


CR 2007/49 - Income tax: treatment of payments received under the Securing our Fishing Future package: * Onshore Business Development Assistance * Business Advice Assistance

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Class Ruling

Income tax: treatment of payments received under the *Securing our Fishing Future* package:

- Onshore Business Development Assistance
- Business Advice Assistance

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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 (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided 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.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 15-10 of the ITAA 1997;
- section 104-25 of the ITAA 1997;
- paragraph 118-37(2)(a) of the ITAA 1997; and
- Division 392 of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1997 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies is applicants who applied for and received payments under the Onshore Business Development Assistance and/or Business Advice Assistance components of the *Securing our Fishing Future* package.

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 13 to 35 of this Ruling.

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

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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Date of effect

8. This Ruling applies from 1 July 2006 to 30 June 2010. However, the Ruling continues to apply after this date to all entities within the specified class who entered into the specified scheme during the term of the Ruling, subject to there being no change in the scheme or in the entities involved in the scheme.

9. The Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

10. If this Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

11. If this Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

12. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Scheme

13. The following description of the scheme is based on information provided by the applicant. The following documents or relevant parts of them, form part of and are to be read with the description.

- Application for Class Ruling from the Department of Agriculture, Fisheries and Forestry (DAFF) dated 30 January 2006 and supplementary correspondence from DAFF dated 24 October 2006; and
- DAFF Securing our Fishing Future – Onshore Business Assistance Guidelines.

14. The *Securing our Fishing Future package* (Package), announced by the Australian Government on 23 November 2005, is a major structural adjustment package for the Australian fishing industry designed to reduce fishing capacity and better position the industry to be profitable and self-adjust in the future. Onshore Business Assistance is one of the components of the Package. Onshore Business Assistance consists of:

- Onshore Business Development Assistance; and
- Onshore Business Exit Assistance.

15. This Class Ruling deals with Onshore Business Development Assistance and related Business Advice Assistance. Onshore Business Exit Assistance and related Business Advice Assistance are dealt with in a separate Class Ruling.

16. The Australian Government's overall objective for Onshore Business Development Assistance is to help offset the impacts of reduced fishing activity on directly affected onshore businesses. Specifically, the Onshore Business Development Assistance is designed to strengthen the onshore business sector by helping directly affected onshore businesses manage the impact of the reduction in fishing activity.

17. Onshore Business Development Assistance is a competitive grants programme and will target those projects that offer the greatest potential for strengthening the onshore sector that is reliant on Commonwealth managed fisheries.

18. DAFF makes a formal determination of the eligibility of an applicant for Onshore Business Development Assistance and the level of assistance that may be granted.

19. Onshore Business Development Assistance is proposed for eligible existing businesses who still envisage a prosperous future in the onshore sector to restructure their operations to enhance their future viability.

20. To be eligible for Onshore Business Development Assistance the applicant must be:

- an onshore business that has experienced significant negative impacts or has been made unviable as a consequence of the reductions in fishing activity; or
- a business that leased a fishing concession (fishing concession lessee) that can demonstrate it is unable to obtain a replacement for the leased concession lost as a result of it being surrendered in the Concession Buyback (DAFF Request for Tender (RFT) 47/06 or DAFF RFT 75/06).

21. Owners of a business that was created or acquired after the announcement of the Package on 23 November 2005 are ineligible for Onshore Business Development Assistance. However, a person who became legally bound to acquire or develop a business prior to 23 November 2005, which came into effect after that date, will be eligible to apply for Onshore Business Development Assistance.

22. Eligible onshore businesses must satisfy 3 eligibility tests. The business must be:

- directly impacted;
- otherwise viable; and
- significantly impacted.

First eligibility test: directly impacted business

23. To be eligible for Onshore Business Development Assistance a business must have:

- been directly involved in the wholesaling, retailing, exporting or processing of seafood from Commonwealth-managed fisheries on 23 November 2005; or
- been directly dependant on the Commonwealth fishing sector on 23 November 2005, and be able to demonstrate the proportion of its income that is, or was derived from the supply of goods and services to the Commonwealth fishing sector.

Second eligibility test: otherwise viable business

24. To be eligible for Onshore Business Development Assistance a business would have to have good prospects of being viable if it were not for the reductions in fishing activity. Appendix 1 to the Securing our Fishing Future – Onshore Business Assistance Guidelines contains information about how to demonstrate business viability.

