



# ***PR 1999/56 - Income tax: Coonalpyn Olives Project***

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 This document has changed over time. This is a consolidated version of the ruling which was published on *25 June 2001*



## Product Ruling

### Income tax: Coonalpyn Olives Project

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#### *Preamble*

*The number, subject heading, and the What this Product Ruling is about (including Tax law(s), Class of persons and Qualifications sections), Date of effect, Withdrawal, Arrangement and Ruling parts of this document are a 'public ruling' in terms of Part IVAAA of the Taxation Administration Act 1953. Product Ruling PR 98/1 explains Product Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a public ruling and how it is binding on the Commissioner.*

*[Note: This is a consolidated version of this document. Refer to the Tax Office Legal Database (<http://law.ato.gov.au>) to check its currency and to view the details of all changes.]*

## What this Product Ruling is about

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1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates. In this Ruling this arrangement is sometimes referred to as the Coonalpyn Olives Project, or 'the Project' or the 'product'.

#### **Tax law(s)**

2. The tax law(s) dealt with in this Ruling are sections 6-5, 8-1, 42-15, 42-130, 70-35, 387-55, 387-125, 387-165 and 387-355 of the *Income Tax Assessment Act 1997* ('ITAA 1997'), and sections 82KL, 82KZM and 97, and the relevant provisions of Part IVA of the *Income Tax Assessment Act 1936* ('ITAA 1936').

#### **Class of persons**

3. The class of persons to whom this Ruling applies is those who enter into the arrangement described below on or after the date this Ruling is made, as further qualified in paragraphs 17 and 19 below. They will have a purpose of staying in the arrangement until it is completed (i.e., being a party to the relevant agreements until their term expires), and deriving assessable income from this involvement as set out in the description of the arrangement. In this Ruling these persons are referred to as 'Growers'.

4. The class of persons to whom this Ruling applies does not include persons who intend to terminate their involvement in the arrangement prior to its completion, or who otherwise do not intend to derive assessable income from it.

## Qualifications

5. The Ruling provides this specified class of persons with a binding ruling as to the tax consequences of this product. The Commissioner accepts no responsibility in relation to the commercial viability of this product, and gives no assurance the prices charged for the product are reasonable, appropriate or represent industry norms. A financial (or other) adviser should be consulted for such information.

6. The Commissioner rules on the precise arrangement identified in the Ruling.

7. The class of persons defined in the Ruling may rely on its contents, provided the arrangement (described below at paragraphs 12 to 34) is carried out in accordance with details described in the Ruling. If the arrangement described in the Ruling is materially different from the arrangement that is actually carried out:

- the Ruling has no binding effect on the Commissioner, as the arrangement entered into is not the arrangement ruled upon; and
- the Ruling will be withdrawn or modified.

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## Date of effect

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9. This Ruling applies prospectively from 9 June 1999, the date this Ruling is made. However, 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 (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

10. If a taxpayer has a more favourable private ruling (which is legally binding), the taxpayer can rely on the private ruling if the

income year to which the private ruling relates has ended, or has commenced but not yet ended. However, if the arrangement covered by the private ruling has not begun to be carried out, and the income year to which it relates has not yet commenced, this Ruling applies to the taxpayer to the extent of the inconsistency only (see Taxation Determination TD 93/34).

## **Withdrawal**

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11. This Product Ruling is withdrawn and ceases to have effect after 30 June 2002. The Ruling continues to apply, in respect of the tax law(s) ruled upon, to all persons within the specified class who enter into the specified arrangement during the term of the Ruling. Thus, the Ruling continues to apply to those persons, even following its withdrawal, who entered into the specified arrangement prior to withdrawal of the Ruling. This is subject to there being no material difference in the arrangement or in the persons' involvement in the arrangement.

