


PR 2007/66 - Income tax: FEA Plantations Project 2007 (2008 Growers)

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Product Ruling

Income tax: FEA Plantations Project 2007 (2008 Growers)

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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 FEA Plantations Project 2007 (2008 Growers) 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 28 of this Ruling on or after 1 July 2007 and on or before 30 June 2008. 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;
- entities who participate in the Project through offers made other than through the Product Disclosure Statement;
- entities who are accepted to participate in the Project before 1 July 2007 and after 30 June 2008;
- entities who enter into finance arrangements with Forest Enterprises Australia Limited (FEA) or Allco Managed Investments Limited (AMIL) other than those described at paragraphs 69 to 75 of this Ruling; or
- FEA Plantations Limited or its associates.

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 28 to 76 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 Product Ruling may be withdrawn or modified.

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Date of effect

9. This Product Ruling applies prospectively from 27 June 2007, the date this Product Ruling is made. It therefore applies only to the specified class of entities that enter into the scheme from 1 July 2007 until 30 June 2008, 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 2010.

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 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

18. 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 28 to 76 of this Ruling.

19. The Grower's participation in the Project must constitute the carrying on of business of 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 Management Agreement.

20. A Grower is not eligible to claim any tax deductions until the Grower's application to enter the Project is accepted and the Project has commenced.

The Simplified Tax System (STS)

Division 328

21. 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*.

22. 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

23. 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**Sections 6-5 and 17-5**

24. 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.

Deduction for Establishment Fee, Pruning Fee, insurance premiums, interest, borrowing and stamp duty costs**Section 8-1, section 25-25 and Division 27 of the ITAA 1997 and section 82KZMG of the Income Tax Assessment Act 1936**

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

Fee Type	Year ended 30 June 2008	Year ended 30 June 2009	Year ended 30 June 2010
Establishment Fee	\$3,465 See Notes (i) & (ii)	Nil	Nil
Pruning fee	Nil	Nil	As Incurred See Notes (iii) & (vi)
Insurance premium	As incurred See Notes (v) & (vi)	As incurred See Notes (v) & (vi)	As incurred See Notes (v) & (vi)
Interest payable to FEA	As incurred See Notes (iv) & (vi)	As incurred See Notes (iv) & (vi)	As incurred See Notes (iv) & (vi)
Borrowing costs including Stamp Duty payable to FEA under the Loan Agreement	Must be calculated See Note (vii)	Must be calculated See Note (vii)	Must be calculated See Note (vii)
Interest payable to AMIL	As incurred See Notes (iv) & (vi)	As incurred See Notes (iv) & (vi)	As incurred See Notes (iv) & (vi)
Borrowing costs including Stamp Duty payable to AMIL under the Loan Agreement	Must be calculated See Note (vii)	Must be calculated See Note (vii)	Must be calculated See Note (vii)

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 Application Money is expenditure for 'seasonally dependent agronomic activities' (see paragraphs 93 to 95 of this Ruling) and is deductible in the income year in which it is incurred.
- (iii) The Pruning Fees set out in the Management Agreement are deductible in full in the year in which they are incurred.
- (iv) Interest on loans with FEA or AMIL is deductible in the year in which it is incurred. However, the deductibility or otherwise of interest arising from loan agreements entered into with financiers other than FEA or AMIL, is outside the scope of this Ruling. Growers who borrow from lenders other than FEA or AMIL may request a private ruling on the deductibility of the interest incurred.
- (v) Insurance premiums are deductible in the year in which they are incurred. Where a Grower takes out insurance to cover events against fire, hail and windstorms as set out in the Management Agreement, the premiums will be deductible in full in the year in which they are incurred.
- (vi) This Ruling will not apply to any Grower who prepays the pruning fee, insurance premiums or interest. A prepayment of the pruning fee, insurance premiums or interest will occur where an amount is paid by a Grower for pruning fee, insurance premiums or interest for a period that extends beyond the income year in which the fees or interest are incurred. Such Growers may seek a private ruling on the tax implications of their participation in the Project.
- (vii) Borrowing expenses are deductible under subsection 25-25(1) where the borrowed moneys are used or will be used during that income year for income producing purposes. They are incurred for borrowing moneys that are used or are to be used during that income year solely for income producing purposes. Where the borrowing expenses exceed \$100 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 FEA or AMIL 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

26. A Grower who is an individual accepted into the Project in the year ended 30 June 2008 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 who participate under the following Woodlot Options:

- Woodlot Option 1, from **30 June 2008 to 30 June 2021**; or
- Woodlot Option 2 or Woodlot Option 3 from **30 June 2008 to 30 June 2024**.

