



# ***PR 1999/85 - Income tax: WA Blue Gum Project - Prospectus 1999***

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 This document has changed over time. This is a consolidated version of the ruling which was published on *30 June 1999*



## **Product Ruling**

### **Income tax: WA Blue Gum Project - Prospectus 1999**

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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.*

## **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 laws' 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 'WA Blue Gum Project - Prospectus 1999', or just simply as 'the Project' or the 'product'.

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

2. The tax law(s) dealt with in this Ruling are section 8-1 of the *Income Tax Assessment Act 1997* ('ITAA 1997') and sections 82KL and 82KZM and 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. They will have a purpose of both staying in the arrangement until the whole of the crop of eucalyptus trees planted and tended under the arrangement described below ('the Plantation Crop') has been harvested for the first time, whenever that occurs, and of deriving assessable income from this involvement as set out in the description of the said 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 the completion of the first harvest of the whole of the Plantation Crop, whenever that occurs, 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 30) 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 30 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).

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## Withdrawal

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11. This Product Ruling is withdrawn and ceases to have effect after 30 June 2001. 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 change in the arrangement or in the persons' involvement in the arrangement.

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## Arrangement

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

- Application for a Product Ruling, dated 10 June 1999, lodged on behalf of WA Blue Gum Ltd ('WABG'), together with the following supporting documents ('the application'):
  - ◆ letter from WABG's solicitor to the Australian Taxation Office ('ATO'), dated 10 June 1999, with the information requirements stipulated in both Product Ruling PR 1998/1 and a procedural directive to Product Ruling Applicants issued by ATO and dated 7 May 1999;
  - ◆ copy of the Prospectus issued by WABG in relation to the Project, dated 14 May 1999 ('the Prospectus');
  - ◆ copy of the **Trust Deed for the WA Blue Gum Project consolidated as at 14 July 1997 ('the Trust Deed')** incorporating:

- the Trust Deed between WABG and Sandhurst Trustees Limited ('Sandhurst'), dated 4 June 1993;
- the First Supplemental Deed, dated 16 June 1993;
- the Second Supplemental Deed, dated 29 June 1993;
- the Third Supplemental Deed, dated 20 May 1994;
- the Fourth Supplemental Deed, dated 21 September 1994;
- the Fifth Supplemental Deed, dated 2 June 1995;
- the Sixth Supplemental Deed, dated 8 May 1996; and
- the Seventh Supplemental Deed, dated 29 April 1997;
- ◆ unexecuted copy of a **standard form contract titled 'Project Management Contract (1999)'**, which will be entered into by each Grower, WABG, and Forestry Technical Services Pty Ltd ('Fortech') ('the Project Management Contract');
- ◆ unexecuted copy of a **standard form sublease agreement titled 'Sub-Lease (1999)'**, which will be entered into by each Grower and WA Blue Gum Land Pty Ltd ('the Landholder') ('the Sublease');
- ◆ unexecuted copy of a standard form agreement titled 'Plantation Services Agreement 1999 – xxx 99 Treefarm', which will be entered into by WABG and a certain named contractor company ('Treefarms') ('the Plantation Services Agreement');
- ◆ unexecuted copy of a **standard form agreement titled 'Wood Purchase Agreement 1999 - Treefarm'**, which will be entered into by WABG, as agent for each Grower, and Treefarms ('the Wood Purchase Agreement'); and
- ◆ unexecuted copy of a **standard form loan agreement titled 'Loan Agreement (1999)'**, which will be entered into by Albany Financial

Pty Ltd ('Albany') and each Grower who wishes to take up the loan facility offered by Albany ('the Loan Agreement');

- letter to WABG's solicitor from the ATO, dated 22 April 1999;
- Letter from WABG's solicitor to the ATO, dated 2 May 1999, together with the enclosures accompanying the letter; and
- letter from WABG's solicitor to the ATO dated 3 June 1999.

**NOTE: certain information received from WABG's solicitor 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 are otherwise a party to. They are collectively known as the Project Agreements. For the purposes of describing the arrangement to which this Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, to which a Grower or an associate of a Grower will be a party. The effect of these agreements is summarised as follows.

### **Prospectus**

14. This arrangement is called the 'WA Blue Gum Project - Prospectus 1999'. Under the Prospectus, WABG seeks to raise \$3,627,000 by offering participants the opportunity to sublease land in Western Australia on which plantations of *Eucalyptus globulus* (Tasmanian Blue Gum) will be established. WABG may accept oversubscriptions, but there must be an amount of \$300,000 raised under the Prospectus for the Project to go ahead. People wishing to participate in the Project appoint the directors of WABG to be their Attorney for the purpose of entering into and executing the Sublease, the Project Management Contract and the Wood Purchase Agreement referred to in the Prospectus, plus, where finance is sought from Albany, a Loan Agreement. At the time of entering the abovementioned agreements, the applicant also agrees to be bound by the provisions of the Trust Deed.

