


# ***PR 2008/42 - Income tax: Cool Climate Apricot Project - 2008 Growers***

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## Product Ruling

### Income tax: Cool Climate Apricot Project – 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**

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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 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 Cool Climate Apricot Project – 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. In this Product Ruling, those entities that can rely on the tax benefits set out in this Ruling are referred to as Growers.

3. 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 mentioned in paragraph 27 of this Ruling on or before 15 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;
- are accepted into this Project before the date of this Ruling or after 15 June 2008;
- participate in the scheme through offers made other than through the Product Disclosure Statement;
- who elect to market and sell the Apricots from their Apricot Lot in accordance with clause 9 of the Management Agreement; or
- are Cool Climate Investments Pty Ltd 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 27 to 67 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**

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9. This Product Ruling applies prospectively from 30 April 2008, the date this Product Ruling is made. It therefore applies only to the specified class of entities that enter into the scheme from 30 April 2008 until 15 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 this 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 the extent of those amendments, this Product Ruling will be superseded.

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.

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## Ruling

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### 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 below at paragraphs 27 to 67 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 and Tree Right that is on or before 15 June 2008.

### Small business concessions

20. From the 2007-08 income year, a range of concessions previously unavailable under the Simplified Tax System (STS), will be available to an entity if it carries on a business and satisfies the \$2 million aggregated turnover test (a 'small business entity').

21. A small business entity can choose the concessions that best suit its needs. Eligibility for some small business concessions is also dependent on satisfying some additional conditions. Because of these choices and the eligibility conditions the application of the small business concessions to Growers who qualify as a 'small business entity' is not able to be dealt with in this Ruling.

### Assessable Income

#### ***Sections 6-5 and 17-5***

22. That part of the gross sales proceeds from the Project attributable to the Grower's produce, less any GST payable on those proceeds (section 17-5), will be assessable income of the Grower under section 6-5.

### **Deductions for Initial Services Fee, Tree Right Fee, Orchard Maintenance Fee, Processing Costs, Marketing Fee and Variable Management Fee**

#### ***Section 8-1 and Division 27 of the ITAA 1997 and sections 82KZME and 82KZMF of the Income Tax Assessment Act 1936***

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

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<b>Fee Type</b>	<b>Year ending 30 June 2008</b>	<b>Year ending 30 June 2009</b>	<b>Year ending 30 June 2010</b>
<b>Initial Services Fee</b>	\$7,535 See Notes (i) and (ii)	Nil	Nil
<b>Tree Right Fee</b>	\$12 See Notes (i), (iv) and (v)	\$409 Indexed See Notes (i), (iv) and (v)	\$419 Indexed See Notes (i), (iv) and (v)
<b>Orchard Maintenance Fee</b>	Nil See Note (iii)	As incurred See Notes (i), (iii) and (iv)	\$3,901 See Notes (i), (iii) and (iv)
<b>Processing Costs</b>	Nil	As incurred (to the extent not already deducted from Gross Sale Proceeds). See Notes (i), (iv) and (v)	As incurred (to the extent not already deducted from Gross Sale Proceeds). See Notes (i), (iv) and (v)
<b>Marketing Fee</b>	Nil	As incurred (to the extent not already deducted from Gross Sale Proceeds). See Notes (i), (iv) and (v)	As incurred (to the extent not already deducted from Gross Sale Proceeds). See Notes (i), (iv) and (v)
<b>Variable Management Fee</b>	As incurred See Notes (i), (iv) and (v)	As incurred See Notes (i), (iv) and (v)	As incurred See Notes (i), (iv) and (v)

**Notes:**

- (i) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (ii) For the year ended 30 June 2008, the Initial Services Fee payable on Application is deductible to the extent shown in the table above in the year that it is incurred. The Initial Services Fee payable on Application is deductible in full under section 8-1.