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

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

- expenditure by a Grower does not fall within the scope of sections 82KZME and 82KZMF, refer to paragraphs 90 to 92 of this Ruling;
- 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.

Scheme

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

- Application for a Product Ruling received on 13 December 2006 and additional correspondence and emails dated 18 and 21 December 2006, 8 January 2007 and 7 February 2007 and 28 May 2007;

- Draft **Product Disclosure Statement** for the FEA Plantations Project 2007 and 2008 (PDS), issued by FEA Plantations Limited (FEAP) the Responsible Entity, received 20 April 2007;
- Draft **Constitution** establishing the FEA Plantations Project 2007, received on 24 January 2007;
- Draft Compliance Plan for FEA Plantations Project 2007 issued by FEAP, received 13 December 2006;
- Draft Forestry Right Deed between Landowner, FEAP and Forest Enterprises Australia Limited (FEA) (as Grantor), including the land titles form 'transfer creating profit a prendre', received 13 December 2006;
- Draft **Forestry Right Lease Deed**, (the Lease), to be entered into by each Grower and FEAP (the Lessor), as amended and received 20 April 2007;
- Head Management Agreement between FEAP and FEA dated 31 May 2001, received 13 December 2006;
- Draft **Management Agreement**, to be entered into by each Grower and FEAP (the Manager), as amended and received 20 April 2007;
- Draft **Finance Application and Loan Agreement**, to be entered into by each Grower seeking finance and FEA, received 13 December 2006;
- Draft **Finance Application and Loan Terms**, to be entered into by each Grower seeking finance and Allco Managed Investments Limited (AMIL), received 13 December 2006;
- Custodian Agreement between FEAP and the Custodian dated 6 June 2000, received 13 December 2006;
- Draft Wood Purchase Agreement between FEAP and FEA, received 13 December 2006; and
- **Plantation Insurance Scheme** to be entered into by each Grower seeking plantation insurance and the Insurer, received 13 December 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.

29. The documents highlighted are those that a Grower may enter into. For the purposes of describing the scheme to which this Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate of a Grower, will be a party to, which are a part of the scheme. The effect of these agreements is summarised as follows.

30. 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.

31. The main features of the FEA Plantations Project 2007 are as follows:

Location	Tasmania and areas of New South Wales and Queensland.
Type of business to be carried on by each participant	Commercial growing and cultivation of <i>Eucalyptus nitens</i> (Shining Gum) and similar species, for the purpose of harvesting and selling timber.
Number of hectares offered for cultivation	Approximately 5,000 with capacity for oversubscription.
Size of each interest	0.5 hectares (one Woodlot).
Woodlot Options	<p>Woodlot Option 1:</p> <ul style="list-style-type: none"> trees will be planted and maintained for approximately 13 years before being harvested. It is anticipated that Growers will receive a thinning return in 2017. <p>Woodlot Option 2:</p> <ul style="list-style-type: none"> trees will be planted and maintained for approximately 16 years before being harvested. It is anticipated that Growers will receive a thinning return in 2017. It is anticipated the trees will be pruned in approximately years 2, 4 & 6. <p>Woodlot Option 3:</p> <ul style="list-style-type: none"> incorporates a fixed combination of woodlots in Woodlot Option 1 and Woodlot Option 2, invested in a ratio of 3:1 respectively.
Minimum allocation	One Woodlot
Minimum subscription	None
Number of trees per Woodlot	Minimum of 600 trees
Term of the Project	<p>Woodlot Option 1 – 14 years</p> <p>Woodlot Option 2 – 17 years</p> <p>Woodlot Option 3 – 17 years</p>
Initial cost per Woodlot	\$3,465 for Establishment Services

