



# ***PR 2000/77 - Income tax: Wrights Bay Vineyard Stage 2***

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 This document has changed over time. This is a consolidated version of the ruling which was published on *21 June 2000*



## Product Ruling

### Income tax: Wrights Bay Vineyard Stage 2

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Potential investors may wish to refer to the ATO's Internet site at <http://www.ato.gov.au> or contact the ATO directly to confirm the currency of this Product Ruling or any other Product Ruling that the ATO has issued.

#### **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 1999/95 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 these products as investments. Further, we give no assurance that the products are 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 products. 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 arrangements are 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 arrangements will be carried out as described in this Product Ruling.

Potential investors should be aware that the ATO will be undertaking review activities in future years to confirm the arrangements have been implemented as described below and to ensure that participants in the arrangements include in their income tax returns income derived in those future years.

#### **Terms of use of this Product Ruling**

This Product Ruling has been given on the basis that the person(s) who applied for the Ruling, and their associates, will abide by strict terms of use. Any failure to comply with the terms of use may lead to the withdrawal of this Ruling.

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## What this Product Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates. In this Ruling this arrangement is sometimes referred to as the Wrights Bay Vineyard Stage 2, or just simply as the 'the Project'.

### Tax law(s)

2. The tax law(s) dealt with in this Ruling are:

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 8-1 (ITAA 1997);
- section 27-5 (ITAA 1997);
- section 27-30 (ITAA 1997);
- section 42-15 (ITAA 1997);
- section 387-125 (ITAA 1997);
- section 387-165 (ITAA 1997);
- section 82KJ, section 82KK and section 82KL of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 82KZM and 82KZMB (ITAA 1936); and
- Part IVA (ITAA 1936).

3. On 11 November 1999, the Government announced further changes to the tax system as part of the New Business Tax System. A number of those changes, especially those to do with 'tax shelters', could affect the tax laws dealt with in this Ruling. Some of the changes apply from the date of the announcement and others are proposed to apply from nominated dates in the future.

4. Although this Ruling mentions certain of those announced changes, the information given on the treatment of expenditure which may be affected by them is not binding on the Commissioner. Legally binding advice in respect of those changes cannot be given until the relevant law(s) are enacted.

5. However, if the changes become law the operation of that law will take precedence over the application of this Ruling and, to that extent, the Ruling will be superseded. If requested, when the relevant law(s) are enacted, the Commissioner will formalise the non-binding information shown in this Ruling by issuing a new Product Ruling that describes the operation of those law(s).

**Class of persons**

6. 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’.

7. 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**

8. The Commissioner rules on the precise arrangement identified in this ruling. If the arrangements described in the Ruling are materially different from the arrangements that are actually carried out:

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

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**Date of effect**

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10. This Ruling applies prospectively from 21 June 2000, the date the 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).

11. 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

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year to which it relates has not yet commenced, the Product Ruling applies to the taxpayer to the extent of the inconsistency only. (see Taxation Determination TD 93/34).

## Withdrawal

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12. This Product Ruling is withdrawn and ceases to have effect after 30 June 2003. 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.

## Arrangement

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

- Application for Product Ruling for Wrights Bay Vineyard – Stage 2 (“WBVPL”) dated 20 April 2000;
- Wrights Bay Vineyard Stage – 2 Information Memorandum, dated 15 January 2000;
- **Sale of Land Contract, which includes additional clauses covering:**
  - **the development of the vineyard;**
  - **management and operations of the vineyard;**
  - **and**
  - **grape purchase;**
- Management and Operations Agreement with LCV Management P/L (“LCV”), dated 4 April 2000;
- Supply and Installation Agreement with LCV Management P/L for the supply and installation of trellising, sub-irrigation and rootstock, dated 4 April 2000;
- Supply Contract for the provision of the mains irrigation system with Burnigula Developments Pty Ltd (“BDPL”);
- Grape Sale and Purchase Agreement with Kingston Estate Wines (Australia) P/L (“Kingston Estate”).

**Note: certain information received from Wrights Bay Vineyard Pty Ltd (Vendor and Manager) has been provided on a commercial-in-confidence basis and will not be disclosed or released under Freedom of Information legislation.**

14. The document highlighted are those the Growers enter into. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate of the Grower, will be party to. The effect of these agreements is summarised as follows.

### **Overview**

15. This arrangement is called the Wrights Bay Vineyard – Stage 2.

Location	Mount Benson in southeastern South Australia, 20 kilometres north of Robe, 320 kilometres south of Adelaide.
Type of business each participant is carrying on	Viticulture
Number of hectares under cultivation	The Project involves 26 hectares under cultivation
Product name description	Wright's Bay Vineyard – Stage 2
Number of lots for sale	8
Minimum Subscription	Not applicable
Size of each purchased area	3.28 hectares
Number of vines per hectare	1830
Expected production	The first harvest will be in 2003. Output per hectare in 2003 will be 3.75 tonnes and rising to 11.6 tonnes by the 2005 harvest.
The term of the investment in years	Growers have freehold title over their land and a 12 year management agreement
Initial cost	\$51,648 before 30 June 2000 (net of GST) \$54,258 before 30 June 2001 (net of GST)

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Initial cost per hectare	\$32,288 (net of GST)
Ongoing costs	Management Fees of \$22,500 (2001) \$28,900 (2002) and \$19,640 pa thereafter (net of GST)
Grape Sales Contracts	Sales contract for 100% grapes produced confirmed until 2012

**Description**

16. A Grower in the Project will buy freehold title to 3.28 hectares of land, which is subject to Community Title. The land has already been prepared for the establishment of a vineyard with the land having been ripped, rocks crushed and removed, the land re-levelled and marked out for planting. Under the terms of the Community Corporation by-laws the land may only be used for viticulture.