- (iii) The Orchard Maintenance Fee payable on Application is a prepayment and not deductible in full in the year incurred. Deductions for these amounts must be determined using the formula in subsection 82KZMF(1) of the *Income Tax Assessment Act 1936* (ITAA 1936) (see paragraphs 78 to 87 of this Ruling). This provision operates to apportion expenditure over the eligible service period. The eligible service period extends from 1 July 2008 to 30 June 2010. Therefore, an amount of \$3,704 per Apricot Lot plus that sum which equals the Grower's Proportion of the Net Proceeds to Growers is deductible for the Orchard Maintenance Fee in the year ending 30 June 2009 and an amount of \$3,901 per Apricot Lot is deductible for the Orchard Maintenance Fee in the year ending 30 June 2010.
- (iv) Other than those discussed in Note (iii), this Ruling does not apply to Growers who choose to prepay fees, or who choose, or who are required to prepay interest under a loan agreement. Amounts that are prepaid for a period that extends beyond the income year in which the expenditure is incurred may be subject to the prepayment provisions in sections 82KZME to 82KZMF of the ITAA 1936. Any Grower who prepays such amounts may request a private ruling on the taxation consequences of their participation in the Project.
- (v) The Tree Right Fee, Processing Costs, Marketing Fee and Variable Management Fee are deductible in the year that they are incurred under section 8-1.

### **Deductions for capital expenditure**

#### ***Division 40***

24. A Grower will also be entitled to tax deductions relating to the establishment of the Trees and the Processing Fee if the Grower elected to pay the Initial Services Fee under the Terms Payment Option. All deductions shown in the following table are determined under Division 40:

<b>Fee Type</b>	<b>Year ending 30 June 2008</b>	<b>Year ending 30 June 2009</b>	<b>Year ending 30 June 2010</b>
<b>Establishment of the Apricot Trees</b>	See Notes (i) and (vi)	See Notes (i) and (vi)	See Notes (i) and (vi)
<b>Processing Fee under the Terms Payment Option</b>	Must be calculated  See Notes (i) and (vii)	Must be calculated  See Notes (i) and (vii)	Must be calculated  See Notes (i) and (vii)

## Notes:

- (vi) Apricot Trees are a 'horticultural plant' as defined in subsection 40-520(2). As Growers hold a Tree Right over the land, one of the conditions in subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the Trees is determined using the formula in section 40-545 and is based on the capital expenditure that is attributable to their establishment. If the Trees have an 'effective life' of 10 to fewer than 13 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 17%. The deduction is allowable when the Trees enter their first commercial season (item 2 of section 40-530). The Manager will inform Growers of when the Trees enter their first commercial season and the amount that may be claimed.
- (vii) Under section 40-880 the Processing Fee for the Terms Payment Option is deductible on a straight line basis over five income years (see paragraphs 76 to 77 of this Ruling).

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

### ***Section 35-55 – exercise of Commissioner's discretion***

25. A Grower who is an individual accepted into the Project by 15 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 below, the Commissioner will exercise the discretion in paragraph 35-55(1)(b) for Growers for the income years ended **30 June 2008 to 30 June 2010**. 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.

## **Recouped expenditure and anti-avoidance provisions**

### ***Section 82KL and Part IVA***

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

- section 82KL does not apply to deny the deductions otherwise allowable; and
- the relevant provisions in Part IVA will not be applied to cancel a tax benefit obtained under a tax law dealt with in this Ruling.

## Scheme

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

- Application for a Product Ruling as constituted by documents provided on 19 October 2007 and additional correspondence dated 17 December 2007, 20 December 2007, 21 December 2007, 30 January 2008, 4 February 2008, 4 March 2008, 31 March 2008, 9 April 2008, 11 April 2008, 15 April 2008, 17 April 2008, 18 April 2008, 21 April 2008, 22 April 2008 and 23 April 2008;
- Draft Product Disclosure Statement (2008 Growers) received on 23 April 2008 (PDS);
- Draft **Application Form** which forms part of the PDS to be entered into by each Grower, received on 23 April 2008;
- Draft **Constitution** of Cool Climate Apricot Project received on 19 October 2007;
- Rules for Cool Climate Apricot Project dated 30 June 2006;
- Draft **Management Agreement** between Primary Securities Ltd (as Responsible Entity) and a Grower, received on 22 April 2008;
- Compliance Plan for Cool Climate Apricot Project made by Primary Securities Ltd (as Responsible Entity), dated 20 January 2006;
- Draft Sub-Management Agreement between Primary Securities Ltd (as Responsible Entity) and Cool Climate Investments Pty Ltd (as Manager), received on 19 October 2007;
- Draft Orchard Management Agreement between Primary Securities Ltd (as Responsible Entity), Cool Climate Investments Pty Ltd (as Manager) and the Orchard Manager, received on 11 April 2008;
- Responsible Entity Services Agreement between Primary Securities Ltd (as Responsible Entity) and Cool Climate Investments Pty Ltd (as Manager), dated 20 March 2006;
- Draft **Tree Right** between Primary Securities Ltd (as Responsible Entity) and a Grower, received on 31 March 2008;

