

PR 1999/89 - Income tax: Old Stornoway Vineyard Project

⚠ This cover sheet is provided for information only. It does not form part of *PR 1999/89 - Income tax: Old Stornoway Vineyard Project*

⚠ This document has changed over time. This is a consolidated version of the ruling which was published on *25 August 1999*



Product Ruling

Income tax: Old Stornoway Vineyard 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.*

No guarantee of commercial success

The Australian Taxation Office (ATO) **does not** sanction or guarantee this product as an investment. Further, we give no assurance that the product is commercially viable, that charges are reasonable, appropriate or represent industry norms, or that projected returns will be achieved or are reasonably based.

Potential investors must form their own view about the commercial and financial viability of the product. This will involve a consideration of important issues such as whether projected returns are realistic, the 'track record' of the management, the level of fees in comparison to similar products, how the investment fits an existing portfolio, etc. We recommend a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential investors by confirming that the tax benefits set out below in the **Ruling** part of this document are available, **provided that** the arrangement is carried out in accordance with the information we have been given, and have described below in the **Arrangement** part of this document.

If the arrangement is not carried out as described below, investors lose the protection of this Product Ruling. Potential investors may wish to seek assurances from the promoter that the arrangement will be carried out as described in this Product Ruling.

Potential investors should be aware that the ATO will be undertaking review activities to confirm the arrangement has been implemented as described below.

What this Product Ruling is about

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 person, who take part in the arrangement to which this Ruling relates. In this Ruling this arrangement is sometimes referred to as 'the Old Stornoway Vineyard Project No 1', 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');
 - section 42-15 of the ITAA 1997;
 - section 43-25 of the ITAA 1997;
 - section 387-125 of the ITAA 1997;
 - section 387-185 of the ITAA 1997;
 - Part IVA of the *Income Tax Assessment Act 1936* ('ITAA 1936');
 - section 82KL of the ITAA 1936; and
 - section 82KZM of the 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 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. 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

7. This Ruling applies prospectively from **25 August 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).

8. 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

9. 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

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

- Application for a Product Ruling lodged by Tasvinum Management Pty Ltd ('TVM') dated 11 June 1999, together with the application's attachments listed below ('the application'):
 - ◆ a copy of a draft information memorandum titled '“Old Stornoway” Vineyard Project No.1'

which was proposed to be issued by Tasvinum Group Limited ('TVGL') in June 1999;

- ◆ an unexecuted copy of a standard form agreement titled 'Lease and Management Agreement', which will be entered into by each Grower, TVGL and Tasvinum Pty Ltd ('Tasvinum') in respect of an area of the proposed vineyard amounting to 0.086 hectares ('the LM Agreement No 1');
- ◆ a copy of an executed grape supply agreement dated 21 August 1998 between a certain named company which owns and operates wineries ('Wine Co 1') and Tasvinum ('Grape Sale Agreement No 1');
- ◆ a copy of an executed Deed of Assignment of Agreement dated 25 May 1999 between Tasvinum as assignor, TVGL as assignee, and Wine Co 1 ('Deed of Assignment No 1');
- ◆ a copy of an undated executed fruit sale and purchase agreement between another named company ('Wine Co 2') and TVM ('Grape Sale Agreement No 2');
- ◆ a copy of an executed Deed of Assignment of Agreement dated 25 May 1999 between TVM as assignor, TVGL as assignee, and Wine Co 2 ('Deed of Assignment No 2');
- ◆ an unexecuted copy of a standard form agreement titled 'Loan Agreement – Old Stornoway Vineyard Project No.1', which will be entered into by OFS Australia Pty Ltd ('OFSA') and each Grower who wishes to take up the loan facility offered by OFSA ('the Loan Agreement');
- ◆ a copy of a taxation opinion in respect of the 'Old Stornoway Vineyard Project No 1' prepared by the Project's independent Tax Advisor;
- ◆ a copy of a unaudited general purpose financial report for the period ended 25 May 1999 prepared for TVGL by the Project's independent Accountant;
- ◆ a copy of a balance sheet for TVM for the period ended 31 March 1999;

- ◆ a copy of a schedule titled ‘Old Stornoway Vineyard Expenditure by Investor’;
- ◆ a copy of a schedule titled ‘Investor Flow of Funds’;
- ◆ a copy of a schedule titled ‘Breakdown of Management Fee’;
- ◆ a copy of a schedule titled ‘Old Stornoway Vineyard Expenditure – After Tax Cash Flow Projection’;
- a letter from the Project’s independent Tax Advisor dated 18 June 1999 together with a copy of a document titled ‘ “Old Stornoway” Vineyard Project No.1 – Information Memorandum’ issued by TVGL and dated 18 June 1999 (‘the Information Memorandum’);
- a printed copy of an e-mail message dated 22 June 1999 from the Project’s independent Tax Advisor to the ATO;
- a printed copy of an e-mail message dated 29 June 1999 from the Project’s independent Tax Advisor to the ATO;
- a printed copy of an e-mail message dated 30 June 1999 from the Project’s independent Tax Advisor to the ATO;
- a printed copy of an e-mail message dated 5 July 1999 from the Project’s independent Tax Advisor to the ATO;
- a printed copy of an e-mail message dated 8 July 1999 from the Project’s independent Tax Advisor to the ATO, together with a revised version of the document titled ‘Constitution of the “Old Stornoway” Vineyard Project No. 1’ (‘the Constitution’);
- a printed copy of an e-mail message dated 9 July 1999 from the Project’s independent Tax Advisor to the ATO;
- a copy of an unexecuted and undated agreement between TVGL and TVM in which the parties agree that TVM will be appointed to manage the viticultural project on the land described in the schedule to the agreement owned by Tasvinum (‘the Vineyard Management Agreement’);

- a printed copy of an e-mail message dated 16 July 1999 to the Project's independent Tax Advisor from the ATO together with an issues paper developed by the ATO also dated 16 July 1999;
- a copy of a letter to the ATO from the Project's independent Tax Advisor dated 23 July 1999 together with its attachments;
- a printed copy of an e-mail message dated 23 July 1999 from the Project's independent Tax Advisor to the ATO together with its attachments; and
- a letter from TVM to the ATO dated 9 August 1999.

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

11. For the purposes of describing the arrangement to which this Ruling applies, except for the agreements reflected by the documents listed at paragraph 12, 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, is or will be a party.