## **Arrangement**

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12. The arrangement that is the subject of this Ruling is described below. This description incorporates the following documents:

- Draft Prospectus prepared for the Coonalpyn Olives Project, dated 13 April 1999;
- **Constitution** prepared for the Coonalpyn Olives Project, dated 30 April 1999, between Playford Management Limited ('PML') as the Responsible Entity and each Grower;
- **Trust Deed** for The Coonalpyn Olives Unit Trust, dated 30 April 1999, between Founder and PML as the Trustee;
- Draft Plantation Agreement between PML and Coonalpyn Olives Pty Ltd ('COPL');
- Draft Farm Management Agreement between COPL and Agrolive Pty Ltd ('APL');
- Land Option Agreement between PML and Land Owner, dated 11 May 1999;
- Draft Custody Agreement between PML and Cardinal Financial Securities Limited ('CFSL');

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- Olive Tree Supply Contract between COPL and APL, dated 22 March 1999;
- Draft Olive Crushing Agreement between PML and Australian Olive Oil Company Pty Ltd ('AOOC');
- Draft Olive Oil Sale Agreement between PML and AOOC;
- Draft Costs of Issue Contract between PML and COPL;
- Draft Option Agreement between PML and COPL; and
- Letters, facsimile transmissions and attachments from Applicant dated 25 March, 1 April, 23 April 1999 (including the Valuation Report prepared for COPL dated 17 March 1999), 11, 12, 19, 25, 28 May 1999, 1 June 1999, 13 December 2000 and 15 June 2001.

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

13. The documents highlighted are those Growers enter into or become a party to. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate<sup>1</sup> of a Grower, will be a party to, which are part of the arrangement to which this Ruling applies, except agreements that come within paragraph 31 below, concerning the provision of finance. The effect of the agreements listed above is summarised as follows.

14. This arrangement is called the Coonalpyn Olives Project. The Responsible Entity, PML, proposes to offer 1,781 Investment Units. Additional Units may be acquired by COPL at a discount. **This Ruling will not apply to Units provided at a discount or otherwise than as described below.** The Investment Units will be 'stapled' units, comprising 1 Grower Unit and 1 Unit in The Coonalpyn Olives Unit Trust.

15. PML, as trustee of this trust, has an option to acquire land near Coonalpyn, South Australia. The total area to be purchased is 2,197 hectares, of which 500 hectares have been identified as being suitable for establishing an olive plantation. If all the Investment Units to be offered are taken up, approximately 150,000 olive trees will be planted.

16. Participants in the Project become bound by the terms of the Constitution, by executing an application in which they agree to be

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<sup>1</sup> In this Ruling 'associate' has the meaning as defined in section 318 of the ITAA 1936.

bound by its terms (cls 1.2 and 2.1<sup>2</sup>). On PML entering their name in the Project Register they become accepted as a Grower for the purposes of this Ruling.

17. PML have set a minimum Project size of 200 hectares, which equates to 720 applications. If this number is not achieved no names will be entered in the Project Register and the Project will not go ahead. **This Ruling only applies to Growers whose names are entered in the Project Register.**

### **Interests applied for**

18. All persons applying to participate in the Project must apply for a stapled Unit, consisting of a Unit in The Coonalpyn Olives Unit Trust and a Grower Unit. However, they have the choice of whether the Unit in the Unit Trust is to be held by them, or an associated party. They also have the choice of whether or not the Grower Unit is to be a Managed Grower Unit (cl 29.1). Both the unmanaged Grower Unit and the Managed Grower Unit entitle the holder to use a specified area of land (their 'Olive Grove'), to carry on a business of growing olive trees, and harvesting, processing and selling any resulting olives for the production of olive oil (cls 19 to 31). Under clause 19.4 property in the harvested olives passes to the Grower at the time of harvest.

19. However, the Managed Grower Unit also involves appointing PML as the Grower's agent to carry on this business. The rest of this description of the arrangement only covers Growers who acquire Managed Grower Units. **Therefore, this Ruling will not apply to persons who enter the Project but choose not to use the services of PML.**

20. To be accepted into the Project each Grower will be required initially to contribute \$10,000, payable in four instalments as follows:

- \$6,563 payable on lodging application;
- \$990 payable on or before 30 June 2000;
- \$1,030 payable on or before 30 June 2001; and
- \$1,417 payable on or before 30 June 2002 (cl 12).

### **The Constitution**

#### ***Management conditions***

21. There is no separate Management Agreement for this Project. Instead, the terms under which PML is to provide management

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<sup>2</sup> In this Ruling all references to clauses are to clauses in the Constitution, unless otherwise stated.