- Custodian Agreement between Primary Securities Ltd (as Responsible Entity) and the Custodian, dated 30 January 2006;
- Draft Infrastructure and Planting Agreement between Cool Climate Investments Pty Ltd (as Manager) and the Orchard Manager, received on 31 March 2008;
- Lease Agreement between the Lessor and the Facilitators (as Lessees) in relation to land described in the agreement as Register Volume 109388, Folio 3, received on 31 March 2008 (Facilitating Lease);
- Sub-Lease Agreement between the Facilitators (as Lessors) and Cool Climate Investments Pty Ltd (as Lessee) in relation to part of the land described in the agreement as Register Volume 109388, Folio 3, received on 31 March 2008 (Qew Lease);
- Lease Agreement between the landowner (as Lessor) and Cool Climate Investments Pty Ltd (as Lessee) in relation to land described in the Sub-Lease to RE as the New Property and further described in that agreement as Register Volume 144678, Folio 1, received on 31 March 2008 (Head Lease);
- Sub-Lease Agreement between Cool Climate Investments Pty Ltd (as Sub-Lessor) and Primary Securities Ltd (as Sub-Lessee) in relation to part of the land described in the agreement as Register Volume 109388, Folio 3 and land described in the agreement as Register Volume 144678, Folio 1, received on 31 March 2008 (Sub-Lease to RE);
- Draft Apricot Offtake Agreement between Primary Securities Ltd (as Responsible Entity), Cool Climate Investments Pty Ltd (as Manager) and the Orchard Manager, received on 19 October 2007;
- Deed of Subordination between Cool Climate Investments Pty Ltd (as Borrower), the Lender and Primary Securities Ltd (as Responsible Entity), dated 31 May 2006; and
- Draft **2008 Terms Agreement** between Primary Securities Ltd (as Responsible Entity) and a Grower, received on 15 April 2008 (Terms Agreement).

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

28. 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.

29. All Australian Securities and Investment Commission (ASIC) requirements are, or will be, complied with for the term of the agreements. The effect of these agreements is summarised as follows.

### Overview

30. Following is a summary of the scheme:

Location	Fingerpost Road, Campania, Southern Tasmania
Type of business to be carried on by each participant	Cultivating Apricot trees for the purpose of harvesting and selling the produce
Number of hectares offered for cultivation	Approximately 14.9 hectares
Size of each Apricot Lot	0.10 hectare of which approximately 0.0025 hectare will be on Qew Property and 0.0975 hectare will be on New Property
Minimum allocation per Grower	2 Apricot Lots
Number of Trees per Apricot Lot	Approximately 138 Trees (approximately 3 Trees on Qew Property and approximately 135 Trees on the New Property)
Minimum subscription	No minimum subscription
Term of the Project	Approximately 18 years
Initial cost per Apricot Lot	\$8,647
Initial cost per hectare	\$86,470
Ongoing costs	<ul style="list-style-type: none"> <li>• Orchard Maintenance Fee</li> <li>• Tree Right Fee</li> <li>• Processing Costs</li> <li>• Marketing Fee</li> <li>• Variable Management Fee</li> <li>• Deferred Management Fee payable in respect of Years 1 and 2 at a rate of 2% of Net Harvest Proceeds for each year, that is a total of 4% per year commencing in Year 7 and continuing for 10 years</li> <li>• Performance Incentive commencing in Year 5</li> </ul>