15. Growers will sublease a discrete area of land situated in Western Australia from the Landholder. The sublease is for 12 years, or the completion of the first harvesting, whichever occurs first. Growers will also enter into a Project Management Contract with WABG to have Tasmanian Blue Gum (*Eucalyptus globulus*) seedlings planted and tended on this leased land for the purpose of eventual felling and sale in

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8 to 13 years. The Wood Purchase Agreement that Growers enter into has provisions governing the harvesting and sale of the timber grown on the leased land.

16. There are 806 hectares on offer at an initial cost of \$4,500 per hectare, with each applicant being required to take out a minimum investment of \$27,000 (being the amount necessary to establish six (6) hectares of plantations). The abovementioned initial payment is made for the performance of certain specified works by WABG to be completed by 27 July 2000. Other obligations associated with the Project and assumed by Growers, in addition to the initial cost, are an annual management fee of \$70 per hectare (CPI adjusted and indexed from 30 June 1999), an annual rental amount of \$265 per hectare (also CPI adjusted) and the granting of a right in favour of WABG whereby WABG is to receive 12.5% of the amount by which the net proceeds from the first harvest of the timber exceed the sum of \$9,250 per hectare (CPI adjusted from 30 June 1999). The payment schedule for the above obligations is as follows. The annual management fee is payable on 28 February in each year, with the first such payment being due on 28 February 2000. The first annual rental amount is due on 15 November 1999 but, thereafter, the annual rental amount is payable on each 30 September. With respect to WABG's right to share in the net proceeds from the first harvest of timber, this entitlement is a contingent one and, as a result, Growers will not know whether they, in fact, will have to pay WABG this entitlement until or after the time of harvest and sale of the timber.

17. It is expected that 1,000 to 1,250 trees will be planted on each hectare of plantable land, and it is estimated that the Tasmanian Blue Gum trees established and maintained under the Prospectus will be available for harvesting as woodchips in 2009 and 2010. At page 7 of the Prospectus, WABG estimates that Growers will derive net returns (in 1999 dollars) of \$68,328 from an investment in six (6) hectares of plantation as against costs incurred of \$47,100. The assumptions underpinning this projection are listed at page 8 of the Prospectus.

18. By investing in the Project, Growers also get the opportunity to invest in a second rotation plantation crop, by means of a coppice option. Should Growers decide to take up this option, they will be required both to pay extra amounts at a future date and enter into arrangements to extend the effect of the abovementioned Project agreements. They do not, however, have to decide whether to exercise this option until the time of the harvest of the first plantation crop. **The arrangement to be ruled on in this Product Ruling does not include this coppice option.**

**Trust Deed**

19. The parties to the Trust Deed are WABG as Manager, Sandhurst as the Representative of the Growers, and any person who enters into a Project Management Contract with WABG in the form set out in the First Schedule of the Trust Deed. Among other things, the Trust Deed recites and stipulates:

- that Sandhurst is appointed as Representative of the Growers, subject to the terms and conditions of the Trust Deed, and Sandhurst agrees to act in this capacity (cl 2.1);
- that Sandhurst will establish a 'Project Account' into which all Growers' Contributions (i.e., all amounts contributed by Growers at the time of investing in the Project pursuant to the Prospectus) will be deposited (cl 4.1);
- that, provided the minimum subscription level of \$300,000 specified in the Prospectus has been reached, Sandhurst will be required on 30 June next occurring after the date of the 1999 Prospectus, to distribute the funds standing to the credit of the Project Account as follows:
  - ◆ an amount agreed between Sandhurst and WABG shall be deposited in a 'Contingency Trust Account' set up by Sandhurst; and
  - ◆ the balance shall be paid to WABG (cl 4.5);
- that all management income (i.e., the annual payments due to WABG by a Grower for the establishment and management of a Plantation pursuant to the provisions of the Project Management Contract) shall be paid to Sandhurst and shall be deposited by Sandhurst into a 'Management Trust Account' established by Sandhurst for that purpose (cl 6.1);
- that, provided WABG is entitled to the management income under the terms of the Project Management Contracts, Sandhurst will, from time to time at the request of WABG, distribute the balance of the Management Trust Account, as at the date of the request, to WABG for services provided, or to be provided, in the maintenance of Plantations pursuant to the Project Management Contracts (cl 6.1);
- that all amounts of annual rental due to the Landholder by a Grower pursuant to a Sublease shall be paid by the