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services to the Growers holding Managed Grower Units, are set out in clauses 32 to 38 of the Constitution. In fact, the Constitution is intended to set out in full the legal relationships between a Grower and PML, on acceptance of the Grower into the Project.

22. Where the Grower appoints PML, they enter into a management arrangement with that company for a period of 25 years (cl 32). PML is then responsible for the establishment of an olive tree plantation on their behalf, and the ongoing maintenance of those trees, the harvesting and processing of olives from those trees, and the marketing and selling of the olive oil. The Grower, and therefore PML as their agent, must plant no less than 84 olive trees, of only specific varieties, on each Olive Grove (cls 28 and 29).

23. PML may subcontract its obligations under this arrangement to another party, and propose to contract with COPL in this regard.

24. Under clause 34.1 PML will be responsible for maintaining records of the activities carried out on behalf of the Grower. The Grower may inspect these records at any time. PML is, under clause 34.2, to supply the following reports to each Grower at least once a year:

- the state of health of the olive trees;
- the expected crop levels;
- previous crop and oil yield levels (after first harvest);
- revenue generated; and
- expenses incurred.

25. A Grower may terminate their agreement with PML in certain situations:

- where PML commits a breach of any of its obligations and the default is not remedied within 10 Business Days of receiving notice of the breach (cl 38.2); or
- where a meeting of members, complying with section 252J of the Corporations Law, passes a motion, by at least 50% of the total number of votes, to do so (cl 39.2).

26. Any stakes affixed to the land on behalf of a Grower will remain the property of the Grower (cl 19.5) and the Constitution grants the Grower the right to remove these stakes at the end of the Project. There will be one main stake per tree, with each stake treated as a unit of plant.

27. Each Grower's name will be entered in a Growers Register. Each Grower's name will be matched with a 'uniquely identified' Olive Grove (cl 13.5), and they will be advised of the exact location of

this by reference to the 'GRO' plan lodged with the South Australian Land Titles Office.

***Fees payable and work to be performed***

28. Under clause 12.2 application fees payable in relation to each Managed Grower Unit, in respect of the first Issue (the first allocation of Olive Groves) are:

- \$370 for 1 Unit in the Unit Trust;
- \$1,576 for Landcare works that fall within the definition of 'landcare operations' in section 387-60;
- \$363 for the purchase and erection of stakes;
- \$56 for the construction of buildings;
- \$1,277 for the purchase and installation of certain irrigation items that will be 'water facilities', as defined in section 387-130;
- \$365 for connecting power to the land, as defined in section 387-360;
- \$484 for certain pre-planting and planting work, including the cost of purchasing the olive trees, that will be 'establishment expenditure' for the purposes of Subdivision 387-C;
- \$420 for the cost of acquiring certain items that will be units of 'plant' for the purposes of Division 42 of the ITAA 1997, such as a harvester, various vehicles and other equipment;
- \$9 for various consumables required up until 30 June 2003 for the plant and equipment;
- \$49 for the overall design of the olive groves;
- \$1,516 Management fee for post-planting and other maintenance services for the period up to 30 June 2000;
- \$989 Management fee for management services from 1 July 2000 to 30 June 2001;
- \$1,030 Management fee for management services from 1 July 2001 to 30 June 2002;
- \$1,248 Management fee for management services from 1 July 2002 to 30 June 2003; and

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- \$248 Grant of Use fee<sup>3</sup>, being licence fees for use of the land, for the 4 years ending on 30 June 2003.

29. After the initial application fees of \$10,000 have been applied in the above manner, fees payable in subsequent years (as set out in cls 20 and 35) are to be met, in the first instance, from the Grower's proceeds from sale of olive oil (cl 36.3.1). However, to the extent that the annual management fee and/or Grant of Use fee cannot be discharged in this manner, Growers will continue to be liable personally for any balance owing to PML.

30. Growers may also be made liable personally to contribute additional amounts of capital in respect of their Unit in the Unit Trust, under clause 4.5.1 of the Trust Deed.

31. Liability for the fees totalling \$10,000 does not become a presently existing liability until such time as a Grower completes and lodges their Application Form, minimum subscription is reached, and PML issues the appropriate interests. At this time a Grower will have incurred an amount totalling \$10,000.