31. The Project is registered as a managed investment scheme under the *Corporations Act 2001*. Primary Securities Ltd has been issued with an Australian Financial Service Licence, number 224107 and will be the Responsible Entity for the Project.
32. An offer to participate in the Project will be made through a PDS for 149 Apricot Lots which comprises a total of 14.9 hectares. Participants will be invited to subscribe in the Project on or before 15 June 2008. Each entity will become a Grower of Apricots by acquiring a Tree Right over a 0.10 hectare Apricot Lot, of which 0.0025 hectare will be on Qew Property and 0.0975 hectare will be on New Property.
33. To participate in the Project participants must complete the Application Form in the PDS and pay the Application Fee in accordance with the payment Schedule outlined in the PDS. The Application Fee will be banked into the Custodian's trust account. These monies will be released to the Responsible Entity.
34. A Grower accepted on or before 15 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 on or before 15 June 2008.**
35. Each Grower will enter into a Tree Right with the Responsible Entity. The Tree Right will comprise contractual rights in relation a parcel of land of 0.10 hectare called an Apricot Lot.
36. Each Apricot Lot will comprise of 0.0025 hectare of fully established Trees situated within the 'Qew Property' and 0.0975 hectare which will be situated within the 'New Property', the Trees for which will be planted before 15 June 2008.
37. Each Grower will also enter into a Management Agreement to contract with the Responsible Entity to provide the Initial Services and undertake services related to Apricot Farming and Processing. The Responsible Entity will also arrange to market and sell the Apricots.
38. The Responsible Entity will appoint the Manager to perform the Apricot Farming, Processing and marketing and selling of the Apricots. The Manager will, in turn, sub-contract the Orchard Manager to perform most of these responsibilities.

## Constitution

39. The Constitution for the Project sets out the general functions, powers and duties under which the Responsible Entity agrees to act for the Growers and to manage the Project. The Tree Right and the Management Agreement are Schedules to the Constitution. These Agreements will be executed by or on behalf of each Grower who has signed the Application Form and Power of Attorney attached to the PDS and who is accepted into the Project on or before 15 June 2008. Note that this Ruling only applies to an entity which is accepted to participate in the Project on or before 15 June 2008. After acceptance and execution of the agreements, Growers are bound by the Constitution by virtue of their participation in the Project.

40. Upon acceptance of an Application, the Responsible Entity will allocate the Apricot Lot(s) to the Grower and contract the Grower to the Tree Right and Management Agreement in accordance with clause 6.

41. The Responsible Entity is deemed to have received the Application Fee as fees on acceptance of an Application according to clause 3.5 and may invest all or part of the Application money and Receipts according to clause 6.

42. Among other things the Constitution sets out in detail the following:

- general functions, powers and duties, clauses 6 to 9;
- deal with Receipts and other money in the Trust Account of the Grower, clause 11;
- complaints, clause 12;
- withdrawal from the Project, and buy-back or re-purchase of any Tree Right, clause 13;
- termination, clause 14;
- payments to Growers, clause 19; and
- compliance with rules laid down by the Responsible Entity, clause 22.

### **Custodian Agreement**

43. The Custodian is to hold the Application Fee and Project Property as agent for the Responsible Entity in its capacity as a trustee for Applicants or Growers. Further, it will observe all of the usual duties and obligations of an agent acting in the best interest of its principal and in a professional and business like manner, according to clause 6.

### **Compliance Plan**

44. As required by the *Corporations Act 2001*, 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 interests of Growers are protected.

### **Sub-Lease to RE**

45. The Manager will lease both the New Property and the Qew Property under the Head Lease and Qew Lease respectively. Under the Sub-Lease to RE, the Manager has entered into a sub-lease with the Responsible Entity granting various exclusive and non-exclusive rights over the land as set out in clause 2.