Ongoing costs	<ul style="list-style-type: none"> Growers will be charged for the cost of any insurance, except for Public Liability insurance. Pruning fees will be payable for Woodlot Option 2 and some Woodlot Option 3, in year 2 (\$396), year 4 (\$418) & year 6 (\$440), for each Woodlot. These costs will be increased in line with CPI.
Other costs	<ul style="list-style-type: none"> Deferred management fee and deferred rent will be a percentage of harvest proceeds or from insurance proceeds where the plantation crop is damaged or destroyed. The fee will be equal to 15% of the harvest proceeds.

32. The Project is registered as a managed investment scheme under the *Corporations Act 2001*. FEAP Plantations Limited (FEAP) has been issued with an Australian Financial Services Licence and will be the Responsible Entity for the Project.

33. Participants who will be accepted as Growers will establish, manage, harvest and sell a commercial plantation of *Eucalyptus nitens* (Shining Gum) and similar species for the purpose of carrying on a commercial business of afforestation during the Term of the Project.

34. An offer to participate in the Project will be made through a PDS. The offer under the PDS is for 5,000 hectares in the Project and will invite participants to subscribe for at least 1 Woodlot in the Project on or after 1 July 2007 and on or before 30 June 2008.

35. To participate in the Project participants must complete and sign the Application and Power of Attorney Form in the PDS and pay \$3,465 per Woodlot with their Application by 30 June 2008. The Application Money will be banked into the relevant Application Fund and released to FEAP when the Grower's application to acquire an Interest has been accepted by FEAP.

36. By signing the Application Form the participant is deemed to have signed and have agreed to be bound by the terms of the Management Agreement and Forestry Right Lease Deed, and authorise FEAP to date and complete the terms of the management agreement and Forestry Right Lease Deed.

37. Once FEAP receives the participant's signed Application, FEAP may accept or refuse any application. For an Applicant who is accepted as a Grower in the Project, FEAP will allocate Woodlots, place their details in a Register and enter into agreements in relation to the Woodlots allocated to the Grower with FEAP and its associates.

38. A Grower accepted on or after 1 July 2007 and on or before 30 June 2008, will commence participation as a '2008 Grower'. **This Ruling only applies in respect of a '2008 Grower' who is accepted into the Project between 1 July 2007 and 30 June 2008.**

39. Plantations in this Project will be established close to other existing plantation holdings that the Forest Enterprises Group has established in Tasmania, northern New South Wales and Queensland.

40. Each Grower will be granted by, and take from the Responsible Entity, a lease of a Forestry Right in a Woodlot under the Forestry Right Lease Deed for the purpose of cultivating and nurturing Trees, and harvesting Timber. The minimum area of land that can be leased by a Grower under the Project is 1 or 4 Woodlots of 0.5 hectare per woodlot depending on which Woodlot Option is selected.

41. The Grower's rights under the Forestry Right Lease Deed will include the right to enter and exclusively use the Woodlot allocated to the Grower including the right to plant, cultivate, manage and harvest Trees on that Land and to sever, take away and sell the Timber.

42. The Grower will enter into a Management Agreement with FEAP to have suitable Eucalyptus seedlings planted on their Woodlot for the purposes of thinning at approximately 9 years after planting and clear fell at approximately 13 or 16 years after planting, depending on which Woodlot Option is selected. FEAP will establish the Woodlot during the optimal planting season but no later than 12 months after the acceptance of the application.

43. Under the Management Agreement, FEAP will also cultivate the Grower's Trees and be responsible for harvesting, processing and selling the Grower's Timber. Growers in Woodlot Option 2 and Woodlot Option 3 will be required to prune their Trees in approximately years 2, 4 and 6.

44. The sale proceeds of Timber will be placed in a Proceeds Fund established under the Constitution which will include the proceeds from amounts received at thinning and clear felling of the Timber on the plantation Woodlots from one or both of the Option 1 Proceeds Fund or Option 2 Proceeds Fund. From the relevant Proceeds Fund the Custodian will deduct and pay to FEAP each Grower's respective Rent under the Forestry Right Lease Deed and their Management Fees under the Management Agreement. The amount remaining will be distributed to Growers. Distributions to Growers will be based on the percentage that their Woodlots bear to the total number of Woodlots.