## Finance

32. There are no funding arrangements to be offered by PML or any associated entity, in connection with this Project. Growers may use their own funds, or arrange finance from an independent lender. Loan transactions to which this Ruling applies will exhibit the following features:

- all loan terms will be of an arm's length nature;
- borrowers will remain fully liable for the balance of the loan outstanding at any time, and the lender will take full legal action against defaulting borrowers;
- none of the funds lent will be transferred back to the lender, or any associate, as part of any 'round robin' or equivalent transaction;
- the loan will not be a 'split-loan', of the type described in Taxation Ruling TR 98/22;
- there will be no indemnity, or equivalent agreement, to reduce the borrower's liability; and
- repayment of principal and payment of interest will not be linked to deriving income from the Project, and will be made regularly, commencing from or about, the time of the making of the loan.

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<sup>3</sup> Under cl 20.1 this fee is payable to PML in its capacity as trustee of The Coonalpyn Olives Unit Trust

**Derivation of income**

33. Growers with Managed Grower Units appoint PML to be their exclusive agent to process olives, and market and sell the olive oil produced from their Olive Groves (cl 32).

34. PML may, at its discretion, mix all or some of the olives from each Grower's Olive Grove for subsequent processing and sale (cl 32.7). PML may also reject and dispose of any olives which it deems unsuitable for the production of extra virgin oil (cl 32.8).

35. Growers will be entitled to the proceeds from the sale of the olive oil without reference to olive type, quality or volume. However, sale proceeds will be derived by each Grower based on the number of Grower Units held (cl 32.10). Possible projected returns for Growers are set out in Section 8 of the draft Prospectus. They depend on a range of assumptions and PML does not give any assurance or guarantee whatsoever in respect of the future success of, or financial returns associated with entering into the Constitution and associated agreements. However, based on the financial model prepared for the Project, Growers can expect to achieve an internal rate of return before tax of approximately 16.4%, and an internal rate of return after tax of approximately 22.9%.

**Ruling****Sections 8-1, 42-15, 42-130, 387-55, 387-125, 387-165 and 387-355**

36. For a Grower who enters the Project by 30 June 1999 and who incurs the fees set out in paragraph 28 because they choose to engage PML, the following deductions will be allowable to them for the years ended 30 June 1999 to 30 June 2003, providing that the option to acquire the land is exercised by 30 June 1999 and PML becomes the owner of the land by that date; as set out in the following table:

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Fee type (tax law applicable)	Year ended 30 June 1999	Year ended 30 June 2000	Year ended 30 June 2001	Year ended 30 June 2002	Year ended 30 June 2003
Licence Fees (8-1)	\$248 (see Note i)				
Management Fees (8-1)	\$2,505 (see Note ii)		(see Note ii)	\$1,030 (see Note ii)	\$1,248 (see Note ii)
Stakes (42-15, 42-130)	\$363			-	
Machinery (42-15)	\$10 (see Note iii)	\$60 (see Note iii)	\$45 (see Note iii)	\$34 (see Note iii)	\$76 (see Note iii)
Landcare (387-55)	\$1,576				
Irrigation (387-125)	\$426 ( $\frac{1}{3}$ each year)	\$426	\$426		
Tree estab't (387-165)					\$26 (see Note iv)
Electricity connection (387-355)	\$36 ( $\frac{1}{10}$ for 10 years)	\$36	\$36	\$36	\$36
Consumables (8-1)	\$6 (see Note v)		\$1	\$1	\$1

**Notes:**

- (i) Although the amount of \$248 is incurred at the time of accepting a Grower into the Project, and is for the doing of a thing not to be wholly done within 13 months after this time, section 82KZM will not apply to it. This is because it is 'excluded expenditure' (i.e., < \$1,000- refer to subparagraph 82KZM(1)(b)(ii)). Accordingly, the \$248 deduction shown in respect of the year ended 30 June 1999 only applies where a Grower acquires less than 5 Managed Grower units.
- However, if a Grower were to acquire 5 or more Managed Grower units they would incur expenditure that would not be 'excluded expenditure' and section 82KZM would apply. For example, if a Grower were to acquire 5 Managed Grower units they would incur a licence fee of \$1,240, which would be deductible according to the formula set out in subsection 82KZM(1).
- (ii) The amounts of \$1,030 and \$1,248 Management Fees will be incurred at the time of acceptance of a Grower into the Project. They **will** be for the doing of things that are not to be wholly done within 13 months after the day on which they will have been incurred. Therefore, they are amounts to which section 82KZM applies. The application of section 82KZM involves identifying the 'eligible service period' in relation to these amounts, and for each income year, the number of days of that 'eligible service period' that