The Information Memorandum

12. TVGL issued an Information Memorandum in relation to the Project on 18 June 1999. It states, among other things, that:

- investments in the Project are 'excluded issues' for the purposes of the Corporations Law;
- the minimum initial investment per investor will be 11 interests in the Project at \$517,495.00, unless the Investor satisfies, or all Investors satisfy, other requirements for an excluded offer or excluded issue under the Corporations Law;
- the term of the Project will be approximately 16 years from 1 July 1999 to about 30 June 2015;
- TVGL expects that harvesting of the 2014/2015 fruit crop will be completed by 31 May 2015 and that all fruit from that harvest will be sold by 30 June 2015;
- TVGL expects that the proceeds from the sale of the 2014/2015 fruit crop harvest will be collected by 2015;

- the Project will terminate when the proceeds from the sale of the 2014/2015 fruit crop have been distributed to Growers;
- the Project is governed by a Constitution binding TVGL and Growers;
- key features of the Project include:
 - ◆ the establishment and operation of a 48 hectare vineyard in northern Tasmania at Relbia, and also the operation of a 10 hectare vineyard already established in northern Tasmania at Relbia (collectively described as ‘the vineyard’);
 - ◆ an expectation that there will be a commercial harvest for the first time in 2002;
 - ◆ the pre-sale of all wine grapes on 50 hectares of the vineyard to 2015;
 - ◆ the pre-sale of all wine grapes from the remaining 8 hectares to 2008;
- the offer to investors incorporates the following features:
 - ◆ 116 interests will be available in the Project;
 - ◆ each interest will incorporate, among other things, rights to occupy, for the term of the Project, two separate areas in the vineyard totalling, in aggregate, 0.5 hectares;
 - ◆ the abovementioned rights to occupy will be set out in two separate lease and management agreements, LM Agreement No 1 and LM Agreement No 2:
 - (i) LM Agreement No 1 will be in respect of an area of 0.086 hectares derived from that portion of the vineyard that, at the date of the Information Memorandum, has had improvements such as surveying, row pegging, deep ripping, fertilising, trellising and planting already carried out on it; and
 - (ii) LM Agreement No 2 will be in respect of an area of 0.414 hectares derived from that portion of the vineyard that, at the date of the Information Memorandum,

has had no development works carried out on it, save for the clearing of the land;

- ◆ the Project will commence on the execution of the lease and management agreements;
- ◆ there will be a planting of 1,200 vines per interest, split between the two leased areas comprising each interest;
- ◆ on applying to participate in the Project, Growers will be required to pay \$47,045.00 per interest, being the total rental amounts and annual management fees in respect of both leased areas for the period commencing on the commencement date of the relevant Grower's lease and management agreements and ending on 30 June 2003;
- ◆ for the balance of the Project's term after 30 June 2003, Growers will be liable to pay rental amounts and management fees on an annual basis in the amounts set out at pages 19 and 20 of the Information Memorandum;
- ◆ with respect to the rental amounts and management fees payable by Growers after 30 June 2003, these amounts may be deducted out of 'Gross Sale Proceeds' from the sale of grapes from the Growers' leased areas in each year;
- ◆ if the Gross Sale Proceeds from the sale of grapes from the leased areas is insufficient in any year to meet the rental amounts and management fees due in respect of that year, the Grower must pay the balance;
- ◆ income after expenses from the sale of the grapes harvested will belong to Growers;
- ◆ the Information Memorandum seeks to raise \$5,457,220.00 from up to 20 investors, although the Minimum Subscription required for the Project to proceed is \$2,352,250 (the equivalent to a subscription for 50 interests);
- ◆ no rental amounts or management fees will be paid out of the Application Monies until the Minimum Subscription is reached;

- ◆ there is expected to be a pre-tax internal rate of return of 9.88%; and
- ◆ finance is available, but not a pre-requisite for investment;
- Project Management will be structured as follows:
 - ◆ TVGL will manage the Project as Project Manager in accordance with the terms of the Constitution;
 - (i) TVGL will be responsible for establishing that portion of the vineyard not already established, and will also be responsible for managing the whole vineyard until completion of the 2015 harvest and sale of grapes and the distribution of the proceeds therefrom;
 - (ii) TVGL will be able to delegate its obligations and has a Vineyard Management Agreement in place with TVM under which TVM will establish and manage the Project on behalf of Growers, as well as look after the marketing, harvesting and selling of grapes grown on the vineyard;
 - ◆ Tasvinum, being owner of the land at Relbia comprising the leased areas, will lease those leased areas to Growers whose applications to participate in the Project are accepted;
 - ◆ applicants will enter into lease and management agreements with Tasvinum (as the Landowner) and TVGL (as Project Manager) to lease their leased areas for a period of 16 years on condition that TVGL establish the remaining undeveloped part of the vineyard and carry on the future management and maintenance of the whole of the leased areas;
 - ◆ Tasvinum and TVGL are related corporations;
- the Project Structure and Application Process is as follows:
 - ◆ applications to participate in the Project must be made on the Application Form attached to the Information Memorandum;

- ◆ TVGL has a discretion to refuse any application;
- ◆ the Application Money of \$47,045 per interest relates to the first 4 years of the Project and is comprised of:
 - (i) the management fees relating to the establishment of the vineyard on the leased area covered by LM Agreement No 2;
 - (ii) the annual management fees for the first 4 years of the Project in respect of both the leased areas comprising each interest in the Project;
 - (iii) the rental amounts for both the leased areas comprising each interest in the Project;
 - (iv) the payment for the rootstock for vines to be planted on the leased area of 0.414 hectares to be derived from that portion of the vineyard that, at the date of the Information Memorandum, has had no development works carried out on it, save for the clearing of the land;
- ◆ as at the date of the Information Memorandum, vineyard establishment works have been completed on 10 hectares of the vineyard and the rental amounts charged in relation to this area reflect the improved value of that land arising from the completed establishment works;
- ◆ vineyard development costs in relation to the undeveloped portion of the vineyard on the remaining 48 hectares of Project land will be paid for by Growers as part of the Management Fee under their Lease and Management Agreement;
- ◆ funds invested by each Grower may, pending expenditure on the Project, be applied by TVGL to investments in viticulture or to investments authorised under the Constitution;
- ◆ TVGL will, through TVM, maintain public liability insurance with a specified insurance