45. FEAP will endeavour to procure, if requested by the Grower, insurance cover against destruction or damage of the Grower's Woodlot by fire and other usual risks. The Manager will invoice the Grower the relevant insurance premium together with an administration charge of 10% of the amount of the premium in each year or part thereof. Insurance will be compulsory for Growers who obtain finance longer than one year for their investment from FEA and AMIL. Growers may elect to arrange their own insurance.

46. Growers will receive an annual report from the Independent Forester and FEAP summarising the progress of plantations in the Project. The report from FEAP will cover:

- compliance with the arrangement as described in the Product Ruling;
- compliance with any changes to the tax laws subsequent to the issue of the Product Ruling and any significant changes to the market which may impact product marketing; and
- any changes to fees.

47. The Project will conclude upon final harvest of the Trees and the sale of the Timber. The thinning of all Woodlots is scheduled to occur about 9 years from planting, when approximately half the Trees will be harvested.

Constitution

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

49. An applicant for an Interest in the Project must complete and sign the application in the form and manner approved by the Responsible Entity. Clause 6 provides that the application must:

- be accompanied by payment of the amount due to, and in the form required by, the Responsible Entity for an Interest in the Project;
- include an irrevocable and binding authority by the applicant to enter into the Forestry Right Lease Deed and Management Agreement, in the form in Schedules 4 and 5 of the Constitution or in such other form and content as the Responsible Entity determines from time to time;
- include a power of attorney in favour of the Responsible Entity; and
- be accompanied by such other information and documents and in such forms as the PDS may require.

50. All moneys received from applications shall be held by FEAP in the Application Fund, on trust for the Growers. The Responsible Entity may transfer money paid by an Applicant from the Application Fund when FEAP is reasonably satisfied that certain specified criteria in the Constitution have been met (Clause 15). If Application Money is paid and Interests are not issued to the Applicant who paid the Application Money, then the Application Money must be refunded to the Applicant before the end of one month starting on the day on which the Application Money was received, or if it is not reasonably practicable to do so before the end of one month, then by the end of such longer period as is reasonable in the circumstances.

51. In summary, the Constitution also sets out provisions relating to:

- interests of Applicants and Growers in the Application and Proceeds Funds, clause 7;
- the transfer of the Grower's interest in the Project, clause 10;
- Growers' default, clause 13;
- Grower's income and distributions, clauses 16 and 17;
- Responsible Entity's powers, clause 20 and rights, clause 21;
- withdrawal rights, clause 23;
- Complaints Handling, clause 24;
- the right of FEAP to be paid fees and other expenses, clause 26; and
- winding up the Project, clause 30.

Compliance Plan

52. As required by the Corporations Act, the Responsible Entity has prepared a Compliance Plan. The purpose of the Compliance Plan is to ensure that the Responsible Entity manages the Project in accordance with its obligations and responsibilities contained in the Constitution and that the interest of a Grower is protected.

Forestry Right Deed

53. The Landowner grants to FEAP the Forestry Rights described in clause 6 for the Term commencing on the Commencement Date and ending on the Termination Date. FEAP will register a Forestry Right by lodging an Instrument Form detailing the particulars of the Forestry Right (in Tasmania), a Registration of profit a prendre (in Queensland) or a Transfer Creating Profit a Prendre or Forestry Right (in New South Wales), and lodge a caveat or other document with the Land Titles Office.

Forestry Right Lease Deed

54. The Responsible Entity grants to the Grower a lease of the Responsible Entity's Forestry Right over the Land on which the Grower's plantation will be established including the right for the Authorised User to have the use and benefit of the Forestry Right as it pertains to the Land and includes the right granted in clause 2.1(a)(i) to (iii).

55. Under this Lease the Grower agrees to pay to the Lessor the Rent for the lease of the specified area of Land for the term of the lease period. The term of the Lease is from the date of the allocation of the Land by FEAP, until the clear fell of Trees on the Land or the expiry of 20 years from the date the Land is allocated, whichever is the earlier.