occur in that income year. This application results in the amounts of \$1,030 and \$1,248 being deductible in the income years shown in the above table. The amount of \$989 is 'excluded expenditure' (i.e., < \$1,000) and has been added to the amount of \$1,516, to arrive at the deductible amount for the year ended 30 June 1999. **The amounts shown in the table in this regard only apply to a Grower who acquires 1 Managed Grower unit.**

However, if a Grower were to acquire 2 or more Managed Grower Units they would incur \$1,978 or more, which would not be 'excluded expenditure', and section 82KZM would apply. For example, if a Grower were to acquire 2 Managed Grower units they would incur \$3,032 (2 x \$1,516) for services to be provided wholly within 13 months of the date this amount was incurred, which would be deductible for the year ended 30 June 1999, as section 82KZM would not apply to it. The amount of \$1,978 (2 x \$989), however, incurred for the doing of things wholly to be done in the period 1 July 2000 to 30 June 2001, would be deductible for the year ended 30 June 2001, as section 82KZM will apply to it.

- (iii) Deductions for depreciation under section 42-15 for the income years shown will depend, for the purposes of either section 42-160, 'Diminishing value method', or section 42-165, 'Prime cost method', on the number of 'days owned', being the number of days in the income year in which the Grower owns an interest in the respective item of plant. PML is to advise Growers of this and the relevant depreciation rate that applies. Growers will need to choose which depreciation method they use. The figures shown in the table are, therefore, included for illustrative purposes only and are subject to change. The deductions shown are based on the machinery being purchased in May 1999 and July 2002, using depreciation rates of 22.5% for motor vehicles and 30% for other machinery, and adopting the diminishing value method.
- (iv) Deductibility under section 387-165, for horticultural plant establishment expenditure, will commence from the time the olive trees, as horticultural plants, enter their first commercial season. PML will advise Growers of this, but anticipate that approximately 70% of the trees to be planted will enter their first commercial season in October 2002. PML considers that a Grower will be able to determine, for the purposes of section 387-175, that the trees have an 'effective life' for the purposes of section 387-185 of 30 years or more, resulting in a write-off rate of 7%. For the purposes of illustration, the deductions shown in the table are based on a 7% write-off rate commencing from 1 October 2002.
- (v) Deductibility of expenditure on consumables has been based on the treatment set out in Taxation Ruling IT 333. The figures shown in the table are for illustrative purposes only. PML will advise actual figures.

37. For a Grower who enters into the Project after 30 June 1999 but before 30 June 2000, or for a Grower who applies to enter into the Project before 30 June 1999 but the option to acquire the land is

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exercised after 30 June 1999 and on or before 30 June 2000, the Grower will be entitled to the same deductions as set out in the table above (provided that the Grower incurs the fees set out in paragraph 28), except:

- their deductions will not commence until they year ended 30 June 2000 (i.e., all the deductions are 'moved forward' a year); and
- their deductions for depreciation are anticipated to be:

Year ended 30 June	2000	2001	2002	2003	2004
	\$63	\$47	\$35	\$76	\$55

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

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

37.1. For a Grower who is an individual and who entered the Project on or after 9 June 1999 and prior to any withdrawal of this Product Ruling, the rule in section 35-10 may apply to the business activity comprised by their involvement in this Project. Under paragraph 35-55(1)(b) the Commissioner has decided for the income years ended 30 June 2001 to 30 June 2003 that the rule in section 35-10 does not apply to this business activity provided that the Project has been, and continues to be, carried on in a manner that is not materially different to the arrangement described in this Ruling.

37.2. This exercise of the discretion in subsection 35-55(1) will not be required where, for any year in question:

- a Grower's business activity satisfies one of the objective tests in sections 35-30, 35-35, 35-40 or 35-45; or
- the 'Exception' in subsection 35-10(4) applies.