Growers directly to the Landholder in accordance with the terms of the Sublease (cl 7.1);

- that all Harvest Income (i.e., all moneys received by WABG or Sandhurst arising out of the harvesting of timber from a Plantation) shall be payable to Sandhurst and shall be deposited by Sandhurst into a 'Harvest Trust Account' (cl 8.10);
- that Sandhurst shall distribute the Harvest Income, as follows, within twenty-one days (21) days of its payment into the Harvest Trust Account:
  - ◆ first, WABG shall be reimbursed for all costs, expenses and outgoings properly incurred by it in carrying out the thinnings or clear-fall of timber on the relevant Plantations;
  - ◆ secondly, Sandhurst shall pay WABG the amount of any entitlement to 12.5% of the difference between the amount due to the Grower from the first Harvest of the Plantation Crop and the sum of \$9,250 Indexed per hectare of Plantable Area multiplied by the number of hectares of Plantable Area;
  - ◆ thirdly, Sandhurst shall pay to itself an amount equal to one (1) per cent of the Harvest Income;
  - ◆ fourthly, Sandhurst shall repay to WABG the amount owing on account of any relevant Contingency Loans;
  - ◆ subject to entitlements to deduct amounts from Harvest Income for any unpaid fees due by a Grower in relation to the Project, the balance of Harvest Income shall be distributed to Growers in the proportion that their Plantation Hectares bears to the total Plantation Hectares in the Project (cls 8.10 and 8.11);
- that WABG shall be entitled to receive and shall be paid the following amounts by way of remuneration:
  - ◆ the Growers' contributions;
  - ◆ all annual fees payable to WABG pursuant to the terms of the Project Management Contracts; and
  - ◆ the amount of any entitlement to 12.5% of the difference between the amount due to the Grower from the first Harvest of the Plantation

Crop and the sum of \$9,250 Indexed per hectare of Plantable Area multiplied by the number of hectares of Plantable Area(cl 9.1);

- that no money available for investment under the Trust Deed will be invested in or lent to WABG, Sandhurst or, subject to certain specified exceptions, any person who is by virtue of the Corporations Law associated with WABG or Sandhurst(cl 11.1(g));
- that WABG will establish, manage and maintain the Plantations on behalf of Growers in accordance with good silvicultural practice and in accordance with the terms and conditions of the Project Management Contracts (cl 11.2(a));
- that the Representative will exercise due care and diligence in carrying out its functions (cl 12.1(a));
- that Sandhurst will send, or cause to be sent, to each of the Growers a statement of accounts of the Project together with the report of the Project Auditor within ninety (90) days after the end of each financial year (cl 12.1(g));
- that Sandhurst will take all reasonable steps necessary to become informed of the exercise by WABG of its powers and performance of its functions under the Trust Deed (cl 12.1(s));
- that, subject to certain specified conditions, each Grower may freely assign its rights and privileges under the Trust Deed, the Project Management Contract and the Sublease (cl 14.1);
- that Growers may, in certain specified circumstances, remove WABG as the Manager (cl 18.3);
- that the Project shall terminate on 4 June of the year 25 years after the date of the Prospectus provided, however, that the Growers may, by extraordinary resolution, vote to extend the period of duration of the Project. If Sandhurst and WABG agree to such extension, then the Project shall, to that extent, extend for such further period as may be determined by Sandhurst and WABG (cl 22.1( c)); and
- that Sandhurst and WABG may modify the Trust Deed, but only in certain prescribed circumstances (cls 24.1, 24.2 and 24.3).

## Project Management Contract

20. The parties to the Project Management Contract are WABG as Project Manager, Fortech as the Forestry Consultant, and the Grower.

21. The Project Management Contract recites:

- that the Grower is the registered proprietor, lessee or sublessee of the land specified in the schedule, or otherwise occupies the land;
- that the Grower desires to carry out forestry operations and the development of a plantation of *Eucalyptus globulus* on the Land for commercial wood production;
- that WABG has, and has access to, expertise in relation to management of *Eucalyptus globulus* plantations;
- that the Grower desires to engage WABG to carry out such services as are required to plant, manage and maintain a plantation of *Eucalyptus globulus* trees on the land; and
- that Fortech has agreed with WABG to provide supervisory services in respect of the services to be provided by WABG.