46. All leases have been registered against the relevant titles.

47. The Sub-Lessor has carried out all works and installed all infrastructure necessary for the establishment of the Project on the New Property, clause 5.4. The Sub-Lessor will plant Trees on the New Property to a density of 138 Trees per Apricot Lot, being 3 Trees already existing on the Qew Property, 135 Trees on the New Property to be planted before Allotment of Apricot Lots to Growers.

## **Tree Right**

48. Growers participating in the Project will enter into a Tree Right with the Responsible Entity for the term of the Project. The Responsible Entity will grant to each Grower Tree Rights over the Apricot Lot which include the following under clause 2:

- access to the Apricot Lot;
- an exclusive right to access, use and enjoy the benefit of the Trees;
- an exclusive right to harvest the Apricots;
- an exclusive right to take all right, title and interest in the Apricots; and
- access to and use of the Orchard infrastructure, plant and equipment.

49. Other rights and obligations of the Grower and of the Responsible Entity are set out in clauses 2 to 6.

50. Under clause 4.1, the Responsible Entity is entitled to the Tree Right Fee as described in clause 1.1 and Part 5 of the Schedule. In respect of the period from the Commencement Date to 30 June 2008, the Tree Right Fee will be included in the Application Fee. In respect of the years ended 30 June 2009 and following, the Tree Right Fee will be invoiced annually by 31 October.

51. After 30 June 2010, the Tree Right Fee may be bought into line with the Tree Right Fee for Growers in previous year's projects.

52. If Trees are destroyed or materially damaged, or a Mineral or Petroleum Lease is established over the Apricot Lots, or the Grower and Responsible Entity agree that it is no longer viable to carry out Apricot Farming then the parties may terminate the obligations created by the Tree Right, clause 10.

## **Management Agreement**

53. A Management Agreement is entered into between the Responsible Entity and each Grower, under which the Responsible Entity agrees to cause to be carried out during the term, Apricot Farming on the Apricot Lots, Processing and Sale of the Apricots.

54. The parties also agree that the Responsible Entity will provide the Initial Services in respect of each Grower's Apricot Lot. These services include:

- checking that the training wire or mesh or other suitable support structure between the strainer posts is suitable for Apricot Farming;
- reviewing the positioning of newly planted Trees;
- cultivating, tending, culling, watering, pruning, thinning, replanting, fertilising, spraying and otherwise caring for the Trees;
- inspection of the above ground components of the Irrigation System; and
- inspection and supervision of Initial Services that are carried out by subcontractors.

55. The Responsible Entity must provide the Initial Services during the period from Allotment to 30 June 2008. Payment of the Application Fee constitutes full payment for these services to be carried out by 30 June 2008.

56. The Responsible Entity will perform the Initial Services and Apricot Farming in accordance with good horticultural and agricultural practices and in accordance with the requirements of clause 5.6

57. The Responsible Entity will prepare by 30 June 2008 a written report to be forwarded to each Grower confirming that their Apricot Lots have been established or substantially established in accordance with the Management Agreement, and a report concerning the potential market for the Apricots. The Responsible Entity will also provide a written report to each Grower by 30 September each year in relation to the state of the Orchard and the report from the Horticultural Expert, clause 12.

58. The Responsible Entity is entitled to an annual Management Fee as set out in Part 2 of the Schedule in consideration for the performance of its obligations.

59. The Grower appoints the Responsible Entity to sell (and to appoint the Orchard Manager to sell) Apricots harvested from the Grower's Trees for the highest price practicable having regard to circumstances at the time, clause 8.

60. The Responsible Entity will be responsible for insuring the Orchard against public risk. The Responsible Entity is also required to keep insurance on behalf of the Growers insuring the Apricot Lots against damage or theft of the Apricots, damage to picked Apricots resulting from cool-store breakdown or other plant breakdown, loss due to fortuitous circumstances, product liability and other such risks in respect of the Apricot Lots and Apricots in a manner consistent with the prevailing usual industry practice, clause 7.

## **Pooling of Apricots and distribution of proceeds**

61. The Management Agreement sets out provisions relating to the pooling of Grower's Apricots and the distribution of proceeds from that sale. This Product Ruling only applies where the following principles apply to those pooling and distribution arrangements:

- only Growers who have contributed Apricots from a Harvest to the pool are entitled to benefit from distributions from the proceeds of sale; and
- Apricots can only be pooled with the Apricots of Growers accepted to participate in the Project on or before 15 June 2008.