56. In summary, the Lease also sets out provisions relating to:

- Grower's covenants (clause 3);
- mutual covenants (clause 4);
- payment of Rent (clause 5);
- events of damage or destruction (clause 7); and
- termination (clause 10).

Management Agreement

57. Under the Management Agreement, each Grower contracts with the Manager to establish and maintain a plantation of Trees on their leased area of Land until maturity. At maturity, the Trees will be harvested and the Timber sold on behalf of the Grower.

58. The Manager will provide the Plantation Establishment Services described in clause 1 of the agreement. These include:

- the completion of all preparatory work necessary for the planting of seedlings on the Woodlot including all ploughing and vermin control deemed necessary by the Manager;
- the supply and planting of healthy seedlings to an average density per hectare appropriate to the soil and climatic circumstances of the Woodlot; and
- the control of weeds and other vegetation which might inhibit the growth of the seedlings on the Woodlot.

59. The Plantation Establishment Services shall commence as soon as practical after the date of execution of the Management Agreement being the date on which the Grower's application is accepted (Agreement Commencement Date). The Manager will use its best endeavours to complete all Plantation Establishment Services within the first 12 months from the date that the Grower is accepted into the Project.

60. The Manager will provide Management Services related to the tending and rearing of the seedlings and the management and maintenance of the plantation established on the Woodlot (clause 3). These include:

- the replanting to 90% of the average initial planting density, of any seedlings which die during the first 2 years after the date the Grower is registered as the holder of the Woodlots, where such death is caused by planting technique or vermin destruction;
- the trees subject to Woodlot Option 2, and a proportion of Woodlot Option 3, will be pruned three times before such trees reach approximately 6 years of age;
- the general maintenance of the plantation, fire breaks, and access roads;
- the application of fertiliser to maintain satisfactory growth;
- the provision of an annual written report; and
- the provision of advice and assistance to the Grower generally.

61. In the event that a Grower's plantation suffers damage and it is not economic to nurture the plantation to harvest, the Management Agreement will come to an end as at the date of destruction. The only obligation remaining on the parties will be the obligation of the Grower under the Constitution to pay Deferred Fees (which includes the Management Fees). The Deferred Fees will crystallise on the date of destruction and thereupon become due and payable (clause 15).

62. On behalf of the Grower the Manager will determine the appropriate time for the thinning and clear fell of the Grower's Trees and will market and sell the Grower's Timber.

Draft Wood Purchase Agreement

63. The Manager has entered into a Wood Purchase Agreement with FEA whereby FEA has agreed to purchase the harvested wood for the purchase price, which is fair and reasonable having regard to the market prices at the time of harvest for wood of similar quality and quantity.

Pooling of amounts and distribution of Proceeds

64. The Constitution (clause 16 and 17) sets out provisions relating to the pooling of amounts from the sale of the Grower's Timber and the distribution of Proceeds Funds from that sale or from Insurance Proceeds. This Product Ruling only applies where the following principles apply to those pooling and distribution arrangements:

- only a Grower who has contributed to the pool making up the Proceeds Fund is entitled to benefit from distribution from those proceeds; and

- any pool of Trees must consist only of Trees contributed by a Grower in the FEA Plantations Project 2007.

Fees

65. The following fees, per Woodlot, are set out in the Management Agreement and Forestry Right Lease Deed:

- \$3,465, for the Plantation Establishment Services to be provided within 12 months of the Grower's application being accepted, payable on application;
- Rent of 12% of the Harvest Proceeds;
- a Management Fee of 3% of the Harvest Proceeds; and
- Pruning fees will be payable for Woodlot Option 2 and Woodlot Option 3, in year 2 (\$396), year 4 (\$418) and year 6 (\$440), for each Woodlot. These costs will be increased in line with CPI.

Finance

66. A Grower who does not pay the Application Monies in full upon application can borrow from FEA, borrow from AMIL the Preferred Financier, or borrow from an independent lender external to the Project.