22. The Project Management Contract, among other things, provides:

- that, in consideration of the fees payable by the Grower under the contract, WABG will provide the services as are provided for in this Contract in accordance with the Management Plan (cl 3);
- that the Project Manager will perform, or cause to be performed, all the services in relation to the Land and the Plantation Crop, as are set out in the Management Plan (cl 4.1);
- that the services to be performed by WABG include (cl 4.2):
  - ◆ the establishment and management of the Plantation Crop in accordance with the Management Plan;
  - ◆ the planting of a plantation of eucalyptus trees pursuant to the specifications set out in the Wood Purchase Agreement;
  - ◆ tending, maintaining and generally monitoring and caring for the Plantation Crop;

- ◆ the provision of sufficient healthy *Eucalyptus globulus* seedlings to achieve a specified stocking rate; and
- ◆ at the cost to the Grower, the keeping of certain specified insurance policies.
- that Fortech will supervise WABG and provide advice to it as required or desirable (cl 5.1);
- that the Project Management Contract commences from the date of its execution and terminates when the whole of the Plantation Crop has been harvested for the first time, whenever that occurs (cl 6.1);
- that the Grower may express opinions and give recommendations to WABG relating to matters the subject of this contract and may, subject to certain limitations, object to and disallow any changes to the Management Plan (cl 9.1);
- that WABG agrees to give due consideration to the Growers' opinions expressed in writing (cl 9.2);
- that WABG does not have to carry out a Grower's recommendations (cl 9.3);
- that WABG shall provide certain specified reports to Growers each year and as soon as practicable following the completion of the planting of the Plantation Crop (cl 10);
- that Fortech will provide an annual report and reports as necessary to Growers (cl 10);
- that the Grower shall not assign or dispose of its rights and obligations under the Contract, unless the Grower provides to WABG an indemnity in respect of the performance by the proposed Assignee of each obligation of the Grower under the Contract (cl 11.9);
- that the harvesting of the Plantation Crop shall be conducted in accordance with the terms of the Wood Purchase Agreement (cl 12.1); and
- that, in consideration of the performance by WABG of its duties and obligations under the Contract, the Grower agrees to pay WABG the following charges:
  - ◆ \$4,500 per hectare to be paid on or before 30 June 1999 for services in respect of the establishment and management of the Plantation

Crop until 27 July 2000, in accordance with the Management Plan;

- ◆ for the annual management of the Plantation Crop from 28 July 2000 until the Plantation Crop has been harvested for the first time, \$70 per hectare of the Plantable Area per year, indexed, with the first amount being payable on 28 February 2000 and, thereafter, on 28 February in each year; and
- ◆ in addition to the above fees, WABG will be entitled to 12.5% of the difference between the amount due to the Grower from the first Harvest of the Plantation Crop and the sum of \$9,250, indexed, per hectare of Plantable Area multiplied by the number of hectares of Plantable Area.

## Sublease

23. The parties to the Sublease are the Landholder and the Grower.

24. The Sublease recites that the Landholder holds a lease or sublease over the land specified in the Schedule and that the Landholder has agreed to sublet to the Grower the Leased Area for the purpose of planting, tending and harvesting a plantation of eucalyptus trees for commercial wood production.

25. The Sublease, among other things, states:

- that the Landholder subleases to the Grower and the Grower takes a sublease of the Leased Area for the Term (cl 4.1);
- that the Term may not exceed the period that is one day less than the Head Lease (cl 4.2);
- that, subject to complying with certain specified conditions, the Grower may extend the Term of the Sublease (cl 5.1);
- that, as consideration for the granting of the Sublease, the Grower shall pay to the Landholder, during the term of the Sublease, the rent as follows:
  - ◆ for the first year of the term, the amount of \$265 per hectare of the Plantable Area payable on 15 November 1999;
  - ◆ for the second and subsequent years of the term, subject to certain specified procedures for

adjustment, the amount of the rent payable for the previous year, indexed, payable on 30 September during the relevant year, provided that in no event shall the rent be less than that payable for the previous year (cl 6);

- that the Grower agrees to establish, tend and maintain the Plantation Crop in a proper and skilful manner, and in accordance with sound silvicultural and environmental practices adopted within the forestry industry (cl 7.2);
- that the Grower agrees to leave all stumps, roads and tracks on the Leased Area at the expiry of the term of the Sublease (cl 7.9);
- that the Landholder shall, subject to certain specified qualifications, and upon the Grower paying the rent and observing and performing the covenants and stipulations contained in the Sublease, permit the Grower peaceably and quietly to hold the Leased Area during the term (cl 8.1);
- that each Party has full and free right to assign its rights under this Sublease, provided the transferring Party first obtains a deed of covenant by the proposed assignee including a covenant by the Grantee in favour of the non-transferring Party that the Grantee will, at all times, observe and perform all or any of the covenants contained or implied in this Sublease to be observed or performed by the transferring party (cl 9.13);
- that the Parties acknowledge and agree that the Plantation Crop is, and shall remain, the property of the Grower until the end of the Term and the Grower shall be entitled to harvest the Plantation Crop and retain all income from the sale thereof (cl 9.18); and
- that the Sublease Commencement Date is 30 June 1999 and the term of the Sublease is from 30 June 1999 until the expiration of 12 years, or until the completion of first harvesting, whichever occurs first (Parts 4 and 5 of the Schedule).