37.3. Where either the Grower's business activity satisfies one of the objective tests, the discretion in subsection 35-55(1) is exercised, or the Exception in subsection 35-10(4) applies, section 35-10 will not apply. This means that a Grower will not be required to defer any excess of deductions attributable to their business activity in excess of any assessable income from that activity, i.e., any 'loss' from that activity, to a later year. Instead, this 'loss' can be offset against other assessable income for the year in which it arises.

37.4. Growers should not see the Commissioner's decision to exercise the discretion in paragraph 35-55(1)(b) as an indication that the Tax Office sanctions or guarantees the Project or the product to be

a commercially viable investment. An assessment of the Project or the product from such a perspective has not been made.

### **Section 82KZM**

38. Some of the expenditure listed in the above table does fall within the scope of section 82KZM, as explained in Notes 1 and 2 above.

### **Section 82KL**

39. Section 82KL does not apply to deny the deductions otherwise allowable under section 8-1, as set out in the above table.

### **Part IVA**

40. The relevant provisions of Part IVA will not be applied to cancel a tax benefit obtained under a tax law dealt with in this Ruling.

### **Section 6-5 and section 97**

41. Growers deriving gross proceeds from the sale of olive oil must include these proceeds in their assessable income for the relevant year, under section 6-5. Growers presently entitled to income from The Coonalpyn Olives Unit Trust, who are not under a legal disability, must include the appropriate amount in their assessable income under section 97 of the ITAA 1936.

### **Section 70-35**

42. Growers who have harvested olives on hand at the end of any income year will be holding trading stock of a business carried on by them. The excess of the value of this trading stock at the end of any income year over the value of trading stock at the start of that income year must be included in their assessable income under section 70-35.

## **Explanations**

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### **Section 8-1**

43. Consideration of whether the fees payable to PML are deductible under section 8-1 proceeds on the following basis:

- the outgoings in question must have a sufficient connection with the operations or activities that directly gain or produce the taxpayer's assessable income;

- the outgoings are not deductible under paragraph 8-1(1)(b) if they are incurred when the business has not commenced; and
- where all that happens in a year of income is a taxpayer contractually commits themselves to a venture that may not turn out to be a business, there can be doubt about whether the relevant business has commenced, and hence, whether paragraph 8-1(1)(b) applies. However, that does not preclude the application of paragraph 8-1(1)(a) in determining whether the outgoings in question have a sufficient connection with activities to produce assessable income.

44. An agriculture scheme can constitute the carrying on of a business. Where there is a business, or a future business, the gross proceeds from sale of the agricultural produce from the scheme, will constitute assessable income in their own right. The generation of 'business income' from such a business, or future business, provides the backdrop against which to judge whether the outgoings in question have the requisite connection with the operations that more directly gain or produce this income. These operations will be the planting, tending, maintaining and harvesting of the agricultural crops, in this case, olives, and sometimes processing of those crops, as in this case.

45. Generally, an investor will be carrying on a business of agriculture where:

- the investor has an identifiable interest in specific growing crops coupled with a right to harvest and sell the produce from those crops;
- the agriculture activities are carried out on the investor's behalf; and
- the weight and influence of the general indicators of a business, as developed by the Courts, point to the carrying on of a business.

46. For this Project Growers have, under the Project Constitution, rights to farm an identifiable area of land consistent with the intention to carry on a business of growing olives. Under the Constitution, Growers appoint PML to provide services such as planting, cultivating, tending, fertilising, spraying, watering, maintaining and otherwise caring for their olive trees. Growers are considered to have control of their investment.

47. The Constitution gives Growers an interest in the olives grown on their behalf and the right to have those olives processed and olive oil sold for their benefit. The Project documentation contemplates that Growers will have an ongoing interest in the growing crops. The

crops belong to the Growers in the sense that they have an interest in the land on which they are growing and a profit à prendre in respect of the produce, which confers an equitable interest in the crops upon the Grower.

48. Growers have the right to use their Olive Grove areas for agricultural purposes and to have PML come onto the land to carry out its obligations under the Constitution. The Grower's degree of control over PML, as evidenced by the Constitution and supplemented by Corporations Law, is sufficient. A majority of the Growers are able to terminate the arrangements with PML in certain instances, such as default in performance of its duties and failure to rectify the default. The agriculture activities described in the Constitution are, therefore, carried out on the Growers' behalf.