67. Only the finance arrangements set out below are covered by this Product Ruling. A Grower cannot rely on this Product Ruling if they enter into a finance arrangement with FEA or AMIL that materially differs from that set out in the documentation provided to the Tax Office with the application for this Product Ruling. A Grower who enters into a finance arrangement with an independent lender external to the Project other than AMIL may request a private ruling on the deductibility or otherwise of interest incurred under finance arrangements not covered by this Product Ruling.

68. Growers cannot rely on any part of this Ruling if the Application Monies are not paid in full on or before 30 June 2008 by the Grower or, on the Grower's behalf, by a lending institution. Where an application is accepted subject to finance approval by any lending institution other than FEA, Growers cannot rely on this Ruling if written evidence of that approval has not been given to the Responsible Entity by the lending institution by 30 June 2008.

Finance offered by FEA

69. A Grower can finance the cost of their Application by borrowing from FEA an amount equal to their full Application Fee less any deposit that applies to the finance option selected. For loan terms longer than one year, the initial minimum deposit for principal and interest loans is 10%. For 12 months interest free loans, the initial deposit is optional. Growers are also liable to pay applicable stamp duty on the 12 months interest free loans and a loan establishment fee of \$150 plus 0.2% of finance sought is payable for principal and interest loans.

70. FEA will only provide loan funds to Growers if FEA has sufficient funds available to advance the loan monies for the Growers.

71. Subject to FEA accepting the Grower's application, the Grower will be bound by the terms and conditions of the Loan Agreement.

72. FEA provides the loan on a full recourse basis and recovery action will be taken in respect of any default by the borrower. Security is provided by a charge over the whole right, title and interest of the benefits arising out of each of the project documents. Overdue repayments will incur interest at the default rate of 15% per annum.

73. The details to each loan term offered by FEA are summarised below. Interest rates shown below are for indicative purposes only and FEA will confirm the rate of interest applicable to your loan.

Investment Option	Finance Option
Woodlot Option 1, 2 and 3	12 months interest free Principal repayable in 12 monthly instalments and the first monthly repayment starting on 31 July 2008.
Woodlot Option 1, 2 and 3	3 years principal & interest at 10.00%
Woodlot Option 1 and 2	5 years principal & interest at 10.25%
Woodlot Option 3	6 years principal & interest at 10.25%
Woodlot Option 1 and 2	7 years principal & interest at 10.50%
Woodlot Option 3	9 years principal & interest at 10.50%
Woodlot Option 1 and 2	10 years principal & interest at 11.00%
Woodlot Option 3	12 years principal & interest at 11.00%

Finance offered by AMIL

74. As an alternative, a Grower is able to borrow from AMIL an amount up to 90% of the Application Money. Growers are liable to pay a loan Establishment Fee of \$250 plus 0.5% of the finance sought. Security is provided by a charge over the whole right, title and interest of the benefits arising out of each of the project documents. The loan is on a full recourse basis and recovery action will be taken in respect of any default.

75. The details to each loan term offered by AMIL are summarised below. Interest rates shown below are for indicative purposes only and AMIL will confirm the Initial Interest Rate applicable to your loan.

Investment Option	Finance Option with Principal and Interest repayments
Woodlot Option 1, 2 and 3	3 years principal & interest at 11.00%
Woodlot Option 1 and 2	5 years principal & interest at 11.00%
Woodlot Option 3	6 years principal & interest at 11.00%
Woodlot Option 1 and 2	7 years principal & interest at 11.00%
Woodlot Option 3	9 years principal & interest at 11.25%
Woodlot Option 1 and 2	10 years principal & interest at 11.25%
Woodlot Option 3	12 years principal & interest at 11.25%

Investment Option	Finance Option with Interest Only period then reverting to Principal and Interest repayments
Woodlot Option 1 and 2	2 years interest only plus 3 years principal & interest at 11.00%
Woodlot Option 1 and 2	2 years interest only plus 5 years principal & interest at 11.00%
Woodlot Option 1 and 2	2 years interest only plus 8 years principal & interest at 11.25%
Woodlot Option 3	3 years interest only plus 3 years principal & interest at 11.00%
Woodlot Option 3	3 years interest only plus 6 years principal & interest at 11.25%
Woodlot Option 3	3 years interest only plus 9 years principal & interest at 11.25%

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

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL of the ITAA 1936 or the funding arrangements transform the Project into a 'scheme' to which Part IVA of the ITAA 1936 may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project, other than FEA, are involved or become involved in the provision of finance to a Grower 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?