**‘Plantation Services Agreement 1999 – xxx 99 Treefarm’**

26. The parties to the ‘Plantation Services Agreement – xxx 99 Treefarm’ are WABG as Project Manager and Treefarms as Contractor. The agreement, among other things, provides:

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- that WABG engages Treefarms to carry out the Plantation Services during the term of this Agreement in accordance with the Plantation Development and Maintenance Plan and on the terms and conditions set out in this Agreement (cl 3);
- that, subject to certain specified qualifications, the term of this Agreement expires on the earlier of the termination of the Sublease and the date that harvesting of the Plantation Crop takes place for the first time (cl 4);
- that, in consideration of the performance by Treefarms of its duties and obligations as set out in this Agreement, WABG agrees to pay to Treefarms:
  - ◆ in respect of planting and maintenance of the Plantation Crop until 30 July 2000 in accordance with the Plantation Development and Maintenance Plan, an initial amount per hectare unit of the land, payable in instalments over the thirteen month period between 1 July 1999 and 30 June 2000 (cl 5(a) and Part 3(a) of the Schedule); and
  - ◆ in respect of the annual maintenance of the Plantation Crop in accordance with the Plantation Development and Maintenance Plan, a amount per hectare unit per annum for each year, commencing on 30 June 2000 payable annually in arrears, on or before 30 June each year of the term of the Agreement, as reviewed from time to time pursuant to the process outlined in the Agreement (cls 5(b) and 5(c) and Part 3(b) of the Schedule);
- that Treefarms agrees with WABG to carry out, or cause to be carried out, such services and duties as are set out in the Plantation Development and Maintenance Plan (cl 6(a));
- that, among other things, Treefarms shall:
  - ◆ establish, tend and maintain the Plantation Crop in accordance with the Plantation Development and Maintenance Plan;
  - ◆ infill or replant any part of the Plantation Crop that fails to achieve the survival objective; and
  - ◆ acquire seeds or seedlings on behalf of WABG (cl 6(b));

- that Treefarms shall commence to carry out, or cause the commencement of the carrying out, of the Plantation Services on or before 30 June 1999 (cl 6(c)); and
- that Treefarms agrees to provide all reasonable assistance to Fortech to enable Fortech properly to supervise the planting and tending of the Plantation Crop and to perform Fortech's other obligations to WABG and the Growers (cl 20).

#### **'Wood Purchase Agreement 1999 - Treefarm'**

27. The Parties to the Wood Purchase Agreements are WABG as Representative, Treefarms as Purchaser, and the Grower(s) listed in the Schedule to the Agreement. The Wood Purchase Agreement, among other things, provides:

- that the Grower(s) agrees to sell and Treefarms agrees to purchase all wood grown on the Hectare Units described against each Grower's name in Part 1 of the Schedule on the terms and conditions set out in this Agreement (cl 3(a));
- that, if the parties do not agree that Treefarms may use the wood for a use other than woodchipping, the Grower may retain up to 10% of the total quantity of wood following harvesting for sale for a purpose other than woodchipping (cl 3(b));
- that the purchase price shall be calculated in accordance with the terms of this Agreement and shall be paid in respect of all wood harvested and delivered in accordance with the Harvest Plan (cl 3(c));
- that Treefarms may use the wood so purchased for:
  - ◆ woodchipping or for sale for woodchipping; or
  - ◆ if the Parties agree, any other use yielding a higher return to the Grower (cl 3(d));
- that the purchase price (if any) shall be paid by Treefarms after the twentieth day of and before the end of the month following delivery of the wood, in accordance with the Harvest Plan (cl 3(e));
- that the Grower irrevocably authorises and directs Treefarms to pay any moneys payable by Treefarms to the Grower under this Agreement direct to WABG (cl 3(g));