- broker for amounts designated in the Information Memorandum;
- ◆ Growers will be responsible for obtaining their own insurance in relation to other risks on the leased areas;
 - ◆ TVGL will not borrow moneys on behalf of Growers;
 - ◆ Tasvinum has granted a first mortgage to an Australian bank over the land on which part of the vineyard is already established, and also over the land on which it is proposed to develop a further part of the vineyard, in order to secure the loan funds that that bank will make available to OFSA which, in turn, will on-lend those funds to Growers to finance their investments in the Project;
- subject to the assumptions set out at page 21 of the Information Memorandum, income and cash flow projections are as follows:
 - ◆ where a Grower self-finances his/her investment in the Project, a profit of \$43,709 per interest over the 16 years of the Project; and
 - ◆ where a Grower has borrowed 90% of the funds required for the investment at an interest rate of 9.5% per annum, a profit of \$13,798 per interest over the 16 years of the Project;
 - the Project's material contracts are:
 - ◆ the Constitution;
 - ◆ the lease and management agreements;
 - ◆ the vineyard management agreement;
 - ◆ Grape Sale Agreement No 1;
 - ◆ Grape Sale Agreement No 2;
 - ◆ the marketing agreement; and
 - ◆ the loan agreement.

The Application Form attached to the Information Memorandum

13. By signing the Application Form, the applicant agrees and acknowledges, amongst other things:

- that the application is made subject to the information memorandum;
- that he/she will be bound by the terms and conditions of the Constitution and any subsequent amendments which may be made by TVGL; and
- that he/she appoints TVGL to be his/her attorney for the purposes specified on the form.

The Constitution

14. The Constitution states, among other things, that:
- TVGL will hold the Project property (i.e., all the property, rights and income of the Project) on trust for the Growers;
 - the Constitution binds TVGL and each present or future Grower (but not the Growers inter se) in accordance with its terms as if each had been a party to it;
 - the Grower has:
 - ◆ the right to attend and vote at meetings of Growers;
 - ◆ the right, as at midnight on the last day of a Distribution Period, to receive a share of Net Income (if any) for the Distribution Period on a pro rata basis with other interests;
 - ◆ the right to participate in the division of any surplus assets or profits of the Project on a pro rata basis with all other interests on the winding up of the Project;
 - the interests of each Grower in the Project and in the Leased Area(s) are set out in this Constitution and the Lease and Management Agreement;
 - TVGL will manage the Project on behalf of each Grower;
 - the price to be paid on each issue of an interest will be the sum of:
 - ◆ the annual management fee payable under the lease and management agreements for the initial period, as set out in Schedule 2 of the Constitution ('Schedule 2');

- ◆ the rents payable under the lease and management agreements for the initial period, as set out in Schedule 2; and
- ◆ the cost of rootstock as set out in Schedule 2.
- there are certain conditions precedent (set out in clause 10) that must be fulfilled before TVGL can pay out any of the Application Money received;
- provided the conditions precedent in clause 10 have been complied with, TVGL may apply the Application Money as follows:
 - ◆ it must pay Tasvinum, ‘on behalf of each Grower, that portion of the Application Money paid by the Grower that relates to the Rent that is due and payable under clause 4 of the Lease and Management Agreements executed by or on behalf of the Grower in relation to each of the Leased Areas which are leased by the Grower, for the Initial Period’;
 - ◆ it must pay itself, ‘on behalf of each Grower, that portion of the Application Money paid by the Grower that relates to the Annual Management Fees that are due and payable under clause 25 of the Lease and Management Agreements executed by or on behalf of the Grower in relation to each of the Leased Areas which are leased by the Grower, for the Initial Period’; and
 - ◆ it must pay itself, on behalf of each Grower, that portion of the Application Money paid by the Grower that relates to the Rootstock Payment due and payable under clause 25 of the Lease and Management Agreements executed by or on behalf of the Grower;
- TVGL must establish a ‘Produce Fund’ for the purpose of receiving and distributing the proceeds from the sale of the grapes produced from the vineyard;
- TVGL holds the Produce Fund, on trust, as a separate and distinct fund, to be invested in accordance with the Constitution and distributed in accordance with the succeeding provisions of clause 12 of the Constitution;
- within 30 days after the last day of each Distribution Period, TVGL must, subject to certain specified conditions, distribute the Produce Fund to each of the

Growers in proportion to his or her Proportional Interest in the Net Sale Proceeds (i.e., the gross amount received from the sale of fruit from the Leased Areas less the amounts that TVGL is entitled to deduct from the gross amount under clauses 22.4 of LM Agreement No 1 and LM Agreement No 2);

- TVGL must deduct any amounts payable by the relevant Grower under the Lease and Management Agreements, or under any other provision of the Constitution, from the amounts to be distributed;
- each Grower must pay the Grower's Annual Contribution (i.e., the Grower's contribution to the annual fees and charges payable to TVGL for the Annual Management Fee, Rent and premiums payable on account of insurance relating to the leased area) payable under the Lease and Management Agreement for each leased area which is leased by the Grower, on the date that the Grower's Annual Contribution is payable under the Lease and Management Agreement;
- TVGL must apply the Grower's Annual Contributions in accordance with the relevant Lease and Management Agreement, or **at TVGL's absolute discretion**, any unpaid Annual Contribution of each Grower may be set off against any entitlement to Net Sale Proceeds of the relevant Grower;
- Growers are entitled annually to receive a copy of the accounts of the Project together with a copy of the auditor's report on those accounts;
- Growers are entitled annually to receive an independent expert's report on the performance of TVGL in managing the Project;
- each Grower is entitled to assign his/her interest in the Project subject to certain conditions and subject to TVGL's right to refuse to register such a transfer;
- each Grower irrevocably appoints TVGL and its nominees to be his/her attorney to execute and deliver certain specified documents;
- TVGL is entitled to be remunerated for its services under this Constitution, or a Lease and Management Agreement, by receiving from the relevant Grower, or out of the relevant Property, those fees provided for in any Lease and Management Agreement;

- TVGL is entitled to be reimbursed out of the Project Property for all costs, charges, expenses and outgoings reasonably and properly incurred by it under this Constitution;
- TVGL can be removed by a resolution of Growers demanding its retirement;
- subject to certain specified conditions, TVGL can alter, revoke or add to the provisions of this Constitution by a Deed executed by it; and
- the Project must be wound up and terminated on the first to occur of the following dates:
 - ◆ if the Growers by Special Resolution so determine, the date the Special Resolution is passed;
 - ◆ if TVGL considers it to be in the interest of Growers, the date TVGL so determines;
 - ◆ the day before the 80th anniversary of the commencement date of the Project; or
 - ◆ if wound up pursuant to the order of a court, the date of that order or such other date as the court may determine.