## **Project Fees**

62. The Grower must pay an Application Fee of \$8,647 per Apricot Lot payable on Application which will be applied towards the following:

- \$7,535 Initial Services Fee for services to be provided from the Commencement Date to 30 June 2008;
- \$12 Tree Right Fee for the period from the Allotment to 30 June 2008; and
- \$1,100 prepaid Orchard Maintenance Fee for services to be provided in the period 1 July 2008 to 30 June 2010.

63. Under clause 4 and Part 2 of the Schedule to the Management Agreement and clause 4 and Part 5 of the Schedule to the Tree Right each Grower will make the following other payments per Apricot Lot.

*For the year ending 30 June 2009:*

- \$3,154 Orchard Maintenance Fee plus that sum which equals the Grower's Proportion of the Net Proceeds to Growers payable out of Net Proceeds to Growers; and
- \$409 (indexed) Tree Right Fee.

*For the year ending 30 June 2010:*

- \$3,351 Orchard Maintenance Fee;
- \$419 (indexed) Tree Right Fee;
- Grower's Proportion of Processing Costs (to the extent not already deducted from Gross Sale Proceeds);
- Marketing Fee capped at \$152.90 (indexed). For the Financial Year up to and including Year 6, the fee is that proportion of the Marketing Fee as the actual or anticipated harvest yield for the Financial Year bears to peak forecast yield;

- Variable Management Fee being the Grower's Proportion of that sum that equals 28% of the Net Proceeds to Growers, less a Base Management Fee and an amount equal to the Tree Right Fee payable out of Gross Sale Proceeds; and
- Processing Costs (to the extent not already deducted from Gross Sale Proceeds), and the Marketing Fee are payable out of the balance of the Gross Sale Proceeds

*For the year ending 30 June 2011, the same costs as for the year ending 30 June 2010 (indexed where applicable), except for:*

- the Grower's Proportion of the budgeted costs, Orchard Maintenance Fee;
- \$430 (indexed) Tree Right Fee; and
- the years ending 30 June 2015 and following a Deferred Management Fee payable in respect of Years 1 and 2 at a rate of 2% of Net Harvest Proceeds for each year, that is a total of 4% per year commencing in Year 7 and continuing for 10 years.

64. Project agreements indicate, and the Manager has confirmed, that where Gross Sale Proceeds are insufficient, Growers will be invoiced for the shortfall.

### **Finance**

65. Growers can fund their participation in the Project as follows:

- from their own financial resources;
- borrow from an independent lender external to the Project; or
- under a Terms Agreement with Primary Securities Ltd.

### **Terms Agreement**

66. If Primary Securities Ltd accepts that the Application Fee can be paid under a Terms Agreement. The Grower must complete a Terms Application and Direct Debit Authority. The Grower will be required to pay their Application Fee as follows:

- an additional fee of \$824 for processing the Terms Payment Option;
- Growers must pay a deposit of \$1,431 on Application;
- the balance of the Application Fee and the Processing Fee of \$8,040 by 12 monthly payments of \$670 (the first Monthly Instalment is due on the last Business Day of the month in which Allotment occurs);

- Primary Securities Ltd will take security over the Grower's Apricot Lot(s); and
- there will be no interest levied to the Grower, unless instalments are not paid on time, then Primary Securities Ltd may charge Interest, calculated on a daily basis from the due date until payment is received.

67. 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 are involved or become involved in the provision of finance to any Grower in the Project.

## **Appendix 1 – Explanation**

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

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

68. For the amounts set out in paragraph 23 of this Ruling, to constitute allowable deductions the Grower's horticulture activities as a participant in the Cool Climate Apricot Project – 2008 Growers must amount to the carrying on of a business of primary production.

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

70. 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?

71. Taxation Ruling TR 2000/8 Income tax: investment schemes, particularly paragraph 89 of this Ruling, is more specific to arrangements such as the Cool Climate Apricot Project – 2008 Growers. 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.