- that a Harvest Plan must commence to be negotiated between Treefarms and WABG at least 5 to 6 months before Treefarms requires delivery of the wood to commence (cl 4);
- that Treefarms will give WABG notice of the proposed purchase price and a fixed quote for the harvesting and delivery of the wood to the nominated facility at least 2 months prior to the date on which harvesting will commence (cl 5);
- that the Proposed Purchase Price for the wood must be fair and reasonable, taking into account certain specified factors (cl 6(a));
- that WABG can negotiate another purchase price with Treefarms for the wood if it does not approve the purchase price initially offered and, if unsuccessful in those negotiations, can sell the wood to another purchaser provided certain pre-conditions are complied with (cl 6(b));
- that ownership of, and risk in relation to, the wood shall pass from the Grower to Treefarms only upon acceptance by Treefarms of the wood at the facility(s) nominated in the Harvest Plan, as meeting the specifications set out in the Harvest Plan (cl 8(1));
- that the earliest date for Delivery to commence is 15 April 2007, providing that no harvesting shall take place prior to 1 July 2009 unless the Plantation Crop is estimated to produce a minimum of 320 cubic metres per hectare of wood (Part 4(1) of the Schedule); and
- that the latest date for Delivery to be completed is 14 April 2012 (Part 4(2) of the Schedule).

## **Finance and the Loan Agreement**

28. The Prospectus outlines a finance option offered by Albany, a company associated with WABG. The Prospectus states that finance is available to all participating Growers to a maximum of 80% of the amount that must be paid immediately by the Grower in respect of the Project Management Contract. It also states that the amounts borrowed are to be repaid in instalments (comprising both principal and interest) over the period ending on 30 September 2003. If taken up, the loan transaction is evidenced by the execution of a Loan Agreement between Albany, as financier, and the Grower, as borrower.

29. The Loan Agreement, among other things, provides:
- that, in consideration of the Grower entering into an Agreement with WABG to manage certain forestry operations on the leased land described in the Schedule to the Agreement, Albany agrees to advance to the Grower the principal sum specified in the said Schedule (cl 1);
  - that the Grower agrees to repay the principal sum by nine instalments (cl 2 and the Schedule);
  - that the Grower shall pay interest at the rate of 8.6% per annum on the amount of the principal sum outstanding from time to time on the same dates as are used for the repayment of principal (cl 3); and
  - that the Grower assigns, transfers and sets over to Albany by way of security all its right, title and interest in and under the Plantation Management Contract, the Sublease, the Wood Purchase, all money payable to the Grower under the Wood Purchase Agreement, and the insurances effected in respect of the forestry operations on the land and all money payable to the Grower under such Insurances, provided that, upon the repayment of the Principal Sum, interest thereon and all other money secured by this Agreement, this assignment shall be void and of further effect (cl 6).

**Statements made in the Application, in written communications between the ATO and WABG's solicitor relevant to the Application, and in discussions with WABG's solicitor**

30. WABG, or its solicitor, makes the following statements in support of the Application:
- that loans provided under the finance facility provided by Albany will be made on a full recourse basis;
  - that Albany will sue Growers in the event of a loan default;
  - that no Growers' Contributions made in relation to the Project are lent by WABG to Albany or any other entity associated with Albany;
  - that all loans made by WABG to Albany are made at commercial rates of interest and are sourced from amounts earned by WABG in carrying on its income-earning activities in years prior to the year in which the relevant loan was made to Albany;

- that no Growers' Contributions made in relation to the Project are lent by WABG to Bunbury Option Pty Ltd ('Bunbury') or any other entity associated with Bunbury; and
- that all loans made by WABG to Bunbury are made at commercial rates of interest and are sourced from amounts earned by WABG in carrying on its income-earning activities in years prior to the year in which the relevant loan was made to Bunbury.

## Ruling

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### Section 8-1

31. Provided that the Project's Minimum Subscription level of \$300,000, mentioned in the Prospectus at page 3, is achieved during the year ending 30 June 1999, where a Grower acquires an interest in the Project in the year ending 30 June 1999, the following outgoings will be allowable deductions under section 8-1 of the ITAA 1997 in respect of the years of income mentioned below:

#### *Year of income ending 30 June 1999*

- the initial fee of \$4,500 per hectare incurred under the Project Management Contract for services in respect of the establishment and management of the Plantation Crop until 27 July 2000; and
- where fire insurance has been taken out by WABG on behalf of the Grower pursuant to clause 4.2(j)(ii) of the Project Management Contract during the year ending 30 June 1999, the amount representing the Grower's share of the insurance premium paid or payable by WABG in respect of that insurance.

