Investor, being 30 June 2007. The production contract will specify that the investment moneys contributed represent the estimated cost of production of the Film (paragraph 124ZAFA(1)(a) and subparagraph 124ZAFA(1)(d)(iv));
- (c) at the relevant time, a provisional certificate (section 124ZAB) or a final certificate (section 124ZAC) is in force in relation to the Film;
- (d) each Investor, at the relevant time, expects to become one of the first owners of the Copyright in the Film when the Copyright comes into existence (subparagraph 124ZAFA(1)(c)(i));
- (e) each Investor, at the relevant time, intends to use the interest in the Copyright for the purpose of producing assessable income from the exhibition of the Film as mentioned in subparagraph 124ZAFA(1)(c)(ii);
- (f) there will be in force a declaration lodged in respect of the Film in accordance with subsection 124ZADA(1) by a person accepted by the Commissioner under subsection 124ZADA(2) as an appropriate person to make such a declaration (subparagraph 124ZAFA(1)(d)(iii));
- (g) before the expiration of six months after the time when the Film is completed, an application will be made for a final certificate in accordance with section 124ZAC, otherwise the provisional certificate shall be deemed never to have been in force (subsection 124ZAB(10));
- (h) all requirements of the Department of Communications, Information Technology and the Arts will be met and a final certificate will be issued;
- (i) the Film will be completed and the Investors' interest in the Copyright in the Film will be used for income producing purposes within two years after the close of the financial year in which the contributions are made (subsection 124ZAFA(2));

- (j) by reason of the said capital moneys being expended, the Investor will become one of the first owners of the Copyright in the Film before 1 July 2009;
- (k) in producing the Film:
- where an amount is expended by a person (the Film producer) for the supply of goods or the provision of services; and
  - the Commissioner is satisfied that the Film producer and the person supplying the goods or providing the services are not dealing with each other at arm's length in relation to the transaction,
- that the amount of moneys expended on the supply of those goods or the provision of those services will not exceed the amount of moneys that would have been expended by the Film producer if the Film producer and the person supplying the goods or providing the services had dealt with each other at arm's length (section 124ZAJ);
- (l) at the time the Investor expends the capital moneys by way of contribution to the cost of producing the Film, the Investor is at risk, according to the definition of 'risk' in subsection 124ZAM(2), with respect to an amount equal to or greater than the amount of those capital moneys expended (subsection 124ZAM(1));
- (m) no pre-sale arrangements, distribution rights agreements, distribution guarantee agreements, or other like agreements, have been, or will be, entered into in circumstances where such agreements would put funds into the hands of the Investors, by loan or otherwise, to enable them to expend capital moneys by way of contribution to the cost of producing the Film;
- (n) in the event of any Underage, the Production Company will expend the Underage in a manner that will preserve the status of the Film as a 'Qualifying Australian Film'; and
- (o) the dominant purpose of the Investors is to make a commercial return from their investment in the Film and the arrangements will be executed in the manner described in this Ruling.

## Scheme

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29. The scheme is the Media Funds Management Pty Limited: Film Fund No. 2 of 2007 –‘The Last Stand’ and is described below. This scheme incorporates the following documents:

- Application for a Product Ruling lodged on 21 March 2007, and accepted as valid on 27 March 2007, as constituted by documents provided on 21 and 27 March 2007, 18 April 2007, 7, 14, 21 and 23 May 2007 and additional correspondence dated 21 and 27 March 2007, 18, 19 April 2007, 7, 14, 21, 22 and 23 May 2007;
- Correspondence from the Tax Office to the Applicant 15, 22 and 27, March 2007 and 4 April 2007;
- **Draft Investment Application Deed** for Media Funds Management Pty Limited Film Fund No. 2 of 2007 between Media Funds Management Pty Limited (Manager), the Investor and the Custodian received on 7 May 2007;
- **Draft Joint Venture Deed** for Media Funds Management Pty Limited Film Fund No. 2 of 2007 between Media Funds Management Pty Limited (Manager), the Investors and the Custodian received on 23 May 2007;
- Draft Deed of Assignment for The Last Stand between Cinema Partners Production Pty Limited (Assignor), and Media Funds Management Pty Limited (Assignee) and Production Company received on 23 May 2007;
- Draft Head Distribution Agreement for Film Fund No. 2 between Media Funds Management Pty Limited (Manager) and Screen Corporation Pty Limited (Head Distributor) received on 21 May 2007;
- Draft Information Memorandum for Film Fund No. 2 received on 17 May 2007;
- **Term Loan Finance Agreement and Finance Application Form** between United Pacific Finance Pty Ltd (Lender), the Borrower and the Guarantor received with the Application for a Product Ruling received on 21 March 2007;
- **Investment Loan Schedule** involving United Pacific Finance Pty Ltd received with the Application for a Product Ruling received on 21 March 2007;
- Draft Standard Collection Account Management Agreement between the Collection Account Manager (CAM), Producer, Sales Agent, Investors, Talent and Completion Guarantor received with the Application for a Product Ruling received on 21 March 2007;

- Draft Completion Guaranty Agreement between the Beneficiary and the Guarantor received with the Application for a Product Ruling received on 21 March 2007; and
- Provisional Certificate number P06853 dated 7 October 2004 issued by the Department of Communications, Information Technology and the Arts (DCITA) in relation to The Last Stand.