Third eligibility test: significantly impacted business

25. To be eligible for Onshore Business Development Assistance a business needs to demonstrate that it has been, or will be significantly impacted by the reductions in fishing activity. Applicants must reasonably demonstrate how the reductions in fishing activity have either:

- reduced the business's final surplus¹ by more than a third; or
- made the entire operation unviable by making its total earnings before depreciation, interest and tax less than their financial commitments (including interest and principal repayments) and plant replacement.

¹ 'Final surplus' is defined in Appendix 3 of the DAFF Securing our Fishing Future – Onshore Business Assistance Guidelines as total operating income less total operating expenses (excluding depreciation and interest), less plant replacement and servicing and repayment of debt.

26. The amount of Onshore Business Development Assistance available to an eligible business is equivalent to three years of final surplus that was lost because of the reductions in fishing activity, up to a maximum of \$250,000. Assistance in excess of the equivalent of three years of lost financial surplus may also be granted on a case by case basis to applicants whose businesses are generally managed as non-profit businesses. This amount will be up to a limit of \$250,000. Guidance on how to calculate lost final surplus is at Appendix 1 to the Securing our Fishing Future - Onshore Business Assistance Guidelines.

27. A single Onshore Business Development Assistance application from a group of eligible applicants will be accepted. In such circumstances, the guidelines will be applied as if each applicant is making an individual application. The total amount of Onshore Business Development Assistance applied for by the group of eligible applicants may exceed the individual assistance threshold outlined in section 5 of the Onshore Business Assistance Guidelines.

28. Fishing concession lessees may be eligible for Onshore Business Development Assistance to help manage the impacts of reduced fishing activity on other parts of their operation that were not directly reliant on the concession lease.

29. Onshore Business Development Assistance applicants must develop a proposal that outlines how the business will be restructured to help it to manage the impacts of the reductions in fishing activity. The proposal will contain an anticipated itemised amount of the cost of the restructuring.

30. Examples of appropriate uses of Onshore Business Development Assistance include:

- introducing new processing systems or technology;
- developing new product lines;
- rationalising inefficient processes or uneconomic product lines;
- improving business productivity; and
- developing value adding activities.

31. Successful applicants will enter into a funding agreement with the Commonwealth which includes a negotiated schedule of payments linked to agreed milestones in the restructuring of the business. An applicant may submit invoices to the DAFF in line with the agreed milestones for acquittal against receipts. Alternatively, with prior agreement of the DAFF, the applicant may submit quotes together with an authorisation to pay a preferred supplier that the department will then pay directly for work to be undertaken on behalf of the applicant.

32. Onshore Business Development Assistance applicants may seek funding to reimburse the cost of any activities in their proposal that have already been undertaken directly in response to the reductions in fishing activity provided those activities were undertaken after 23 November 2005.

33. Applicants must lodge an application by the closing date. Onshore Business Development Assistance will consist of two rounds. Applications for Round 1 close on 12 January 2007 and Round 2 closes on 4 May 2007.

Business Advice Assistance

34. Business Advice Assistance is available to help cover the costs of obtaining independent professional advice in preparing an Onshore Business Development Assistance application. Under the Business Advice Assistance component of the package up to \$1,500 may be payable to reimburse eligible applicants, or payable directly to the provider of the business advice, to meet the cost of obtaining advice directly related to the preparation of an Onshore Business Development Assistance application. Applicants must apply separately for Business Advice Assistance and must submit fully itemised tax invoices to the DAFF.

35. Business Advice Assistance will only be paid to an applicant that submits an application for Onshore Business Assistance and is deemed eligible by DAFF or the decision maker. Business Advice Assistance will not be paid if the potential applicant decides not to apply for Onshore Business Assistance.

Ruling

Onshore Business Development Assistance

Section 6-5 – income according to ordinary concepts

36. A payment received under the Onshore Business Development Assistance component of the Package is not income according to ordinary concepts. The receipt is not assessable income under section 6-5.

Section 15-10 – bounty or subsidy

37. A payment received under the Onshore Business Development Assistance component of the Package to assist with the capital costs of restructuring a business is a bounty or subsidy that is received in relation to carrying on a business. The receipt is assessable income under section 15-10.

Capital gains tax

38. CGT event C2 under section 104-25 happens to the entitlement to receive the Onshore Business Development Assistance when the entitlement is satisfied.