#### *Year of income ending 30 June 2000*

- the annual management / maintenance fee of \$70 per hectare payable under the terms of the Project Management Contract on 28 February 2000;
- the rental payment of \$265 per hectare payable under the terms of the Sublease on 15 November 1999;
- where fire insurance has been taken out by WABG on behalf of the Grower pursuant to clause 4.2(j)(ii) of the Project Management Contract during the year ending 30 June 2000, the amount representing the Grower's

share of the insurance premium paid or payable by WABG in respect of that insurance; and

- the interest expense that either has been paid or has fallen due for payment during the year of income ended 30 June 2000, where that interest is incurred by the Grower in respect of a loan from Albany taken out to finance the payment of fees owing under the Project Management Contract.

***Year of income ending 30 June 2001***

- the annual management / maintenance fee of \$70 per hectare, indexed, payable under the terms of the Project Management Contract on 28 February 2001;
- the amount of rental payment for the previous year, indexed, payable under the terms of the Sublease on 30 September 2000, as set out in Part 3.2(ii) of the Sublease;
- where fire insurance has been taken out by WABG on behalf of the Grower pursuant to clause 4.2(j)(ii) of the Project Management Contract during the year ending 30 June 2001, the amount representing the Grower's share of the insurance premium paid or payable by WABG in respect of that insurance; and
- the interest expense that either has been paid or has fallen due for payment during the year of income ended 30 June 2001, where that interest is incurred by the Grower in respect of a loan from Albany taken out to finance the payment of fees owing under the Project Management Contract.

**Section 82KZM**

32. Section 82KZM of the ITAA 1936 will not apply to deny deductions otherwise allowable to Growers under section 8-1 in respect of expenditure incurred in relation to the Project mentioned at paragraph 31, or interest on a loan(s) taken out with Albany to finance the payment of fees owing under the Project Management Contract.

**Section 82KL**

33. Section 82KL of the ITAA 1936 will not apply to deny deductions otherwise allowable to Growers under section 8-1 in respect of expenditure incurred in relation to the Project mentioned at

paragraph 31, or interest on a loan(s) taken out with Albany to finance the payment of fees owing under the Project Management Contract.

## Part IVA

34. The provisions in Part IVA will not be applied to cancel a tax benefit obtained in connection with the arrangement where that tax benefit occurs as a result of an application of a tax law dealt with in this Ruling.

## Explanations

### Section 8-1

#### *Amounts payable by Growers under the Project Management Contract and the Sublease*

35. Consideration of whether amounts payable under the Project Management Contract and Sublease are deductible under section 8-1 begins with the first limb of the section. This view 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 the second limb if they are incurred when the business has not commenced; and
- where all that happens in a year of income is that a taxpayer contractually commits himself/herself 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 the second limb applies. However, that does not preclude the application of the first limb in determining whether the outgoings in question have a sufficient connection with activities to produce assessable income.

36. An afforestation scheme can constitute the carrying on of a business. Where there is a business, or a future business, the gross sale proceeds from the sale of the timber from the scheme will constitute gross 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 trees.

37. Generally, an investor will be carrying on a business of afforestation where:

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

38. For this Project, Growers have, under the Sub-lease Agreement, rights in the form of a sublease over an identifiable area of land consistent with the intention to carry on a business of growing trees. Under the Project Management Contract, Growers appoint WABG, as Project Manager, to provide services such as planting, tending, maintaining and otherwise caring for the trees. Growers control their investment. On behalf of Growers, WABG will ensure that the purchase price paid for the wood will be fair and reasonable.

39. The Sublease gives Growers more than a chattel interest in the wood on harvest. The Project documentation contemplates Growers will have an ongoing interest in the growing trees: a leasehold interest or an interest under a sublease usually confers on an investor an identifiable interest in specific trees in the area covered by the lease, or sublease, as the case maybe.

40. Growers have the right to use the land in question for afforestation purposes and to have WABG and Treefarms, as Contractor, come onto the land to carry out their obligations under the Project Agreements. The Growers' degree of control over WABG, as evidenced by the Project Agreements and supplemented by the Corporations Law, is sufficient. Under the Project Agreements, Growers are entitled to receive regular progress reports (including annual written reports) on WABG's activities. Growers are able to terminate arrangements with WABG in certain instances, including, but not limited to, cases of default or neglect. The afforestation activities described in the Project Management Contract are carried out on the Growers' behalf.

41. The general indicators of a business, as used 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. The Independent Forester's Report indicates that he is confident that 'the proposed plantings will be successful'. 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 an 'after 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.

42. 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 silvicultural practices and are of the type ordinarily found in afforestation ventures that would commonly be said to be businesses.