49. The general indicators of a business, as developed by the Courts, are described in Taxation Ruling TR 97/11. Positive findings can be made from the arrangement's description for all the indicators discussed in that Ruling. Growers to whom this Ruling applies intend to derive assessable income from the Project. This intention is related to projections in the Prospectus that suggest the Project should return a 'before-tax' profit to the Growers, i.e., a 'profit' in cash terms that does not depend in its calculation, on the fees in question being allowed as a deduction.

50. Growers will engage the professional services of a manager with appropriate credentials. There is a means to identify which trees Growers have an interest in. These services are based on accepted agricultural practices and are of the type ordinarily found in farming ventures that would commonly be said to be businesses.

51. Growers have a continuing interest in the trees from the time they are acquired and planted on their behalf. The agricultural activities, and hence the fees associated with their procurement, are consistent with an intention to commence regular activities that have an 'air of permanence' about them. The Growers' agricultural activities will constitute the carrying on of a business.

52. The fees associated with the agricultural activities will relate to the gaining of income from this business, and hence have a sufficient connection to the operations by which this income (from the sale of the crop produce) is to be gained from this business. They will, thus, be deductible under section 8-1, except to the extent they are capital, or of a capital nature. Capital components of the fees have been separately identified in clause 12. No additional capital component, or 'non-income producing purpose' in incurring the fees, is identifiable from the arrangement. The tests of deductibility under section 8-1 are met. The exclusions in subsection 8-1(2) do not apply, other than in relation to the capital exceptions noted above.

## Section 387-55

53. Section 387-55 allows a taxpayer a deduction for capital expenditure incurred on landcare operations for land used to carry on a primary production business.

54. Landcare operations for land includes work on erecting fences primarily and principally for the purpose of excluding animals from an area affected by land degradation to prevent or limit extension of that degradation and to help reclaim the area. It also includes work on constructing drainage works primarily and principally for the purpose of controlling salinity or assisting in drainage control, and work primarily and principally for the purpose of eradicating pests and plants detrimental to the land.

55. Growers need not own the land to qualify for the deduction, so long as it is to be used by them in carrying on a primary production business. In this Project there will be no delay between the execution of the relevant agreements and the commencement of 'business operations' on the Grower's behalf. Accordingly, a Grower's primary production business will have commenced at the time the expenditure in question has been incurred, and the requirements of section 387-55 will have been satisfied.

## Section 387-125

56. Section 387-125 allows a deduction for capital expenditure on the construction, manufacture, installation or acquisition of a water facility, if incurred primarily and principally for the purpose of conserving or conveying water for use in a primary production business conducted on land in Australia.

57. The section allows this expenditure to be deducted over a 3 year period, i.e., at a rate of 33.3 per cent per annum, starting with the year in which the expenditure is incurred. The taxpayer to whom such deductions are allowable does not need to own the land in question. Irrigation works of the kind to be carried out for Growers in this Project by PML are of the type to which section 387-125 applies.

## Section 387-165

58. Subdivision 387-C allows deductions in respect of capital expenditure on establishing horticultural plants for use in a horticultural business. For the purposes of this Subdivision, a lessee or licensee of land, such as the Growers in this Project, carrying on a business of horticulture, is treated as owning the plants growing on the land, rather than the actual owner. The deductions allowable under section 387-165 commence from the time the plants enter their first commercial season. PML will advise Growers of this event.

59. Horticultural plant establishment expenditure is capital expenditure on establishing the horticultural plants, and includes such things as the cost of acquiring the plants, costs of pre-planting and planting, such as ploughing, contouring, top dressing, fertilising and stone removal. Expressly excluded is expenditure on draining swamps or the initial clearing of land.

### **Section 42-15**

60. Throughout this Project Growers will acquire interests in various items of plant and equipment, which will be used by PML in carrying out its obligations under the Constitution. These items will constitute units of plant for the purposes of Division 42 and will be used for the purpose of producing assessable income for the Growers. PML will advise Growers of the details required for them to calculate their depreciation deductions for expenditure on these items.