72. Having applied these principles to the arrangement set out above, a Grower in the Cool Climate Apricot Project – 2008 Growers is accepted to be carrying on a business of growing and harvesting Apricots for sale.

### **Deductibility of the Initial Services Fee, Tree Right Fee, Orchard Maintenance Fee, Processing Costs, Marketing Fee and Variable Management Fee**

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

73. The Initial Services Fee, Tree Right Fee, Orchard Maintenance Fee, Processing Costs, Marketing Fee and Variable Management Fee 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 Initial Services Fee, Tree Right Fee, Orchard Maintenance Fee, Processing Costs, Marketing Fee and Variable Management Fee (see paragraphs 49 to 51 of TR 2000/8).

74. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply. Provided that the prepayment provisions do not apply (see paragraphs 78 to 87 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).

75. The deductibility of interest incurred by Growers who finance their participation in the Project 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.

## **Processing Fee payable under a Terms Payment Agreement**

### ***Section 40-880***

76. Growers who elect to pay their Grower's contribution under the Terms Payment Agreement must pay a Processing Fee of \$824. This expenditure does not constitute a borrowing expense and is therefore not deductible under section 25-25. As it is capital in nature it is also not deductible under section 8-1.

77. However, section 40-880 will allow the Processing Fee to be deducted on a straight line basis over five income years. Section 40-880 applies to capital expenditure that is incurred in relation to a business and which is not taken into account elsewhere or denied deductibility under another provision of income tax law.

## **Prepayment provisions**

### ***Sections 82KZL to 82KZMF***

78. The prepayment provisions contained in Subdivision H of Division 3 of Part III of the ITAA 1936 affect the timing of deductions for certain prepaid expenditure. These provisions apply to certain expenditure incurred under an agreement in return for the doing of a thing under the agreement (for example, the performance of management services or the leasing of land) that will not be wholly done within the same year of income as the year in which the expenditure is incurred. If expenditure is incurred to cover the provision of services to be provided within the same year, then it is not expenditure to which the prepayment rules apply.

79. For this Project, only section 82KZL of the ITAA 1936 (an interpretive provision) and sections 82KZME and 82KZMF of the ITAA 1936 are relevant. Where the requirements of sections 82KZME and 82KZMF of the ITAA 1936 are met, taxpayers determine deductions for prepaid expenditure under section 82KZMF of the ITAA 1936 using the formula in subsection 82KZMF(1) of the ITAA 1936.

**Sections 82KZME and 82KZMF**

80. Where the requirements of subsections 82KZME(2) and (3) of the ITAA 1936 are met, the formula in subsection 82KZMF(1) of the ITAA 1936 (see paragraph 84 of this Ruling) will apply to apportion expenditure that is otherwise deductible under section 8-1. The requirements of subsection 82KZME(2) of the ITAA 1936 will be met if expenditure is incurred by a taxpayer in return for the doing of a thing that is not to be wholly done within the year the expenditure is made. The year in which such expenditure is incurred is called the 'expenditure year' (subsection 82KZME(1) of the ITAA 1936).

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

- (i) the taxpayer's allowable deductions under the agreement for the 'expenditure year' exceed any assessable income attributable to the agreement for that year;
- (ii) the taxpayer does not have effective day to day control over the operation of the agreement. That is, the significant aspects of the scheme are managed by someone other than the taxpayer; and
- (iii) either:
  - (a) there is more than one participant in the agreement in the same capacity as the taxpayer; or
  - (b) the entity who promotes, arranges or manages the agreement (or an associate of that entity) promotes similar agreements for other taxpayers.

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

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

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

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

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

*Application of the prepayment provisions to this Project*

86. The expenditure incurred by a Grower in the Project for the Orchard Maintenance Fee paid on Application meets the requirements of subsections 82KZME(1) and (2) of the ITAA 1936 and is incurred under an 'agreement' as described in subsection 82KZME(3) of the ITAA 1936. Therefore, unless one of the exceptions to section 82KZME of the ITAA 1936 applies, the amount and timing of tax deductions for those fees are determined under section 82KZMF of the ITAA 1936.