LM Agreement No 1

15. In general terms, LM Agreement No 1 confers upon a Grower a leasehold interest in the portion of the vineyard which, as at the date of the Information Memorandum, has had improvements such as surveying, row pegging, deep ripping, fertilising and planting already carried out on it. It also sets out the terms upon which the Grower engages TVGL to manage his /her interest in that portion of the vineyard. The parties to the Agreement are Tasvinum (as Landowner), TVGL (as Project Manager) and the relevant Grower.

16. More specifically, LM Agreement No 1 recites that, among other things:

- Tasvinum is, or is entitled to become, the registered proprietor of the land of which each area leased to the Grower forms part;
- the Grower has applied for interests in the Project and TVGL has accepted that application;
- the Grower wishes to appoint TVGL to:

- ◆ undertake certain defined works required to develop the Project; and
- ◆ manage the viticultural project on the Leased Area (and in that capacity, to manage and maintain the Project and to harvest the fruit);
- TVGL wishes to accept the appointment; and
- Tasvinum has installed certain pumping, bore water and other facilities which it has agreed to licence TVGL to use in relation to the Project.

17. It goes on to state, among other things, that:

- Tasvinum leases the leased area to the Grower for the term commencing on the Commencement Date (i.e., the date of execution of this Agreement by the last party to do so) and terminating on the Completion Date (i.e., whichever is the earlier of the following dates - (1) the date on which the Project is terminated under clause 37 of the Constitution; or (2) the 31st day of December 2015; or (3) the date on which the Grower receives its final payment for fruit harvested between 1 January and 30 June 2015 and sold pursuant to this agreement) subject to the provisions of the Agreement;
- the Grower must pay the rent in accordance with the processes set out in Items 5(1) and 5(2) of the Schedule to LM Agreement No 1 ('LM1 Schedule');
- the rent will be paid to Tasvinum:
 - ◆ **in respect of the Initial Period** (i.e., the period commencing on the Commencement Date to 30 June 2003), by TVGL on behalf of the Grower, from the Grower's Application Money (i.e., the amount payable by an applicant under the Information Memorandum for rootstock, rent and management fees during the initial period), on the due dates and for the periods specified in Item 5(1) of LM1 Schedule;
 - ◆ **after the Initial Period**, by TVGL on behalf of the Grower in accordance with clause 22 of the Agreement;
- the Grower will at all times keep the leased area, Tasvinum's fixtures, the vines and the trellises in good and substantial repair, order and condition, fair wear and tear excepted;

- the Grower will not install or remove, or permit any other person to install or remove on or from the lease area prior to the expiry of the lease, any earth, gravel, stones, sand minerals, or fixtures without first obtaining the written consent of Tasvinum which Tasvinum may in its absolute discretion withhold;
- subject to certain specified qualifications, the Grower may, during the Term of the lease remove the vines, trellises and other equipment which physically reside on the Grower's leased area;
- the qualifications are:
 - ◆ if the Grower wishes to remove the vines, trellises and other equipment that physically reside on the Grower's leased area, the Grower must request TVGL in writing to undertake or arrange such removal;
 - ◆ TVGL must comply with this request unless it reasonably considers that the requested removal would detrimentally affect the vines, trellises or other equipment of other Growers;
 - ◆ if TVGL agrees to a Grower's request to remove the vines, trellises and other equipment that physically reside on the Grower's leased area, the Grower will cease to have any further claim or rights in relation to the Trust, the Fund, the Project and the Leased Area and TVGL will become lessee of the leased area in place of the Grower;
- the Grower will at the expiration or prior to the termination of the term of the lease, peaceably surrender and yield up to Tasvinum the leased area and Tasvinum's fixtures (i.e., all fences, fittings, equipment and improvements leading through, over or into or situated on the leased area, other than the vines and the trellises) free and clear of rubbish and in good and substantial repair, order and condition;
- subject to certain specified qualifications, the Grower will at all times have full right, title and interest in the fruit from the leased area and have the right to have the fruit from the leased area sold for the benefit of the Grower;
- the Grower engages TVGL as an independent contractor to perform the works (i.e., all work required

to maintain the part of the vineyard the subject of this Agreement) on the land during the term of the lease;

- the Grower appoints TVGL to manage and maintain the leased area and to harvest the fruit from the leased area and TVGL accepts this appointment;
- TVGL is appointed as the Grower's agent for the purpose of marketing and selling the fruit from the leased area;
- TVGL will deposit the Gross Sale Proceeds from the sale of fruit into the Produce Fund;
- on or before the last day of each distribution period, TVGL will distribute the Produce Fund to each of the Growers in proportion to their respective proportional interest in the Produce Fund ('the Proportional Amount'), in accordance with the Constitution and after any deduction required under clause 22.4 of this Agreement;
- the deductions required under clause 22.4 are as follows:
 - ◆ if TVGL is entitled under the Constitution to deduct or recover and retain any other amounts, those amounts must be deducted and paid from the Grower's Proportional Amount to the appropriate person(s);
 - ◆ if the Grower's Annual Contributions are due and unpaid, TVGL must deduct those contributions and any interest payable thereon from the Grower's Proportional Amount and pay them to the appropriate person(s);
 - ◆ TVGL must deduct from the Proportional Amount any other amounts payable by the relevant Grower under this Agreement and pay them to the appropriate person(s);
- TVGL may apply any of the Gross Sale Proceeds received from the sale of fruit derived from a leased area in payment of the Grower's Annual Contributions for each financial year during that part of the lease term occurring after 30 June 2003;
- in consideration of TVGL performing the works and the services, the Grower agrees to pay TVGL the annual management fee;
- the annual management fee:

- ◆ **for the period to 30 June 2003**, will be paid to TVGL on behalf of the Grower from the Grower's Application Money (i.e., the amount payable by an applicant under the Information Memorandum for rootstock, rent and management fees during the initial period) on the due dates and for the periods specified in Item 4(1) of LM1 Schedule;
- ◆ **after 30 June 2003**, will be paid to TVGL by the Grower annually on the dates specified in Item 4(2) of LM1 Schedule;
- the annual management fee can be paid for out of a Grower's share of any Net Sale Proceeds from the sale of fruit from a leased area; and
- the Grower can assign its interests under the Agreement, subject to certain specified conditions.