39. However, any capital gain or capital loss made as a result of a payment of Onshore Business Development Assistance is disregarded under paragraph 118-37(2)(a).

40. To the extent that the Onshore Business Development Assistance relates to the acquisition of a new CGT asset, it is a recoupment of the cost of acquiring that asset. However it does not reduce the cost base of the new asset because the amount of the recoupment is included in assessable income.

Business Advice Assistance

Section 6-5 – income according to ordinary concepts

41. A payment received under the Business Advice Assistance component of the Package is not income according to ordinary concepts. The receipt is not assessable income under section 6-5.

Section 15-10 – bounty or subsidy

42. A payment received under the Business Advice Assistance component of the Package is a bounty or subsidy that is received in relation to carrying on a business. The receipt is assessable income under section 15-10.

Capital gains tax

43. The payment of Business Advice Assistance represents a recoupment of expenditure incurred in applying for Onshore Business Development Assistance.

44. However, the recoupment of the amount of the Business Advice Assistance does not reduce the cost base of the entitlement to receive the Onshore Business Development Assistance.

Primary production income

45. A payment received under the Onshore Business Development Assistance and Business Advice Assistance components of the Package by an eligible onshore business is not assessable primary production income for the purposes of working out the 'averaging' adjustment under Division 392 unless the onshore business is a primary production business.

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.*

Onshore Business Development Assistance

Section 6-5 – income according to ordinary concepts

46. Subsection 6-5(1) provides that an amount is included in assessable income if it is income according to ordinary concepts (ordinary income). However, as there is no definition of 'ordinary income' in income tax legislation it is necessary to apply principles developed by the courts to the facts of a particular case.

47. Whether or not a particular receipt is ordinary income depends on its character in the hands of the recipient.²

48. In *GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation*³ (*GP International Pipecoaters*), the Full High Court stated:

To determine whether a receipt is of an income or of a capital nature, various factors may be relevant. Sometimes the character of receipts will be revealed most clearly by their periodicity, regularity or recurrence; sometimes, by the character of a right or thing disposed of in exchange for the receipt; sometimes, by the scope of the transaction, venture or business in or by reason of which money is received and by the recipient's purpose in engaging in the transaction, venture or business.

49. In considering whether a grant under the *Industrial Research and Development Grants Act 1967* was income according to ordinary concepts, Mahoney J in *Reckitt & Colman Pty Ltd v. FC of T*⁴ (*Reckitt & Colman*), said that the Court must examine the nature of the payment itself and the relationship of it to the activities, actual or potential of the recipient. A payment which is seen as provided for a purpose which is not part of the recipient's trade will not be income in nature (*Reckitt & Colman*). A subsidy to replenish or augment the recipient's capital is not income under ordinary concepts because it is not a product or incident of the recipient's income producing activity (*GP International Pipecoaters*).

² *Scott v. FC of T* (1966) 117 CLR 514, *Hayes v. FC of T* (1956) 96 CLR 47 and *Federal Coke Co Pty Ltd v. FC of T* (1977) 7 ATR 519; 77 ATC 4255.

³ (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1.

⁴ (1974) 74 ATC 4185; 4 ATR 501.

50. The Onshore Business Development Assistance is available to eligible businesses that experience significant negative impacts as a result of the reduction in fishing activity to assist with business restructuring to remain viable. The Onshore Business Development Assistance is not a product or incident of any contract or agreement to supply goods or services in the applicant's trade. Rather, the Onshore Business Development Assistance is made for the purpose of assisting the applicant with restructuring costs. The nature of the Onshore Business Development Assistance and its relationship to the applicant's business activities indicate that the Onshore Business Development Assistance is capital in nature.

51. The Onshore Business Development Assistance is not income according to ordinary concepts and is not included in the taxpayer's assessable income under subsection 6-5(1).

Section 15-10 – bounty or subsidy

52. Section 15-10 provides that an amount is included in assessable income if it is:

- a bounty or subsidy;
- received in relation to carrying on a business; and
- not assessable as ordinary income under section 6-5.