**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 include those that Investors 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 an Investor, or any associate of an Investor, will be a party to, which are a part of the scheme. In this Ruling the term 'associate' has the meaning given by section 318.

31. In accordance with the above documents, an Investor who participates in the scheme must be a wholesale client. This Ruling does not apply unless the Investor is a wholesale client for the **purposes of section 761G of the Corporations Act**. The meaning of wholesale client is explained in the Information Memorandum for this Project.

32. All Australian Securities and Investment Commission (ASIC) requirements are, or will be, complied with for the term of the agreements.

### **The Participants**

33. The entities involved in the scheme are:

- **Manager:** Media Funds Management Pty Limited (MFM) is conducting a scheme under which Investors are selected to participate and invest in the Joint Venture to fund the production and exploitation of the film 'The Last Stand'.
- **Investor:** a person who directly expends capital monies on the funding of the production of the Film and as a consequence becomes one of the first owners of copyright of and associated rights in the Film and who is accepted by the Manager into the Fund and enters into the following documents:
  - an Investor Application Deed (IAD);
  - Joint Venture Deed (JVD); and

- Term Loan Finance Agreement, where an Investor elects to obtain finance from United Pacific Finance Pty Ltd.
- **Custodian:** KPMG will be appointed as Custodian to deal with and account for the Fund Investment strictly in accordance with the terms and conditions of the IAD and JVD.
- **Production Company:** MFM is the producer of the Film and will engage third party production personnel as required.
- **Head Distributor:** Screen Corporation Pty Limited (SCP) is the Head Distributor and will subsequently enter into sub-distribution arrangements for the worldwide exhibition, distribution and marketing of the film for the term of the Head Distribution Agreement (HDA).
- **Collection Account Manager:** the CAM will:
  - open the collection account;
  - pay Gross Receipts and collection account Interest into the account;
  - calculate and pay entitlements; and
  - provide statements to the parties to the standard collection account management agreement.
- **Completion Guarantor:** the Completion Guarantor guarantees to complete and deliver the Film and agrees to provide completion funds to complete and deliver the Film, if MFM fails to do so.

## Defined terms

34. Terms which have been defined within the relevant documents to the scheme include the following:

- **'Budget'** means the estimate of cost of production of the Film comprising Item 1 Schedule 6 of the JVD.
- **'Capital Contribution'** means in respect of a Joint Venture the total sum comprising the total amount to be invested by the Investor into the Joint Venture.
- **'Capital Proportion'** means the proportion of the Capital Contribution that each individual or single Investor has in the Joint Venture relative to, the total of all of the Investors' Capital Contributions in the Joint Venture.

- **'Copyright'** means:
  - (a) the copyright and all the rights in the nature of copyright as recognised now or in the future for the purposes of the Copyright Act;
  - (b) copyright whether existing now or in the future under the law of any country other than Australia; and
  - (c) rights wheresoever arising in the nature of and analogous to the rights in (a) and (b).
- **'Copyright Act'** means the *Copyright Act 1968*.
- **'Custodial Bank Account'** means the segregated bank account held by the Custodian for the purpose of his holding the Fund Investment (the details of the account being set forth in the Investment Application Deed).
- **'Delivery'** means delivery to and acceptance by the Manager of the Film and Delivery Material on or before the Delivery Date.
- **'Delivery Date'** means the date identified in Schedule 5 of the JVD or such later date as is otherwise agreed by the parties, but being in no case a date after 30 June 2009.
- **'Delivery Material'** means the materials identified at Schedule 2 of the JVD in respect of the Film, together with all other physical materials acquired created or otherwise arising in respect of the Film by or on behalf of the Manager whether under a Production Contract or otherwise.
- **'Event of Default'** means any of the following events in respect of the Manager:
  - (a) its breach of any material term of the JVD, and failure to remedy it within 28 days of receipt by it of written notice from the Manager to so do other than any breach of Clause 63 of the JVD;
  - (b) its failure to comply with clause 63 of the JVD;
  - (c) appointment of a receiver and manager, controller, administrator, trustee or similar officer in respect of all of any part of its business;
  - (d) it being unable to pay its debts as and when they fall due, or being deemed unable so to do under any applicable legislation (except where the failure to pay is in respect of a debt or claim the subject of dispute);

- (e) entry into or resolution by it to enter any arrangement, composition or compromise with or assignment for the benefit of its creditors generally or any class of its creditors or the commencement of proceedings to sanction any such arrangement, composition or compromise (being other than for reconstruction or amalgamation on terms approved by the Manager); and
  - (f) failure to complete and deliver the Film by the Delivery Date or within the period of any extension thereof granted by the Manager.
- **'Film'** means the film or motion picture to be delivered by the Manager in accordance with the JVD having the working title and particulars identified at Schedule 4 of the JVD based on the Screenplay, and where the context so admits shall include all literary, dramatic, artistic and musical material incorporated therein synchronised therewith or otherwise forming part thereof, but shall exclude the original master negative of the film or motion picture.
- **'Film Production Account'** means a bank account of the Manager to be established in respect of its production of the Film.
- **'Film Project'** means a film or motion picture that satisfies the Manager of its artistic and commercial appeal and as such may then be the subject of a Joint Venture.
- **'Final Certificate'** means a certificate issued pursuant to Division 10BA.
- **'Fund'** means the Fund comprising the selection of Investors by the Manager to invest and participate by way of contributing funds for the production and exploitation of individual feature films, as an unincorporated joint venture, established by the Manager pursuant to a power of attorney provided to the Manager by the Investors by executing the IAD.
- **'Fund Close'** means Friday 30 June 2007 at 10.00pm EST.
- **'Fund Investment'** means the amount the Investor deposits with the Custodian as Identified in Item 2 Schedule 1 of the IAD.
- **'Head Distributor'** means as defined in the HDA.