LM Agreement No 2

18. The parties to LM Agreement No 2 are Tasvinum (as Landowner), TVGL (as Project Manager) and the relevant Grower.

19. The Agreement is set out in terms almost identical to those appearing in LM Agreement No 1, save that it is focused on that portion of the vineyard which, as at the date of the Information Memorandum, has had no development works carried out on it, except for land clearance. In general terms, it confers a leasehold interest in the said portion of the vineyard on the Grower and sets out the terms on which TVGL will establish and manage the Grower's interest in that portion of the vineyard over the term of the Project. As with LM Agreement No 1, the Schedule to the Agreement ('LM2 Schedule') sets out the due dates for payment of amounts payable under the Agreement for management fees, rental amounts and insurance premiums. It also specifies the due date for payment of the rootstock payment referred in the Agreement.

The Vineyard Management Agreement

20. The parties to the Vineyard Management Agreement are TVGL (as Project Manager) and TVM (as Vineyard Manager). Under the Agreement, TVGL appoints TVM to manage the viticultural project on the land owned by Tasvinum, which will be leased by Growers. In particular, TVM agrees:

- to develop, manage and maintain the vineyard, to plant and nurture the vines and to harvest the fruit from the

leased areas by performing the services specified in clause 4.2 of the Agreement; and

- to perform (or to arrange for other persons to perform) the services specified in the Agreement in a proper, efficient and diligent manner and in accordance with industry best practice.

Grape Sale Agreement No 1

21. The parties to Grape Sale Agreement No 1 are Wine Co 1 and Tasvinum.

22. Under Grape Sale Agreement No 1, Wine Co 1 agrees to purchase from Tasvinum all wine grapes (subject to specified quality standards) grown on 50 hectares of the vineyard up to 2015. There is, however, a provision in the Agreement for early termination where a party defaults in respect of their obligations under the Agreement and the breach of the Agreement's terms fails to be remedied within 28 days of notice from the other party, specifying the breach and an intention to terminate the Agreement if the breach is not remedied within the required time.

23. The mechanism for determining the price to be paid for the grapes sold under Grape Sale Agreement No 1 is set out in clause 11 of the Agreement.

Deed of Assignment No 1

24. Wine Co 1, Tasvinum and TVGL executed a deed of assignment on 25 May 1999 whereby:

- Tasvinum assigned to TVGL all of its rights, title and interest in, and to, Grape Sale Agreement No 1; and
- TVGL accepted the assignment.

Grape Sale Agreement No 2

25. The parties to Grape Sale Agreement No 2 are Wine Co 2 and TVM.

26. Under Grape Sale Agreement No 2, Wine Co 2 agrees to purchase from TVM all wine grapes (subject to specified quality standards) grown on the remaining 8 hectares of the vineyard up to 2008, at prices set out in clause 7 of the Agreement.

Deed of Assignment No 2

27. Wine Co 2, TVM and TVGL executed a deed of assignment on 25 May 1999 whereby:

- TVM assigned to TVGL all of its rights, title and interest in, and to, Grape Sale Agreement No 2; and
- TVGL accepted the assignment.

The Finance Option and the Loan Agreement

28. The Information Memorandum outlines a finance option offered by OFSA, a related corporation of both TVGL and Tasvinum. If taken up, the loan transaction underlying acceptance of the finance option will be evidenced by the execution of a Loan Agreement between OFSA and the Grower intending to borrow.

29. Under the finance option, Growers will have the opportunity to borrow up to 90% of their Application Monies (i.e., the amounts payable by applicants under the Information Memorandum for rootstock, rent and management fees during the initial period) at an interest rate of 9.5% per annum.

30. Interest payments are to be made over a period of 10 years (unless extended under the terms of the Loan Agreement) from the commencement date of the Loan Agreement in the amounts listed in the Schedule to the Agreement. They will be payable yearly in advance on 30 June in each year of the term of the loan.

31. Repayments of loan principal are to commence on the 4th anniversary of the commencement date of the Loan Agreement. The amount of the repayments will be the lesser of the amount set out in the Loan Agreement Repayment Schedule for each year of the loan term, or the Grower's share of the net sale proceeds (i.e., the gross amount received by TVGL from the sale of fruit from the leased area less the amounts deducted in accordance with clauses 22.4 of the lease and management agreements). If the Grower's accumulated shares of net sale proceeds over the term of the loan are insufficient to have repaid the loan, then OFSA will extend the term of the loan for such period (not exceeding 16 years) as will be required to fully repay the loan.

32. Among other things, the Loan Agreement also specifies:

- that it is a condition precedent to the making of the loan that the parties have entered into a lease and management agreement;
- that OFSA will provide the loan on the commencement date;

- that the manner in which interest on the loan is to be paid yearly in advance on 30 June of each year of the term of the loan is as follows:
 - ◆ that TVGL will seek to pay each interest payment due by the Grower from the balance of the net sale proceeds due to each Grower after deduction of the principal repayment required under this Agreement during the 12 month period immediately preceding the due date of each interest payment;
 - ◆ that if there are insufficient net sale proceeds to meet a Grower's interest obligation for the relevant period, the shortfall is to be paid directly from a Grower's funds;
- that OFSA may assign the benefit of this Agreement; and
- that the loan is on a full recourse basis and under no circumstances will OFSA waive the right and obligation of the Grower to repay the loan and interest as provided in the Loan Agreement.