Bounty or subsidy received in relation to carrying on a business

53. The terms 'bounty' and 'subsidy' are not defined in income tax legislation. The word 'subsidy', as noted by Windeyer J in *Placer Development Ltd v. Commonwealth of Australia*,⁵ derives from the Latin 'subsidiū' meaning 'an aid or help'. The Macquarie Dictionary, 2001, rev. 3rd edn, defines subsidy as including 'a grant or contribution of money'. The ordinary meaning adopted by case law is 'aid provided by the Crown (government) to foster or further some undertaking or industry'.

54. Following the decisions in *The Squatting Investments Co Ltd v. Federal Commissioner of Taxation*,⁶ *Reckitt & Colman* and *First Provincial Building Society Ltd v. Federal Commissioner of Taxation*⁷ (*First Provincial*), it is now well accepted that a 'bounty' or 'subsidy' includes a financial grant made by a government. An Onshore Business Development Assistance payment is a bounty or subsidy.

⁵ (1969) 121 CLR 353.

⁶ (1953) 86 CLR 570; 10 ATD 126; (1953) 5 AITR 496.

⁷ (1995) 56 FCR 320; 95 ATC 4145; (1995) 30 ATR 207.

55. A bounty or subsidy will be 'in relation to' carrying on a business when there is a real connection between the payment and the business. The term 'in relation to' includes within its scope payments that have a direct or indirect connection to the business. As stated by Hill J in the *First Provincial* case:

The words 'in relation to' are words of wide import. They are capable of referring to any relationship between the two subject matters, in the present case the receipt of the bounty or subsidy, on the one hand, and the carrying on of the business, on the other ... the degree of connection will be 'a matter of judgment on the facts of each case'. ...What is necessary, at the least, in the present context is that there be a real connection ... the relationship need not be direct, it may also be indirect.⁸

56. A bounty or subsidy must be related to 'carrying on' the business not merely for commencing or ceasing a business. As stated by Hill J in the *First Provincial* case:

the relationship must be to the 'carrying on' of the business. These words may perhaps be understood in opposition to a relationship with the actual business itself. They would make it clear, for example that a bounty received, merely in relation to the commencement of a business or the cessation of the business, would not be caught. The expression 'carrying on of a business' looks, in my opinion, to the activities of that business which are directed towards the gaining or producing of assessable income, rather than merely to the business itself.⁹

57. In *Plant v. Commissioner of Taxation* [2004] AATA 1296, it was held that a capital payment that assisted in the creation of a bigger and more efficient workshop was received in relation to the carrying on of the business.

58. A government payment to industry received by an entity to assist with the capital costs of restructuring a business to enable that business to improve its overall efficiency is received in relation to 'carrying on' a business.¹⁰

59. The Onshore Business Development Assistance component of the Package is a bounty or subsidy received in relation to the carrying on of a business for the purposes of section 15-10. Accordingly, the receipt is assessable income under section 15-10.

Capital gains tax

60. CGT event C2 under section 104-25 happens when the entitlement to receive the Onshore Business Development Assistance is satisfied, that is, when the assistance is paid by way of a reimbursement directly to the applicant or payment of expenses on the applicant's behalf.

⁸ *First Provincial* (1995) 56 FCR 320 at 333.

⁹ *First Provincial* (1995) 56 FCR 320 at 332.

¹⁰ Taxation Ruling TR 2006/3 Income tax: government payments to industry to assist entities (including individuals) to continue, commence or cease business.

61. However, any capital gain or capital loss made as a result of a payment of Onshore Business Development Assistance is disregarded under paragraph 118-37(2)(a).

62. Paragraph 118-37(2)(a) provides a CGT exemption by disregarding a capital gain or capital loss that results from receipt of a payment as reimbursement or payment of expenses under a scheme established under legislation by an Australian government agency. The Onshore Business Development Assistance is paid under such a scheme.

Payment relates to acquisition of new CGT asset

63. A payment of Onshore Business Development Assistance by way of a reimbursement or payment of the entity's expenditure to acquire a new CGT asset does not reduce the cost base (or reduced cost base) of the asset acquired. This is because, although the expenditure to acquire the asset has been recouped, the Onshore Business Development Assistance is assessable under section 15-10 (see subsection 110-45(3) and subsection 110-55(6)).

Business Advice Assistance

Section 6-5 – income according to ordinary concepts

64. As explained in paragraph 47 of this Ruling it is necessary to consider the character of the payment in the hands of the recipient taxpayer.