- **‘Head Distribution Agreement’** means the agreement in Schedule 7 of the JVD duly completed by the Manager in accordance with the authority given to him by the Investor under Clause 16 of the IAD and given to him in similar terms by the other Investors selected for that Joint Venture under the Fund.
- **‘Intellectual Property’** means all present and future rights conferred by statute, common law, equity or any corresponding law in or in relation to copyright, trade marks, designs, patents, business and domain names, performances, confidential information and other results of intellectual activity in the literary, artistic, commercial, industrial or scientific fields whether or not registrable or registered including all rights in the nature of these rights such as Moral Rights.
- **‘Investors’** means those participating in the Fund by making a Fund Investment.
- **‘Investor Majority’** means the majority of the votes cast by Investors who are present at any meeting of the Investors which constitutes a quorum pursuant to Clause 30 of the JVD.
- **‘Joint Venture’** means the Investors selected by the Manager to fund and exploit the Film Project pursuant to the JVD, each of them acting in his own right severally and not in partnership or association with the others (except insofar as deemed to be a partnership by and for the purposes of the ITAA 1936).
- **‘Joint Venture Deed’** means the deed duly completed by the Manager in accordance with the authority given to him by the Investor under Clause 16 of the IAD and given to him in similar terms by the other Investors selected for that Joint Venture under the Fund. The Deed is titled, ‘Film Fund No. 2 of 2007 Joint Venture Deed’.
- **‘Letter of Credit’** means the perfected security interest validly issued by a bank approved by the Manager to secure payment of the Minimum Guarantee Amount (MGA).
- **‘Manager’** means Media Funds Management Pty Limited as the party appointed by the Investors under the document titled ‘Film Fund No. 2 of 2007 Joint Venture Deed’ to manage the conduct of the Joint Venture.
- **‘Maximum Fund Subscriptions’** means Fund Investments received in respect of the Fund for the sum required to completely fund a Film Project.



- **'Minimum Fund Subscriptions'** means Fund Investments received in respect of the Fund in the sum of \$12,950,000.
- **'Minimum Guarantee Amount'** means the amount payable to investors as set forth in item 2 of Schedule 7 of the HDA.
- **'Moral Rights'** means all present and future rights of integrity of authorship, rights of attribution of authorship, rights not to have authorship falsely attributed and rights of a similar nature that exist or may come to exist anywhere in the world in the Film or in any Underlying Materials.
- **'Outside Date'** means the date 9 months and one day after the date of the HDA.
- **'Overage'** means any amount in excess of the Budget required to complete the Film which is expended by or on behalf of the Manager in respect thereof.
- **'Production Contract'** means an agreement entered into by the Manager with a Third Party Producer in respect of the production of the Film or any aspect thereof.
- **'Production Schedule'** means the schedule for production of the Film comprising Item 2 of Schedule 6 of the JVD.
- **'Provisional Certificate'** means a certificate issued provisionally or otherwise subject to conditions pursuant to Division 10BA.
- **'Qualifying Australian Film'** means a qualifying Australian Film as defined in the ITAA 1936.
- **'Screenplay'** means the original Screenplay for the Film together with any alterations or changes approved by the Manager from time to time and where the context so permits or requires including references to part or parts only of the Screenplay.
- **'Specification'** means the specification in respect of the Film comprising Item 3 of Schedule 6 of the JVD.
- **'Third Party Producer'** means a producer engaged by the Manager to make the Film or any aspect thereof.
- **'Underage'** means any amount less than the Budget required to complete the Film which amount then must be expended on enhancing the film other than an amount of 5% of the underage, which is retained in the Film Production Account by or on behalf of the Manager in respect thereof as a performance fee payable to the Manager.

- **'Underlying Materials'** means the literary, dramatic, artistic and musical and any other underlying materials:
  - (a) in which Copyright may subsist and that are incorporated or proposed to be incorporated in the Film; or
  - (b) on which the Film may in whole or in part be based or adapted including the Screenplay.
- **'Warranties'** means the warranties of the Manager set out in Schedule 1 of the JVD.

### Overview

35. MFM is seeking to raise investment funds to be applied to the production of a qualifying Australian film 'The Last Stand'.
36. Provisional Certificate number P06853 dated 7 October 2004, updated by letters dated 28 February 2007, 15 and 20 March 2007 and 30 April 2007, is currently in force in respect of the Film and states that the proposed Film will, when completed, be a 'Qualifying Australian Film' for the purposes of Division 10BA.
37. The total budgeted cost of the Film is \$12,950,000 which comprises direct production costs of \$12,109,000 and non-deductible expenses of \$841,000. The maximum funds to be raised total \$12,950,000 and the Capital Contribution (CC) required from Investors will be the same as the maximum funds to be raised and contributed on formation of the Joint Venture. Approximately 93.5% of an Investor's CC will be an amount contributed toward the direct production costs of the Film.
38. Investors will be invited to contribute funds to invest in the Fund and will pay an amount known as the Fund Investment to the Custodian to be held in the Custodial Bank Account. Upon execution of the JVD the Custodian will withdraw the Fund Investment from the Custodial Bank Account and transfer it to the Film Production Account for the Joint Venture. The amount transferred to the Film Production Account is known as the Investor's CC.
39. Investors will obtain a 100% interest in the Copyright of and associated rights in the Film. After five years and six months (31 December 2012) SCP has the option (the 'Buyout Option') to acquire the Copyright interest and associated rights from Investors for an amount equal to 20% of the Budget of the Film or its fair market value at that time, whichever is the greater.
40. In addition to being the Manager of the scheme, MFM will also be the Production Company and will engage third party producers to produce the Film. SCP is contracted to act as the Head Distributor of the Film and may enter into license agreements with unrelated sub-licensee's who will be responsible for the distribution of the Film throughout the whole universe.