Statements made in the Application, in documents lodged subsequent to the Application and in discussions with the Applicant's independent Tax Advisor

33. TVM, through its independent Tax Advisor, makes the following statements and commitments in support of its application for a Product Ruling:

- in respect of the portion of the vineyard covered by the lease and management agreement contained in LM Agreement No 1:
 - ◆ that TVM was the entity that had carried out the improvements such as surveying, row pegging, deep ripping, fertilising and planting which were in place at the time of commencement of the Project in relation to the abovementioned portion of the vineyard;
 - ◆ that, at the time it undertook the abovementioned improvements, TVM held a lease of the said land from Tasvinum;
 - ◆ that deduction entitlements under both the ITAA 1936 and ITAA 1997 in respect of the

- abovementioned improvements will be claimed by TVM;
- ◆ that the rental amounts charged in respect of the abovementioned portion of the vineyard reflect the increase in the value of the land brought by the completion of the abovementioned improvements on the land;
 - ◆ that the management fees charged in respect of the abovementioned portion of the vineyard do not incorporate an amount to reflect the increase in the value of the land brought by the completion of the abovementioned improvements on the land;
- that the rootstock payment of \$2,283.00 per interest that Growers were charged for when they subscribed for interests in the Project represented a contribution towards the cost of acquiring rootstock solely for use in establishing that portion of the vineyard covered by the lease and management agreement contained in LM Agreement No 2;
 - for a Grower who invests in the Project during the year ending 30 June 2000 on or after the date of effect of this Product Ruling, TVM intends to vary the Project's constituent documentation, so far as that Grower is concerned, to the following extent:
 - ◆ that where there are provisions in the Project's constituent documents in existence at 18 June 1999, which state that amounts that are owed by a Grower are due and payable by 30 June 1999, those provisions are to be replaced by provisions which state that the said amounts shall instead be due and payable by the said Grower immediately upon acceptance of him/her into the Project.

Ruling

34. Provided that the Project's Minimum Subscription level of \$2,352,250.00, mentioned in the Information Memorandum at page 14, is achieved during the year ending 30 June 2000 or earlier, where a Grower acquires an interest in the Project by 30 June 2000, the following deductions will be available for the years ended 30 June 2000 to 30 June 2002:

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		Deductions available each year		
		Year 1	Year 2	Year 3
Year ended		30/6/2000	30/6/2001	30/6/2002
Fee type	ITAA 1997 section			
Management fee	8-1	\$12,740	\$5,895	\$6,131
Lease fee	8-1	\$1,664	\$966	\$827
Irrigation	387-125	\$1,225	\$1,225	\$1,224
Preplanting and planting	387-165	(see Note a below)	(see Note b below)	(see Note c below)
Trellising	42-15	(see Note d below)	\$872	\$912
Interest on loan	8-1	\$4821	\$3491	\$4,022

Notes:

a. Deductibility under sections 387-125 and 387-165 is dependent on the Grower carrying on a 'primary production business' at the time the expenditure in question is incurred. There is an exception to this rule under subsection 387-165(3) if the effective life of the horticultural plant is more than 3 years. In this case, the later owner is entitled to remaining deductions. A Grower who applies and is accepted into the Project on, say, 30 June 2000, but for whom no services are provided in that year of income, will not be considered to be carrying on such a business. Services will be provided to Growers prior to 30 June 2000.

b. Deductibility under section 387-125 is calculated on the basis of one-third of the capital expenditure in the year in which the expenditure is incurred, and for each of the next 2 years of income.

c. Deductibility under section 387-165 is calculated on the basis of grapevines, as horticultural plants, entering their first commercial season in the 2003/2004 year (i.e., the fourth year of the Project). The calculation is also based on the assumption that the Grower will determine under section 387-175 that the grapevines have an 'effective life,' for the purposes of section 387-185, of greater than 13 but less than 30 years, resulting in a write-off rate of 13%.

In relation to the 10 hectares of established vineyard, the Growers will be entitled to the deduction for the cost of establishing the grapevines due to the operation of section 387-165. The deduction will be available as the Grower will be the owner of the grapevines at the time they are used for commercial horticulture. In addition, subsection 387-165(3) allows a later owner of a horticultural plant to deduct what they could have deducted under section 387-165 claim relevant deductions if the life of the horticultural plant is more than 3 years.

d. Deductibility under section 42-15 for depreciation, for the year ended 30 June 2000, 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 owned an interest in the trellising. TVM is to advise Growers of this for the year ending 30 June 2000. Deductions for the two succeeding years have been calculated, for illustrative purposes, on the basis of using the prime cost method at a rate of 13%, assuming that is the method that the Grower has chosen under section 42-25.

35. For a Grower who invests in the Project, any income received by them from the sale of grapes from their 'farm' will be assessable income to them under section 6-1 of the ITAA 1997.

Section 82KZM

36. Section 82KZM of the ITAA 1936 will not apply to deny deductions otherwise allowable to Growers under section 8-1 of the ITAA 1997 in respect of expenditure incurred in relation to the Project mentioned at paragraph 34, or interest on a loan(s) taken out with OFSA to finance the payment of application monies owing under LM Agreement No 1 and LM Agreement No 2.

Section 82KL

37. Section 82KL of the ITAA 1936 will not apply to deny deductions otherwise allowable to Growers under section 8-1 of the ITAA 1997 in respect of expenditure incurred in relation to the Project mentioned at paragraph 34, or interest on a loan(s) taken out with OFSA to finance the payment of application monies owing under LM Agreement No 1 and LM Agreement No 2.

Part IVA

38. 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

39. Consideration of whether the rental and management fees 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 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 the second limb applies. However, that does not preclude the application of the first limb and determining whether the outgoings in question have a sufficient connection with activities to produce assessable income.

40. An outgoing or a loss incurred in carrying on a business for the purpose of gaining or producing assessable income is deductible under the general deduction provision, section 8-1, provided it is not expenditure or a loss of capital or of a capital, domestic or private nature. A business includes a 'primary production business', which is defined under subsection 995-1(1) to include a business of propagating and cultivating plants. Where there is a business, or a future business, of growing grapes for sale at a profit, the gross sale proceeds from the sale of grapes from the Project will constitute gross assessable income under section 6-1. 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, and maintaining of grapevines and the harvesting of the grapes.

Is the Grower in business?

41. Generally, a Grower will be carrying on a business of viticulture where:

- they have an identifiable interest in specific growing vines coupled with a right to harvest and sell the grapes resulting from those vines;
- the viticulture activities are carried out on their behalf; and
- the weight of the general indicators of a business, as developed by the Courts, point to them carrying on such a business.