77. For the amounts set out in paragraph 25 of this Ruling to constitute allowable deductions the Grower's afforestation activity as a participant in the FEA Plantations Project 2007 must amount to the carrying on of a business of primary production.

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

79. 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?

80. Taxation Ruling TR 2000/8 Income tax: investment schemes, particularly paragraph 89, is more specific to arrangements such as the FEA Plantations Project 2007. 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.

81. Having applied these principles to the arrangement set out above, a Grower in the FEA Plantations Project 2007 is accepted to be carrying on a business of growing and harvesting Wood for sale.

The Simplified Tax System

Division 328

82. 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.

83. 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 Establishment Fee, insurance premiums, pruning fee and interest on loans with FEA or AMIL

Section 8-1

84. The Establishment Fee, pruning fee and insurance premiums 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 Establishment Fee, insurance premium or pruning fee (see paragraphs 49 to 51 of TR 2000/8).

85. 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 88 to 92 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.)

86. Some Growers may finance their participation in the Project through a Loan Agreement with FEA or AMIL, the preferred financier. Applying the same principles as that used for the Establishment Fee and the insurance premiums, pruning fee, interest incurred under such a loan has sufficient connection with the gaining of assessable income to be deductible under section 8-1.

87. Other than where the prepayment provisions apply (see paragraphs 88 to 92 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

88. 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.

89. 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 of the ITAA 1936 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***

90. Other than the Establishment Fee (see below) the fees payable under scheme to which this Product Ruling applies are incurred annually for services to be wholly provided in the year in which those fees are incurred and the interest payable to FEA or to AMIL 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.

91. However, sections 82KZME and 82KZMF of the ITAA 1936 may have relevance if a Grower in this Project prepays all or some of the expenditure payable under the Management Agreement and/or the Forestry Right Lease Deed, or prepays interest under a loan agreement (including loan agreements with lenders other than FEA or AMIL). 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.

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

Section 82KZMG

93. 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.

94. Under the Management Agreement each Grower incurs an initial establishment fee of \$3,465 per Woodlot for 'seasonally dependent agronomic activities' that will be carried out during the 'establishment period' of the Trees.

95. The expenditure for 'seasonally dependent agronomic activities' meets all other requirements of section 82KZMG of the ITAA 1936 and, therefore, a deduction is allowable in the income year ended 30 June 2008 for the full amount of expenditure incurred by the Grower for the Establishment Fee.

Sections 35-10 and 35-55 – deferral of losses from non-commercial business activities and the Commissioner's discretion

96. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis, 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.

97. 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.

98. 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

99. The operation of section 82KL of the ITAA 1936 depends, among other things, on the identification of a certain quantum of 'additional benefits(s)'. Insufficient 'additional benefits' will be provided to trigger the application of section 82KL. It will not apply to deny the deduction otherwise allowable under section 8-1 of the ITAA 1997.

Part IVA – general tax avoidance provisions

100. 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).

101. The FEA Plantations Project 2007 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 25 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.

102. 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 Wood. 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 expenditure
- carrying on a business
- commencement of business
- fee expenses
- forestry agreement
- interest expenses
- management fees
- non-commercial losses
- producing assessable income
- product rulings
- public rulings
- seasonally dependent agronomic activity
- stamp duty
- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters
- tax shelters project
- taxation administration

- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
- ITAA 1936 82KZMD
- ITAA 1936 82KZME
- ITAA 1936 82KZMF
- ITAA 1936 82KZMG
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
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- ITAA 1997 8-1
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- ITAA 1997 25-25(1)
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- ITAA 1997 Div 35
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- ITAA 1997 35-10(2)
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- Corporations Act 2001
- SISA 1993

Legislative references:

- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
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