41. Under the scheme, Investors will be entitled to all receipts of the Joint Venture, being the Adjusted Gross Participation, as defined in the HDA, less any expenses and fees of the Joint Venture. In addition, subject to SCP obtaining a letter of credit by the Outside Date, Investors will be entitled to receive a MGA under the HDA equal to 30% of the Film Budget on 31 December 2012.

## **Obtaining Investor Funds**

42. Applications for investment will only be accepted from an Investor who is a wholesale client as defined in section 761G of the Corporations Act (refer to the Information Memorandum).

43. On entering the Project the Investors will enter into a number of agreements as detailed below.

## **Investor Application Deed**

44. Under the IAD the Investor appoints the Custodian to deal with their investment strictly in accordance with the terms and conditions of the IAD.

45. An Investor will be required to make the Fund Investment at the time of entering into the IAD. The Fund Investment will be held by the Custodian in the Custodial Bank Account pending acceptance into the scheme. Acceptance is considered to be the time that the Investor forms a Joint Venture with other Investors. The minimum Fund Investment is \$55,000 (GST inclusive) and thereafter in multiples of \$27,500 (GST inclusive).

46. Upon execution and delivery of the JVD by the Manager as attorney for the Investor, the Custodian shall withdraw the Fund Investment from the Custodial Bank Account and transfer the same to the Film Production Account for the Joint Venture and such account shall be maintained and operated by the Manager.

47. The Investor irrevocably appoints the Manager to complete the following documents or agreements in a form approved by the Manager and for the purpose of their execution and delivery at any time and in any order, on or after the date of the IAD:

- JVD;
- HDA; and
- other documents listed at clauses 16.1.3 to 16.1.7.

48. The Manager shall allocate the Investor to invest in a Joint Venture which contributes funds for the production and exploitation of the Film by executing the JVD on the Investor's behalf. The Manager shall only allocate the Investor to the production and exploitation of the Film where the Fund Investment is equal to the Budget of the Film.

**Joint Venture Deed**

49. An Investor is accepted into the Fund when they form a Joint Venture with other Investors for the purpose of producing the Film. The Joint Venture is created on the date of execution of the JVD.

50. The purpose of the Joint Venture is to contribute funds for the production of the Film up to the full amount of the Budget, to exploit the Film as first owners of 100% of the copyright therein, and to distribute the proceeds received from its exploitation.

51. The Manager acknowledges that all Copyright and other Intellectual Property rights in the Underlying Materials in the proposed Film (including all underlying literary, dramatic, artistic or musical works that are incorporated into, synchronized with or otherwise form part of the Film or Screenplay) will be assigned to the Manager under a deed of assignment between the owner of the rights and the Manager in consideration of payment from the Budget, to enable the vesting of all Copyright in the final Film, to the Investors.

52. Pursuant to the JVD, each Investor will:

- (a) have an interest in the Copyright as tenant in common equal to their Capital Proportion; and
- (b) subject to any security as contemplated by clause 5, be entitled to deal with its interest in the Copyright in its absolute discretion including, without limitation, dispose of, or otherwise create an interest in the Copyright without the consent of any other party to the JVD.

53. The capital of the Joint Venture shall be contributed by the Investors in the amounts identified in Schedule 8. Such sum shall not exceed for each Investor the sum available for release by the Custodian from that Investor's Fund Investment held in the Custodial Bank Account on behalf of the Investor. The Investors each direct the Custodian to release the said amounts from the Custodial Bank Account and pay the same to the Film Production Account on the date of execution of the JVD.

54. The Joint Venture shall continue for an indefinite period being no less than until 31 December 2012, unless the Joint Venture is terminated by Investor Majority where an Event of Default has occurred in accordance with clause 63. At any time after expiry of the said period or if the aforesaid termination occurs, the Investors may by Investor Majority wind up the Joint Venture.

55. In consideration of the payment of the Budget to the Manager, the Investors agree that the Manager will produce the Film for the cost specified in the Budget. The Manager will hold the funds in the Production Account to expend and disburse same in accordance with the terms of the JVD. The funds held in the Production Account must be expended and disbursed strictly in accordance with the Budget.

56. The Manager will be responsible for any monies expended by the Manager or on the Manager's behalf in connection with the production of the Film in excess of the Budget unless such Overage is approved in advance by the Investors in writing. Where approval is granted by Investors the Investors shall be responsible for the payment of the amount approved. Any Underage that is not expended on enhancing the film is to the sole and exclusive benefit of the Manager to the extent of the performance fee of 5% and dealt with or payable to the Manager as the Manager deems fit.