42. By weighing up all of the attributes of the Project, it is accepted that Growers in the Project will be in a business of primary production from the date that 'business operations' are first commenced on their behalf. 'Business operations', in this context, mean such things as surveying of the land, installation of the trellising and irrigation items, and other preplanting work, all conducted as part of a co-ordinated and concerted plan to grow and harvest grapes for sale at a profit.

43. For this Project investors have, under the two Lease and Management Agreements, a lease of the vineyard, together with a right of access for the purpose of their business, consistent with the intention to carry on a business of growing grape vines. They also have a beneficial interest in the general right to occupy the land as held by the Trustee and the improvements to the land for the duration of the venture. At the termination of the Management and Lease Agreements, Growers also have the right to remove the trellising and above ground irrigation lines or be compensated for the cost of the trellising by virtue of Tasmanian State Legislation.

44. Under the Lease and Management Agreement No 1, Growers appoint Tasvinum Group (TVGL) to carry on business on their behalf. In turn, TVGL will appoint Tasvinum Management Pty Ltd (TVM), as manager to provide ongoing management services necessary to develop a mature fruit bearing vine.

45. Under the Lease and Management Agreement No 2, Growers also appoint Tasvinum Group to carry on the business on their behalf. In turn, TVGL will appoint TVM, as Manager, to provide services such as preplanting and planting of grapevines, the installation of trellising and irrigation, and all cultural operations necessary to develop a mature fruit bearing vine.

46. Growers have the right to use the land in question for viticulture purposes and to have Tasvinum Group come onto the land to carry out its obligations under each Management Agreement. The Growers' degree of control over Tasvinum Group, as evidenced by the Agreements and supplemented by the Corporations Law, is sufficient. Under the general terms of the Project, Growers are entitled to receive regular progress reports on Tasvinum Group's activities. Growers are able to terminate arrangements with Tasvinum Group in certain instances, such as cases of default. The viticulture activities described in the Lease and Management Agreements are carried out on the Growers' behalf. In summary, Growers have the ability to control their investment.

47. 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 in this Ruling for all these indicators. Growers to whom this Ruling applies intend to

derive assessable income from the Project. This intention is related to projections in the draft Information Memorandum 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.

48. Growers will engage the professional services of a Manager who holds itself out as having the appropriate credentials. There is a means to identify which vines Growers have an interest in. The services are based on accepted viticultural practices and are of the type ordinarily found in viticulture ventures that would commonly be said to be businesses.

49. Growers have a continuing interest in the vines from the time they are acquired until the termination of the Project. The viticulture 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' viticulture activities will constitute the carrying on of a business.

Deductibility of expenses

50. The Lease and Management fees payable in years one, two and three, associated with the viticulture activities, will relate to the gaining of income from this business and hence have a sufficient connection to the operations by which this income is to be gained. They will, thus, be deductible under the first limb of section 8-1, to the extent that they are not capital or of a capital nature (see further below). Further, no 'non-income producing' purpose in incurring the fee is identifiable from the arrangement. The fees, on the basis of the information provided, cannot be said to be grossly excessive. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply, except as set out below.

Expenditure of a capital nature

51. Any part of the expenditure of a Grower entering into the viticulture business that is attributable to acquiring an asset or advantage of an enduring kind is generally capital or capital in nature and will not be an allowable deduction under section 8-1 of the ITAA 1997.

52. It is apparent from LM Agreement No 2 that certain payments for management fees are attributable to the acquisition of capital assets. They include preplanting costs, the cost of establishing the vines, and the erection and establishment of such items as trellising and irrigation to support and water the vines. However, expenditures of this nature can fall for consideration under specific deduction

provisions relevant to the carrying on of a business of primary production, and under the general depreciation provisions of the ITAA 1997.

53. TVM has identified the relevant expenditures that are of a capital nature. A Grower entering into the Project incurs and pays an amount to TVM for these capital items amounting to \$17,595 in year 1 and \$307 in year 2.

Expenditure on conserving or conveying water – Subdivision 387-B

54. Capital expenditure incurred by a person carrying on a primary production business, on the construction, acquisition and installation of plant, equipment and structural improvements to be used primarily and principally for the purpose of conserving or conveying water for use in such a business, qualifies for a write-off over a three year period (i.e., $33^{1/3}$ with no pro rating required), under Subdivision 387-B of the ITAA 1997, specifically section 387-125. A taxpayer incurring this expenditure need not be the owner of the land to claim the deduction, so long as they are in a business of primary production. In this case there will generally be no delay between the signing of the Agreements and the commencement of 'business operations'. Accordingly, a Grower's business of primary production will generally have commenced at the time the expenditure is incurred. The requirements of Subdivision 387-B have, thus, been met in this respect.

55. TVM has identified that the expenditure applicable to the conserving or conveying of water for the vineyards, that meets the requirements of section 387-130, amounts to \$3,674 for the year ended 30 June 2000. A deduction will be allowable under section 387-125 for the years ending 30 June 2000 and 2001 of \$1,225 per year, and for the year ending 30 June 2002 of \$1,224.

Horticultural provisions – Subdivision 387-C

56. Subdivision 387-C allows capital expenditure on establishing horticultural plants owned and used, or held ready for use, in Australia in a business of horticulture to be written off for tax purposes. Costs of establishing horticultural plants may include the cost of acquiring the plants; the cost of establishing the plants; and the costs of ploughing, contouring, top dressing, fertilising and stone removal. Expressly excluded is expenditure incurred on draining swamps or clearing land. A lessee or licensee of land carrying on a business of horticulture is taken to own the plants growing on that land rather than the actual owner of the land.

57. Under this Subdivision, if the effective life of the plant is less than three years the expenditure can be written off in full; if the effective life of the plant is more than three years an annual deduction is allowable on a prime cost basis during the plant's maximum write-off period. The period starts from the income year the grapevines first become commercially productive and the Project Manager will advise the Grower of this date.

58. The effective life of a plant is to be determined objectively and should take into account all relevant circumstances. The write-off rate for horticultural plant is detailed in section 387-185. For a plant with an effective life of 13 to 30 years the rate is 13% per annum.

59. TVM has identified that the relevant expenditure attributable to the establishment of the vines in relation to the land described in LM Agreement No 2 is \$7,215 in year 1. This amount will be subject to the grapevine establishment provisions and allowable as a deduction under Subdivision 387-C.