87. The prepaid Orchard Maintenance Fee incurred by each Grower does not fall within any of the five exceptions to section 82KZME of the ITAA 1936. Therefore, the deduction for each year is determined using the formula in subsection 82KZMF(1) of the ITAA 1936. Section 82KZMF of the ITAA 1936 apportions the deduction for prepaid Orchard Maintenance Fee over the period that the services for which the prepayment is made are provided.

**Expenditure of a capital nature**

***Division 40***

88. Any part of the expenditure of a Grower that is attributable to acquiring an asset or advantage of an enduring kind is generally capital or capital in nature and will not be an allowable deduction under section 8-1. In this Project, expenditure attributable to the establishment of the Trees is of a capital nature.

**Terms Payment Option Processing Fee*****Section 40-880***

89. Growers who elect to pay the Initial Services Fee under the Terms Agreement option must pay a Processing Fee of \$824. This expenditure does not constitute a borrowing expense and is therefore not deductible under section 25-25. As it is capital in nature it is also not deductible under section 8-1.

90. However, section 40-880 will allow the Processing Fee to be deducted on a straight line basis over five income years. Section 40-880 applies to capital expenditure that is incurred in relation to a business and which is not taken into account elsewhere or denied deductibility under another provision of income tax law.

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

91. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income years 30 June 2008 to 30 June 2010, 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 apricot industry, a Grower’s business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

92. A Grower who would otherwise be required to defer a loss arising from their participation in the Project under subsection 35-10(2) until a later income year is able to offset that loss against their other assessable income.

93. The exercise of the Commissioner’s discretion under paragraph 35-55(1)(b) is conditional on the Project being carried on in the manner described in this Ruling during the income years specified. If the Project is carried out in a materially different way to that described in the Ruling a Grower will need to apply for a private ruling on the application of section 35-55 to those changed circumstances.

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

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

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

95. For Part IVA of the ITAA 1936 to apply there must be a 'scheme' (section 177A), a 'tax benefit' (section 177C) and a dominant purpose of entering into the scheme to obtain a tax benefit (section 177D).

96. The Cool Climate Apricot Project – 2008 Growers will be a 'scheme'. A Grower will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 23 to 26 of this Ruling that would not have been obtained but for the scheme. However, it is not possible to conclude the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

97. Each Grower to whom this Ruling applies intends to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the Apricots. There are no facts that would suggest that a Grower has the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There is no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing at arm's length or, if any parties are not dealing at arm's length, that any adverse tax consequences result. Further, having regard to the factors to be considered under paragraph 177D(b) of the ITAA 1936 it cannot be concluded, on the information available, that participants will enter into the scheme for the dominant purpose of obtaining a tax benefit.

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

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

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## References

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*Previous draft:*

Not previously issued as a draft

*Related Rulings/Determinations:*

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

*Subject references:*

- carrying on a business
- commencement of business
- management fee expenses
- non-commercial losses
- primary production
- primary production expenses
- producing assessable income
- product rulings
- public rulings
- schemes and shams
- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters
- taxation administration

*Legislative references:*

- ITAA 1997 6-5
- ITAA 1997 8-1
- ITAA 1997 17-5
- ITAA 1997 25-25
- ITAA 1997 25-25(6)
- ITAA 1997 Div 27
- ITAA 1997 Div 35
- ITAA 1997 35-10
- ITAA 1997 35-10(2)
- ITAA 1997 35-55
- ITAA 1997 35-55(1)(b)
- ITAA 1997 Div 40
- ITAA 1997 40-515
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- ITAA 1997 40-520(2)
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- ITAA 1997 40-530
- ITAA 1997 40-545
- ITAA 1997 40-880
- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
- ITAA 1936 82KZMD
- ITAA 1936 82KZME
- ITAA 1936 82KZME(1)
- ITAA 1936 82KZME(2)
- ITAA 1936 82KZME(3)
- ITAA 1936 82KZME(4)
- ITAA 1936 82KZME(7)
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