57. The Manager will enter the HDA on behalf of the Investors and must do all things of every kind reasonably required to enable the completion and delivery of the Film to the Head Distributor in accordance with the terms of the HDA.

58. The Manager on behalf of the Joint Venture shall allocate and distribute to each Investor in proportion to each Investor's CC all receipts, less any expenses and fees of the Joint Venture determined pursuant to clause 14. The date of such distribution shall be no later than 30 days after the end of the financial year in which the receipts are received by the Joint Venture.

59. The following fees are payable by the Investors under the Agreement:

<b>Fee</b>	<b>Amount</b>
Management Fee payable from Adjusted Gross Participation	(a) 8% until the Investors have recouped 100% of their CC, thereafter (b) 10% until the Investors have recouped 150% of their CC, thereafter (c) 15% until the Investors have recouped 200% of their CC, thereafter (d) 20%.
Management Fee payable annually from Exploitation Revenues (as defined in clause 14.3)	1.36% per annum of the Value of Assets Under Management (as defined in clause 14.4) within the Fund.

### **Head Distribution Agreement**

60. Under the HDA, the Manager on behalf of the Investors', licenses to SCP solely, exclusively and irrevocably, the right to exploit the Film and to grant licenses to others to exploit the Film.

61. As full and complete consideration for all rights granted to it, SCP must pay to the Manager, on behalf of the Investors, during the term of the HDA, 100% of the amount of the Adjusted Gross Participation (as defined in Schedule 8) of the Film until:

- (i) the amount of the Adjusted Gross Participation paid to the Manager exceeds the Budget of the Picture;
- (ii) thereafter, 95% of the amount of the Adjusted Gross Participation until the amount of the Adjusted Gross Participation paid to the Manager exceeds 150% of the Budget of the Picture;
- (iii) thereafter, 90% of the amount of the Adjusted Gross Participation until the amount of the Adjusted Gross Participation paid to the Manager exceeds 200% of the Budget of the Picture; and
- (iv) thereafter, 85% of the amount of the Adjusted Gross Participation in perpetuity.

62. The term of the HDA is the period from the date of the HDA until 25 years from the first theatrical release of the Film, subject to the Buyout Option at paragraph 67 of this Ruling.

63. The completed Film will be delivered to SCP as set forth in the Delivery Schedule (Schedule 4) at the Head Distributor's sole cost and expense, on or before the Delivery Date (Schedule 5).

64. In addition to a share of Adjusted Gross Participation outlined in paragraph 61 of this Ruling, Investors are entitled to receive the MGA set forth in Item 2 of Schedule 7. The amount of the MGA equates to 30% of the Film Budget. The MGA is payable on 31 December 2012. SCP is required to secure payment of the MGA by obtaining for the benefit of Investors an irrevocable and validly issued Letter of Credit (LofC) from a bank approved by the Manager.

65. SCP must obtain the LofC by the Outside Date. In the event that the LofC has not been issued by the Outside Date the HDA is terminated (clause 15.1) and no MGA will be payable by SCP. The termination of the HDA because the LofC is not in place by the Outside Date will not stop the production of the film. Should the HDA be terminated the Manager will continue to produce the Film and will seek to establish new distribution arrangements that may not include the payment of a MGA.

66. For avoidance of doubt, the Investors have no entitlement to call on the LofC where the Film has not been delivered to SCP as required by the HDA.

67. At any time from 31 December 2012 and within six calendar months from that date (the 'Option Period'), SCP shall have the sole and exclusive right (the 'Buyout Option') to buyout the Copyright and all other right, title and interest of the Manager, in its capacity as representative of the Investors, in and to the Film for a term commencing upon the date on which the Manager receives notice in writing from the SCP (the 'Buyout Notice') and continuing thereafter in perpetuity (the 'Buyout Rights'). The Head Distributor shall exercise the Buyout Option by giving the Buyout Notice. Upon receipt by the Manager of the Buyout Notice during the Option Period, the Buyout Rights will be assigned to the Head Distributor effective immediately. SCP shall pay the Manager, in its capacity as representative of the Investors, the Buyout Price to secure the Buyout Rights.

68. The Buyout Price shall be the fair market value of the Buyout Rights or 20% of the Budget of the Film, whichever is the greater.

69. The Buyout Price shall be set off against and earned solely out of what, but for exercise of the Buyout Option, would be the Adjusted Gross Participation. It shall be payable as and when the Adjusted Gross Participation would, but for exercise of the Buyout Option, have been payable. The Buyout Price may be less than that stated in paragraph 68 of this Ruling where the Adjusted Gross Participation earned following exercise of the Buyout Option, is less than the market value of the Buyout Rights or 20% of the Budget of the Film, as the case may be.

70. The obligations of the parties under the HDA are subject to the satisfaction of all of the following conditions precedent (clause 2):

- (i) each party's receipt of copies of the HDA, executed by the other party; and
- (ii) the Manager acknowledging and providing the right of SCP to enter into collection or licensing arrangements with other parties to fulfil all or any of the obligations of SCP to the Manager under Clause 11.

## **Deed of Assignment**

71. In consideration of the payment by Cinema Partners Productions Pty Limited (CPP) to MFM of the Assignment Amount (as defined in clause 1.1) CPP irrevocably transfers and assigns with full title guarantee by way of assignment 100% of its right title and interest, including present and future Copyright and other Intellectual Property rights, in and to the Rights and the Physical Materials for the whole period of the existence of the rights to MFM.