43. Growers have a continuing interest in the trees from the time they are acquired until harvest. The afforestation 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' afforestation activities will constitute the carrying on of a business.

44. The fees associated with the afforestation 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 wood) is to be gained from this business. They will be deductible under the first limb of section 8-1. Further, no 'non-income producing' purpose in incurring the fee is identifiable from the arrangement. The tests of deductibility on the outgoings ruled upon under the first limb of section 8-1 are met. The exclusions do not apply.

### **Insurance premiums**

45. Under clause 4.2(j)(ii) of the Project Management Contract, WABG is, subject to certain specified qualifications, required to keep a policy of fire insurance at the Grower's expense. The Grower's share of any insurance recoveries under the above policies will be assessable, thus the Grower's share of insurance premiums paid will have a sufficient connection with the gaining or producing of assessable income. The expenditure is required under the Project Management Contract, and is relevant and incidental to the operations which more directly gain or produce the assessable income. These insurance premiums will have a sufficient connection with the Grower's gaining of assessable income. No capital, private or domestic component is identifiable in respect of them. The Grower's share of the insurance premiums will be deductible under section 8-1.

### **Interest deductibility**

46. Some Growers intend to finance their investment in the Project through a loan facility offered by Albany. Whether the interest expenses are deductible under section 8-1 depends on the same reasoning as that applied to whether the initial fee, the rental amounts

or the annual management / maintenance fees will be deductible. The interest expenses incurred in the years ending 30 June 2000 and 30 June 2001 will be in respect of a loan to finance the services to be performed under the Project Management Contract that will be directly connected with the gaining of 'business income' from the Project. These expenditures will have a sufficient connection with the gaining of assessable income. No capital, private or domestic component is identifiable in respect of them.

### **Section 82KZM**

47. Under the Project Management Contract, the initial fee of \$4,500 per hectare will be payable on or before 30 June 1999. This fee is expressly stated to be for specified services to be undertaken in the establishment and management of the Plantation Crop until 27 July 2000 in accordance with the Management Plan. No explicit conclusion can be drawn from the arrangement's description that the 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 the fee could not be wholly provided within 13 months of the Grower incurring the expenditure in question. For the purposes of this Ruling, it can be accepted that no part of the fee of \$4,500 is for WABG doing 'things' that are not to be wholly done within 13 months of the fee 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 by Growers on the initial fee of \$4,500 per hectare.

### **Section 82KL**

48. Section 82KL's operation depends, among other things, on the identification of a certain quantum of 'additional benefit(s)'. Here, there may be a loan provided by Albany to the Grower. It will be at commercial rates of interest, involve repayments of principal and the payment of interest in nine instalments over a period of four (4) years and be provided on a full recourse basis. In relation to the loan, either insufficient or no 'additional benefits' will be provided to trigger the application of section 82KL. Section 82KL will not apply to deny interest deductions otherwise allowable under section 8-1 in respect of the abovementioned loans.

49. Section 82KL will also not apply to deny deductions otherwise allowable in respect of the obligations to pay initial fees, rental amounts, annual management / maintenance fees or the Grower's share of fire insurance premiums.

**Part IVA**

50. 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 'WA Blue Gum Project - Prospectus 1999' will be a 'scheme'. It commenced in the period leading up to the issue of the Prospectus on 14 May 1999. The Growers will obtain, for example, 'tax benefits' from entering into the scheme, in the form of deductions for the amounts referred to in paragraph 31 above, allowable under section 8-1, 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 these tax benefits.

51. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the eventual harvesting of the whole of the trees for the first time. Further, there are no features of the Project, such as, for example, any of the initial fees, the annual management / maintenance fees or the rental amounts being 'excessive', uncommercial and predominantly financed by a non-recourse loan, 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**

30 June 1999

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*Previous draft:*

No draft issued

*Related Rulings/Determinations:*

PR 98/1; PR 1999/14; TR 92/1;  
TR 94/25; TR 97/11; TR 97/16;  
TD 93/34

*Subject references:*

- carrying on a business
- commencement of business
- fee expenses
- management fees expenses

- land use fees
- plantation forestry
- primary production
- primary production expenses
- producing assessable income
- product rulings
- public rulings
- schemes and shams
- seeds/seedlings fees
- taxation administration
- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters

# PR 1999/85

- tax shelters project
- timber industry

- ITAA1936 177C
- ITAA1936 177D
- ITAA1936 Pt IVA
- ITAA1997 8-1

*Legislative references:*

- ITAA1936 82KL
- ITAA1936 82KZM
- ITAA1936 177A

*Case references:*

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