65. The Business Advice Assistance payment is for the purpose of assisting successful applicants with the costs of seeking professional advice in preparing their application for Onshore Business Development Assistance. The receipt of the Business Advice Assistance is not in the ordinary course of business. It is not income according to ordinary concepts and is not included in the taxpayer's assessable income under subsection 6-5(1).

Section 15-10 – bounty or subsidy

66. A reimbursement, or amount of assistance or direct payment on behalf of the recipient, that is not on revenue account and therefore not assessable as ordinary income but which is a bounty or a subsidy in relation to carrying on the business, is assessable under section 15-10.¹¹

67. Business Advice Assistance paid to or on behalf of an applicant for Onshore Business Development Assistance is considered to be a bounty or subsidy received in relation to carrying on a business as a successful application would have resulted in the receipt of Onshore Business Development Assistance which is a bounty or subsidy received in relation to the carrying on of a business for the purposes of section 15-10. In these circumstances, Business Advice Assistance is assessable under section 15-10 in the income year in which it is received or paid directly to the supplier on behalf of the recipient.

¹¹ TR 2006/3, paragraph 18.

Capital gains tax

68. Expenditure on professional services of preparation of an application for Onshore Business Development Assistance is an incidental cost incurred to acquire the entitlement to receive the Onshore Business Development Assistance, a CGT asset.

Accordingly it is included in the second element of the cost base of the entitlement (subsection 110-25(3) and subsections 110-35(1) and (2)).

69. The payment of Business Advice Assistance by way of a reimbursement directly to the applicant or payment of expenses on the applicant's behalf is a recoupment of this expenditure.

70. However, the expenditure that is recouped is not excluded from the cost base of the entitlement to receive the Onshore Business Development Assistance because the amount of the recoupment is assessable income under section 15-10 (subsection 110-45(3)).

Primary production income

71. Subsection 392-80(2) provides that a taxpayer's 'assessable primary production income' for the current year is the amount of that taxpayer's basic assessable income for the current year that was derived from, or resulted from, their carrying on a primary production business.

72. Under subsection 995-1(1), a taxpayer carries on a 'primary production business' if they carry on particular business activities. In relation to fishing, paragraph (d) of the definition restricts such activities to 'conducting operations relating directly to taking or catching fish, turtles, dugong, bêche-de-mer, crustaceans or aquatic molluscs.'

73. Under the Scheme, it is unlikely that the onshore business undertaken by an entity eligible to receive the Onshore Business Development Assistance and Business Advice Assistance payments would be a primary production business. In these circumstances, the payments received by the entity would not be 'assessable primary production income' for the purposes of working out the 'averaging' adjustment required under Division 392 because they are not income that were derived from, or resulted from carrying on a primary production business.

Appendix 2 – Detailed contents list

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

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/3

Subject references:

- bounties & subsidies
- capital gains tax
- capital receipts
- government grants income
- income
- primary production income

Legislative references:

- TAA 1953
- TAA 1953 Sch 1 357-75(1)
- ITAA 1997 6-5
- ITAA 1997 6-5(1)
- ITAA 1997 15-10
- ITAA 1997 104-25
- ITAA 1997 110-25(3)
- ITAA 1997 110-35(1)
- ITAA 1997 110-35(2)
- ITAA 1997 110-45(3)
- ITAA 1997 110-55(6)
- ITAA 1997 118-37(2)(a)
- ITAA 1997 Div 392
- ITAA 1997 392-80(2)
- ITAA 1997 995-1(1)
- Copyright Act 1968
- Industrial Research and Development Grants Act 1967

Case references:

- Federal Coke Co Pty Ltd v. FC of T (1977) 7 ATR 519; 77 ATC 4255
- First Provincial Building Society Ltd v. Federal Commissioner of Taxation (1995) 56 FCR 320; 95 ATC 4145; (1995) 30 ATR 207
- GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1
- Hayes v. FC of T (1956) 96 CLR 47
- Placer Development Ltd v. Commonwealth of Australia (1969) 121 CLR 353
- Plant v. Commissioner of Taxation [2004] AATA 1296; 2004 ATC 2364
- Reckitt & Colman Pty Ltd v. FC of T (1974) 74 ATC 4185; 4 ATR 501
- Scott v. FC of T (1966) 117 CLR 514
- The Squatting Investment Co Ltd v. Federal Commissioner of Taxation (1953) 86 CLR 570; 10 ATD 126; (1953) 5 AITR 496

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ATO references

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