**Completion Guaranty**

72. The Guarantor guarantees to cause the Completion and Delivery of the Film (as defined in clause 3) in accordance with the terms of the Guarantee and the delivery (or provision of access) to the Recipients (being the persons to whom the Delivery Items are required to be delivered) of applicable Delivery Items (as listed in Schedule B) no later than the Delivery Date (as listed in Schedule B).

73. The Guarantor's obligations, which are listed specifically at clause 4, are subject to:

- (a) the payment to the Guarantor of the Fee (as stated at Schedule A); and
- (b) deposit into the Production Account (or paid directly and irrevocably to third parties, with Guarantor's written consent) of each instalment of the cost of producing the Film in accordance with the Budget as and when required to meet the production requirements and costs of the Film in accordance with the Cash Flow Schedule (as defined in clause 1.1).

**Standard Collection Account Management Agreement**

74. MFM will enter into a Collection Account Management Agreement (CAM Agreement) with an independent third party who is in the business of providing collection account management services. The CAM Agreement will be negotiated on an arms length basis, be based on standard film industry practice and will not differ materially in its terms and effect from the standard CAM Agreement provided as part of the ruling application.

75. The Parties to the CAM Agreement, excluding the CAM, jointly appoint the CAM during the Term of the CAM Agreement to:

- act as their sole and exclusive agent;
- open the Collection Account;
- calculate the entitlement(s);
- provide statements to the parties; and
- carry out the payment of entitlement(s) to each of the Beneficiaries in accordance with the terms and conditions of the Agreement.

76. Any licensee and any sublicensees will undertake to insert into any licence, sublicense or distribution agreements irrevocable instructions that Gross Receipts received from distribution of the Film will be deposited into the Collection Account.

77. The CAM will provide to the parties to the agreement a statement specifying the source of Gross Receipts, the amount of the Collection Account interest and the allocation of those Collected Gross Receipts to the beneficiaries of the Collection Account.



78. The CAM shall pay out entitlements from the Collection Account to the beneficiaries within ten working days of the issue of the Statement.

## Finance

79. Investors can fund their involvement in the Film themselves, borrow from United or borrow from an independent lender. Investors cannot rely on this Product Ruling if they enter into a finance agreement with United that materially differs from that set out in the finance documents provided to the Tax Office by MFM with the application for this Product Ruling.

80. The finance made available by United is offered on the following terms contained in the Term Loan Finance Agreement and Finance Application Form and Investment Loan Schedule ('Finance Agreement'):

Term	5 years and one month
Investment amount able to be borrowed	Full amount of Fund Investment plus the Establishment Fee
Interest Rate	9.75%
Loan Approval and Drawdown Date	On or before 30 June 2007
Repayment Details	<p>61 monthly repayments, payable in arrears as follows:</p> <ul style="list-style-type: none"> <li>• interest only repayments for the first 13 months; then</li> <li>• principal and interest repayments for the remaining 48 months.</li> <li>• The last repayment includes a residual amount of 20%, being \$11,000.</li> </ul>
Establishment Fee	\$1,375

81. The Investor charges the Charged Property to United as Security for the due and punctual payment of the Principal and interest payable and any costs incurred by United for the Investor's non compliance with the Finance Agreement and the performance of all obligations owed by the Investor to United.

82. The Charged Property includes all the Investor's present and future right, title and interest in and to, and all entitlements, benefits and rights arising in favour of the Investor under or in connection with the Film including those under or in connection with the Film Documents, any property owned by the Investor in relation to the Film, that is the Investor's Copyright interest, and any amount due to the Investor in relation to the Film, that is rights to Adjusted Gross Participation and the MGA.

83. If an Investor defaults on his obligations under the Finance Agreement (as defined in clause 14 of the Finance Agreement), then in addition to any rights available to United at law, United may at its sole discretion:

- (i) terminate the Finance Agreement and sue the Investor for the Principal and interest payable and any costs incurred by United for the Investor's non compliance with the Finance Agreement; and/or
- (ii) exercise its rights in relation to the Charged Property and/or any other guarantee that it holds in relation to the Investor's obligations; and/or
- (iii) sell and/or transfer all of the rights and interests which the Investor has in the scheme.

84. This Ruling does not apply if a finance arrangement entered into by an Investor to fund the Investor's Investment in the Film includes or has any of the following features:

- a different finance arrangement is entered into with United.
- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL or the funding arrangements transform the Project into a 'scheme' to which Part IVA may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Film;
- the funds borrowed, or any part of them, will not be available for the conduct of the Film 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.

## 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.*

### Division 10BA

#### *The 'directly expended' requirement*

85. Subsection 124ZAA(6) requires that capital money contributed to the production of a film must be expended directly in producing the film in order for a deduction under Division 10BA to be available.

86. Paragraph 8 of Taxation Ruling IT 2111 discusses this requirement. It states: 'Direct expenses on a film production which qualify for a deduction under section 124ZAA can generally be described as **those relating to the production process** as distinct from those associated with financing or marketing of the Film. Such expenses would **typically include amounts paid for the acquisition of story rights and the surveying of locations, payments to the producers, directors and cast, and the costs of insurance of production associated risks, drawing up performers' contracts and the building of sets and scenery**' (emphasis added).