60. The deduction will be available from the time the grapevines are established and used in the primary production business, which will be in the first year of commercial production, i.e., year 4.

61. A special issue arises in respect of the grapevines established on the land in respect of the portion of the vineyard covered by the lease and management agreement contained in LM Agreement No 1. Tasvinum Management established the grapevines and first carried on business in relation to the grapevines. However, from the time the Grower enters into the Established Vineyard Lease and Management Agreement, the Grower will be considered to be the owner of the grapevines for the purposes of section 387-165. The deduction will be available to the Growers under section 387-165 as the Grower will be the owner of the grapevines when the grapevines are used for commercial horticulture. Additionally, section 387-165 states that it does not matter who incurred the expenditure. Therefore, the portion of the lease fee that relates to the grapevine establishment costs will be deductible under section 387-165, if it is not considered to be deductible under section 8-1.

Trellising – section 42-15

62. Growers accepted into the Project incur a number of expenses under the Management Agreement for items of plant, which are to be used on their behalf in the operation of the vineyard business. Such expenditure includes that on Trellising upon which the vines are attached. This is attached to the land as a fixture. This expenditure is also of a capital nature.

63. Generally speaking, if a taxpayer incurs expenditure of a capital nature on plant or equipment, used during the year of income

for the purposes of producing assessable income, and it is expenditure to which section 42-15 of the ITAA 1997 applies, a deduction will be allowed for depreciation on the item under that section. However, where an item is affixed to land so that it becomes a fixture, at common law it becomes part of the land and is legally, absolutely owned by the owner of the land.

64. However, we accept in certain circumstances a lessee is entitled to claim depreciation where they are considered to be the owner of those improvements. In Taxation Ruling IT 175 we set out our views on this issue. Where a lessee is considered to own the improvements under a state law, as detailed in the Ruling, or where they have a right to remove the fixture or are entitled to receive compensation for the value of the fixture, we accept the lessee is entitled to claim depreciation for the fixture.

65. A Grower accepted into the Project enters into an Agreement for a Lease over certain land upon which they are entitled to grow vines to conduct a business of viticulture. Under Tasmanian Legislation they have a right to remove the trellising at the end of the Project or receive compensation for the cost of the trellising.

66. A deduction for depreciation is allowable on plant from the date it is installed and ready for use. The Manager, Tasvinum Management Pty Ltd, will advise Growers when the trellising is installed and begun to be used for the purpose of producing assessable income.

67. As such, the cost of \$7,013 over three years, that relates to the acquisition and installation of trellises to the land in respect of the portion of the vineyard covered by the lease and management agreement contained in LM Agreement No 2, will be eligible for depreciation deduction by the Growers under section 42-125, at a rate of 13% prime cost or 20% diminishing value.

Section 82KZM

68. Under the Lease and Management Agreements, the Lease and management fees are payable in advance. In each instance the fees are charged for providing services to a Grower only for the period of 12 months from the time they are incurred. The fees are expressly stated to be for a number of specified services. In effect, the Manager is promising to provide significantly more services, in terms of value, in the first year of the Project, compared to years two and three.

69. No explicit conclusion can be drawn from the arrangement's description, that the fees in the first three years have been inflated to result in reduced fees being payable for subsequent years. There is no evidence that might suggest the services covered by the fee could not be provided within 13 months of incurring the expenditure in

question. Thus, for the purposes of this Ruling, no part of the first year management fee of \$22,879 (in respect of the land described in both the Lease and Management Agreements) or for the fees incurred in years two and three, is for Tasvinum Management Pty Ltd doing 'things' that are not to be wholly done within 13 months of each 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 expenditures identified above in each of the financial years ended 30 June 1999 to 30 June 2001.

Section 82KL

70. 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 in respect of this loan, to trigger the application of section 82KL. It will not apply to deny the deduction otherwise allowable under section 8-1.

Part IVA

71. 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 Old Stornoway Vineyard Project will be a 'scheme'. It will commence generally on the date the Information Memorandum is issued. The Growers will obtain a 'tax benefit' from entering into the scheme, in the form of the deduction for the lease fees and management fees allowable under section 8-1, and deductions allowable under Subdivisions 387-B and 387-C, and section 42-15, that would not have been obtained but for the scheme. However, it is not possible to conclude the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

72. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the yearly sale of grapes or grape juice. Further, there are no features of the Project, for example, such as the total Lease and Management fees of \$47,045 being 'excessive', and 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.

Assessable income

73. Gross sale proceeds derived from the sale of grapes harvested from the Project will be assessable income of the Growers, under section 6-1, in the year in which a recoverable debt accrues to them. This will depend on the terms of the specific sale contracts entered into.

Interest deductibility

74. Some Growers intend to finance their investment through a loan facility. Whether the resulting interest fees are deductible under section 8-1 depends on the same reasoning as that applied to whether the Lease and Management fees are deductible. The interest fees incurred will be in respect of a loan to finance the establishment of the vineyard and its development in the first years - which will continue to be directly connected with the gaining of 'business income' from the Project. These fees will, thus, also have a sufficient connection with the gaining of assessable income. No capital, private or domestic component is identifiable in respect of them.

Detailed contents list

75. Below is a detailed contents list for this Ruling:

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Commissioner of Taxation

25 August 1999

Previous draft:

Not previously released to the public as a draft Product Ruling

Related Rulings/Determinations:

IT 75; IT 2001; PR 98/1; TD 93/34;
TR 92/1; TR 92/20; TR 94/25;
TR 97/11; TR 97/16

Subject references:

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

Legislative references:

- ITAA1936 82KL
- ITAA1936 82KZM
- ITAA1936 Pt IVA
- ITAA1936 177A
- ITAA1936 177C
- ITAA1936 177D
- ITAA1997 6-1
- ITAA1997 8-1
- ITAA1997 42-15
- ITAA1997 42-25
- ITAA1997 42-125
- ITAA1997 42-160
- ITAA1997 42-165
- ITAA1997 43-25
- ITAA1997 387-B
- ITAA1997 387-125
- ITAA1997 387-130
- ITAA1997 387-165
- ITAA1997 387-C
- ITAA1997 387-165(3)
- ITAA1997 387-175
- ITAA1997 387 185
- ITAA1997 995-1(1)

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