61. Under the Constitution PML will also, on the Growers' behalf, acquire stakes to support the growing trees, and Growers have the right to remove these stakes. Under Taxation Ruling IT 175 these Growers will be considered to be the 'owners' of these items. These items will also be used for the purpose of producing assessable income from the time they are installed, which is expected to be before 30 June 1999. As each stake will cost less than \$300 the prime cost rate for each one, under section 42-130, is 100%. This means that Growers will be able to claim a depreciation deduction for 100% of their expenditure for the income year ended 30 June 1999. PML will advise Growers of the correct year if the stakes are not owned and used for the purpose of producing assessable income during the year ended 30 June 1999.

### **Section 387-355**

62. A deduction is allowable under Subdivision 387-E for capital expenditure incurred by a person on '\*connecting power to land or upgrading the connection' if the person has an interest in land, or is a share-farmer carrying on a business on the land, and they intend to use all or some of the electricity to be supplied in carrying on a business on that land for the purpose of producing assessable income.

63. The deduction is calculated under section 387-355, over a period of 10 years from the time the expenditure is incurred, i.e., you deduct 10% of the expenditure each year. Work that constitutes 'connecting power to land or upgrading the connection' is exhaustively defined in section 387-360. The work to be performed by PML, for which a fee of \$365 is to be charged, meets the requirements of section 387-360.

64. Growers accepted into this Project will also have an ‘interest in land’ at the time of incurring the expenditure by virtue of their rights under the Constitution and their licence to use their Olive Grove.

## Section 82KZM

65. Under the Constitution the fee for management services deductible under section 8-1 in respect only of the year ended 30 June 1999, is charged for providing services to a Grower only for a maximum period of 13 months from incurring the relevant expenditure. The fee is for a number of specified services. No explicit conclusion can be drawn from the arrangement’s description that this fee has been inflated to result in reduced fees being payable for subsequent years. There is also no evidence that might suggest the services covered by this fee could not be provided within 13 months of incurring the expenditure in question. Thus, for the purposes of this Ruling, it can be accepted that no part of the fee is for PML doing ‘things’ that are not to be wholly done within 13 months of the fees being incurred. On this basis, the basic precondition for the operation of section 82KZM is not satisfied and it will not apply to the expenditure of \$1,516 by Growers under the Constitution.

66. Section 82KZM does apply to other fees, as explained in Notes 1 and 2 to the table in paragraph 36 above.

## Section 82KL

67. The operation of section 82KL depends, among other things, on the identification of a certain quantum of ‘additional benefit(s)’. Here, there may be a loan provided to the Grower. The loan will be provided on a full recourse basis, and on commercial terms. Insufficient ‘additional benefits’ will be provided to trigger the application of section 82KL. It will not apply to deny the deductions otherwise allowable under section 8-1.

## Part IVA

68. For Part IVA to apply there must be a ‘scheme’ (section 177A); a ‘tax benefit’ (section 177C); and a dominant purpose of entering into the scheme to obtain a tax benefit (section 177D). The Project will be a ‘scheme’ commencing generally on the date the Prospectus was issued. The Growers will obtain a ‘tax benefit’ from entering into the scheme, in the form of the deductions for the fees payable to PML, that would not have been obtained but for the scheme. However, it is not possible to conclude that the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit(s).

69. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the regular harvesting of the crops. Further, there are no features of the Project, for example, such as the fees being 'excessive', and uncommercial, predominantly financed by a non-recourse loan, and resulting in insufficient 'real money' coming into the Manager's or Landowner's hands, that might suggest the Project was so 'tax driven', and so designed to produce a tax deduction of a certain magnitude, that would attract the operation of Part IVA.

## **Detailed contents list**

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**Commissioner of Taxation**

9 June 1999

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No draft issued

*Related Rulings/Determinations:*

IT 175; IT 333; PR 98/1; TR 92/1;  
TR 92/20; TR 97/11; TR 97/16;  
TD 93/34

*Subject references:*

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

*Legislative references:*

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- ITAA1936 82KZM
- ITAA1936 82KZM(1)
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- ITAA1936 97
- ITAA1936 Pt IVA
- ITAA1936 177A
- ITAA1936 177C
- ITAA1936 177D
- ITAA1936 318
- ITAA1997 6-5
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- ITAA1997 387-60
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