87. The Tax Office view is that the 'directly expended' requirement is not met at the point in time when the Investors make payments to the Production Company in respect of the Budget for the Film. Rather, the extent of the application of the money by the Production Company to elements of production will ultimately determine the portion of the Investors' contribution that meets this requirement. Generally, this will not be known until after the completion of the Film.

88. In determining the amount that is 'directly expended' on the production of the Film, we will also consider the ultimate application of any funds obtained by the Production Company as Underage. In this regard, the parties have agreed that any Underage will be retained by the Production Company as a success fee in a manner that will preserve the status of the Film as a 'qualifying Australian film'.

89. The Investors will pay the CC to the Production Company which will use 93.5% of total funds for application towards the production costs. In doing this, the Production Company is to ensure that this proportion of funds contributed by investors is only expended on items within the Film's production Budget.

90. Quantification of the amount of money directly expended on the production of a film, and consequently the deduction available under Division 10BA, can only be determined after a film has been produced. To do this, a full audit of the application of the film production funds would normally be required. The practice of conducting an audit of the contribution account that is held by a production company (known as an audit of the Film) is considered inadequate in this regard.

91. Accordingly, while a deduction should be available in respect of the contributions made by Australian Investors, the deduction will be withdrawn with retrospective effect if the amounts contributed are not directly expended on the Film.

***The 'at risk' rule***

92. Section 124ZAM reduces claims for Division 10BA deductions where the Commissioner is satisfied that a taxpayer was not at risk in respect of any part of the expenditure of capital moneys the taxpayer made by way of contribution to the cost of producing a film. Subsection 124ZAM(2) specifies the amount of risk is the amount of loss that, in the Commissioner's opinion, would be suffered by reason of the taxpayer's said capital expenditure where no income is derived from the taxpayer's interest in the copyright of the film, other than excepted income as defined in subsection 124ZAM(3).

93. Paragraph 13 of Taxation Ruling IT 2111 discusses the 'at risk' rule and states the rule:

... does not operate to affect the deductions available to Investors where pre-sale arrangements or the sale of distribution rights are effected prior to completion of the Film unless the arrangements put funds into the hands of Investors – by loan or otherwise – to enable them to make their contributions to the costs of film production. Similar considerations apply in respect of a distribution guarantee arrangement under which an amount may be paid to Investors by a producer or another person in exchange for distribution rights, if a specified return is not achieved within a particular period (for example, a specified percentage of the film budget within 2 years). Payments under an arrangement of that kind would also not offend the 'at risk' rule.

94. The 'at risk' rule applies to an Investor's risk of loss before and after completion and distribution of the Film. Any arrangement which limits an Investor's risk of loss can breach the 'at risk' rule. Certain types of common industry arrangements affecting risk during production of the Film are accepted as not offending the 'at risk' rule. This acceptance does not extend to arrangements which put funds into the hands of Investors to enable them to make their contributions to the costs of film production. This cannot be taken to mean that post-completion arrangements are also acceptable if they do not put funds into the hands of Investors to enable them to make their contributions. The position in paragraph 13 of IT 2111 is limited to the situations expressly mentioned.

95. The arrangement ruled on does not contain any features which attract the operation of section 124ZAM.

## **Non-arm's length transactions**

96. Where, in producing a film, an amount is expended by a person (the film producer) for the supply of goods or the provision of services, subsection 124ZAJ(1) allows the Commissioner to reduce deductions under Division 10BA for such amounts where he is satisfied that:

- the film producer and the person supplying the goods or providing the services were not dealing with each other at arm's length in relation to the transaction; and
- the amount of moneys expended on the supply of those goods or the provision of those services exceeds the amount of moneys that would have been expended by the film producer if the film producer and the person supplying those goods or providing those services had dealt with each other at arm's length.

97. The Commissioner will not be in a position to determine whether his discretion in subsection 124ZAJ(1) ought to be exercised until such time as the Film has been produced. Furthermore, to make such a determination, a full audit of the Film's application and production fund would normally be required.

98. Accordingly, while a deduction should be available in respect of capital moneys expended by Investors by way of contribution to the cost of producing the Film before the end of the financial year ending 30 June 2007, the deduction will be reduced with retrospective effect if the Commissioner determines that a producer of the Film dealt with a supplier of goods or a provider of services, in the course of producing the Film, in circumstances where the parties were not dealing at arm's length and the producer paid more for the goods or the services than the producer would have paid had the transaction been at arm's length.

## **Relevant 24 month period**

99. The relevant 24 month period referred to in subsection 124ZAFA(2) commences from the 30 June 2007, being the end of the financial year in which capital moneys were first expended by way of contribution to the cost of producing the Film.

## **Section 8-1**

### ***Management Fee and Annual Management Fee***

100. Subject to section 124ZAO of the ITAA 1936 (see paragraphs 106 and 107 of this Ruling), the Management Fee and Annual Management Fee are deductible in terms of section 8-1 of the ITAA 1997.

**Interest***(i) Investors who use United as finance provider*

101. Some Investors will elect to finance their CC through a loan facility from United. Subject to section 124ZAO of the ITAA 1936 (see paragraphs 106 and 107 of this Ruling) a deduction will be allowable under section 8-1 of the ITAA 1997 for interest incurred under the United facility.

*(ii) Investors who DO NOT use United as finance provider*

102. Investors who finance their investment through a loan facility with a bank or financier other than United 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.

**Section 25-25**

103. The Establishment Fee payable to United is a borrowing expense and is deductible under section 25-25 of the ITAA 1997 subject to section 124ZAO of the ITAA 1936 (see paragraphs 106 and 107 of this Ruling).

104. The Establishment Fee 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. However, where the total amount of a borrowing expense is \$100 or less, the full amount of the borrowing expense may be deducted in the year in which it is incurred and/or paid.

105. The deductibility or otherwise of borrowing costs arising from loan agreements entered into with financiers other than United is outside the scope of this Ruling.

**Section 124ZAO**

106. With the exception of deductions under section 124ZAF, section 124ZAO will operate to limit the amount of any deduction otherwise allowable in relation to the Film and in gaining or producing assessable income to which section 26AG relates. The deduction allowable in a year of income will be limited to the amount of film income which is derived from the Film (subsection 124ZAO(2)). Any excess deductions may be carried forward indefinitely and offset against future income from the Film (subsection 124ZAO(3)).

107. Section 124ZAO may apply in relation to deductions in respect of the Management Fee, Annual Management Fee, Establishment Fee and interest.

**Partnership and section 26AG**

108. The Investors in the Film will be considered to be a partnership for income tax purposes as they are in receipt of ordinary income or statutory income jointly (see the definition of 'partnership' in section 995-1 of the ITAA 1997). Amounts received by a Partnership of Investors in a Film, from the exploitation of their Copyright interest in the Film, including share of Adjusted Gross Participation and the MGA, will be assessable income of the Investors under paragraph 26AG(1)(d) in the income year in which they are received. Although there exists a tax law partnership, subsection 26AG(9) of the ITAA 1936 provides that income of a partnership assessable under subsection 26AG(1) of the ITAA 1936 is taken to be income derived by the partners/Investors.

109. Consideration receivable by an Investor in a Film, from the disposal of the Investor's Copyright interest in the Film, will be assessable income of the Investor in the income year in which the Copyright interest is disposed of and will be an amount equal to the specified price, or the amount determined by the Commissioner where there is no specified price (paragraph 26AG(1)(e) and subsection 26AG(3)).

110. If the Buyout Option is exercised by SCP the assessable income of the Investors from their disposal of their Copyright interests will be their proportionate share of the greater of the market value of the Buyout Rights or 20% of the Budget of the Film. These amounts will be assessable income of the income year in which the Buyout Option is exercised which may not be the same as the income years in which the payments are actually received from the disposal of the Copyright interests.

**Division 35**

111. Subsection 35-5(2) of the ITAA 1997 specifically provides that Division 35 of the ITAA 1997, which regulates the deduction of losses from non-commercial business activities, is not intended to apply to 'activities that do not constitute carrying on a business, for example, the receipt of income from passive investment'.

112. The transactions covered by the scheme amount to an acquisition of passive investments and the deriving of income from those investments. Hence, Division 35 of the ITAA 1997 does not apply to the Project.

**Section 79D**

113. Section 79D does not apply where there are no 'foreign income deductions' (as defined in subsection 160AFD(9)).

114. The transactions covered by the scheme do not give rise to 'foreign income deductions' because the deductions under Division 10BA do not relate to any 'assessable foreign income' (as defined in subsection 160AFD(9)). The income derived by the Investors under the draft HDA, and any other distribution agreements entered into by the Head Distributor, will have an Australian source and will not be 'assessable foreign income'.

115. The Investors have no beneficial interest in the Gross Receipts received from any licensee or sub licensees. The Investors have no entitlement to any withholding tax credits deducted from amounts paid under the draft HDA entered into by MFM.

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

116. Section 82KL has no application to Division 10BA arrangements and is therefore not relevant to any deductions properly allowable to the Investors under Division 10BA.

#### **Part IVA – general tax avoidance provisions**

117. For Part IVA to apply, there must be a 'scheme' (section 177A), a 'tax benefit' (section 177C), and a dominant purpose of entering into the scheme to obtain a tax benefit (section 177D). The arrangement subject to this Ruling will be a 'scheme'. The Investor will obtain, for example, a 'tax benefit' from entering into the scheme, in the form of a deduction allowable under the provisions in Division 10BA that would not have been obtained but for the scheme. However, it is not possible to conclude, from the arrangement outlined in this Ruling, that the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

118. An Investor to whom this Ruling applies intends to stay in the scheme for its full term and derive assessable income from the exploitation of the Copyright of the Film. Further, there are no features of the Film, as described in the said arrangement, that suggest that the Film is so 'tax driven' and 'so designed to produce a tax deduction of a certain magnitude', that the operation of Part IVA is attracted.



## **Payment of interest by an Investor where an assessment is amended**

119. Section 280-100 of Schedule 1 of the TAA provides that where an amendment of an assessment increasing the liability of a taxpayer to tax is made, the taxpayer is liable to pay a shortfall interest charge to the Commissioner on the amount by which the tax payable by the taxpayer under the amended assessment exceeds the tax payable by the taxpayer under the assessment that was amended.

120. Investors who expend capital moneys by way of contribution to the cost of producing a film should be aware of this provision because, should the circumstances surrounding the production of a 'qualifying Australian film' require the Commissioner to go back and reduce the deductions claimed by Investors in that film, section 280-100 will have application. There is a discretion in section 280-160 of Schedule 1 of the TAA under which the Commissioner can remit, in appropriate circumstances, the whole or part of the charge.

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

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

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### *Related Rulings/Determinations:*

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### *Subject references:*

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- film income
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