17. The Community Title associated with the vineyard is governed by the *South Australian Community Titles Act 1996*. Under this Act the owner of a Community lot owns all of the improvements on that lot and the common property is vested in the owners of the Community lot as tenants in common.

18. Common assets and infrastructure are provided by the Vendor and include: windbreaks, roads, bores, parking lot, gates, multi-purpose shed comprising lock up storage areas, workshop and vehicle bays, amenities room/office and shower and toilet facilities, lock up storage/loading facility, and power connected to the shed.

19. Growers will be required to contribute to the indirect expenses of the Community Corporation, which will include the purchase of fuel for the pumps, rates and insurance in respect of common land and assets. Projected costs for this are \$1,804 per lot per annum, GST inclusive.

20. Growers are required to reimburse the Vendor for the mains irrigation system. This system is designed to supply water from the bore to each lot.

21. Growers contract with the Vendor for supply and installation of trellising, vines and a sub irrigation system for each lot. The Vendor has engaged local vignerons to carry out these functions. Each lot will contain approximately 6,000 vines. These will be grafted rootstock and will be one or more for the following grape types: merlot, cabernet sauvignon, shiraz, chardonnay and sauvignon blanc. The grape type planted on each block will be at the discretion of the Vendor.

22. Growers also contract with the Vendor to provide ongoing management of the vineyard for a period ending 30 June 2012. The

Vendor has contracted with local vignerons to carry out these functions until 30 June 2012. Thereafter the Growers can make other arrangements.

23. The first harvest will be in 2003. Output from each lot is expected to be 12.30 tonnes in the first year, rising to 38.05 tonnes by the 2005 harvest.

24. The Vendor has entered into a Grape Sale and Purchase Agreement with Kingston Estate. This agreement provides for the purchase by Kingston Estate of all the fruit produced by the vineyard up until 30 June 2012. The price to be paid for the fruit is equal to the weighted average "grape price per tonne at farmgate" for each variety as published by the relevant authority, for the "Limestone Coast – Other" Region. The Vendor will contract with each Grower to purchase all the fruit from each lot on essentially the same terms. Under this arrangement the fruit from each lot will be pooled and on sold to Kingston Estate. The price paid to the Growers will be the price received from Kingston Estate less associated costs such as insurance, cartage and an administration fee of 1% of the net proceeds.

25. The assumptions underlying the projected income from the vineyard are found on pages 18 and 19 of the Information Memorandum.

#### **Costs/Fees**

26. The Growers will make the following payments for the first three years commencing 30 June 2000.

27. Cash payments for each 3.28 hectare allotment.

(Note: it is assumed a Grower will be registered for GST and be able to claim input credits in respect to any GST paid).



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<b>Description</b>	<b>Due date for Payment</b>	<b>Amount (GST inclusive)</b>	<b>Amount (net of GST)</b>
<b>Payments to acquire and develop a 3.28 hectare lot</b>			
Freehold Land*	At Settlement	27,060	24,600
Mains irrigation system	30 June 2000	13,860	12,600
Supply and installation of Trellising	31 July 2000	32,111	29,192
Supply and Planting of Rootstock	30 September 2000	27,573	25,066
Supply and installation of Sub-Irrigation	30 June 2000	15,893	14,448
<b>Total</b>		<b>116,497</b>	<b>105,906</b>
<b>First Growing Season</b>			
Management & Operations	30 June 2001	24,750	22,500
Indirect Expenses	Annual	1,804	1,640
<b>Second Growing Season</b>			
Management & Operations	1 July 2001	7,948	7,225
Management & Operations	1.10.2001	7,948	7,225
Management & Operations	1.1.2002	7,948	7,225
Management & Operations	1.4. 2002	7,948	7,225
Indirect Expenses	Annual	1,804	1,640
<b>Third Growing Season</b>			
Management & Operations	1.7.2002	5,401	4,910
Management & Operations	1.10.2002	5,401	4,910
Management & Operations	31.5.2003	5,401	4,910
Management & Operations	30.6.2003	5,401	4,910
Indirect Expenses	Annual	1,804	1,604

\* Includes infrastructure and land prepared for planting.

28. During the third growing season grapes will be harvested and sold. Sale proceeds of \$13,350 are expected from this first harvest based on current prices and industry standards. (Refer to page 18 to 20 of the Information Memorandum for the assumptions underlying this estimate).

29. Payments are required to be made in subsequent years for the ongoing management and operation of the vineyard, and the Community Corporation expenses. Fees are based on the 2003 fees increased annually by the greater of CPI increases or increases in input costs over the preceding year, if any.

### **Finance**

30. Growers are required to obtain their own finance for the Project.

31. This ruling will not apply if a Grower enters into a finance agreement that includes any of the following features:

- there are split loan features of the type described in Taxation Ruling TR 98/22;
- entities associated with the Project become involved in the provision of finance;
- there are indemnity arrangements, or equivalent collateral arrangements, limiting the borrowers risk;
- there are non-arms length terms and conditions;
- “additional benefits” for the purpose of section 82KL are granted to the borrower, or the funding arrangement transforms the Project into a “scheme” to which Part IVA may be applied;
- repayments of principal and payments of interest are limited to income derived from the Project;
- the funds borrowed, in whole or in part, are not available for the conduct of the Project, but are transferred (by means, directly or indirectly) back to the lender or any associate; or
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers.

32. Growers are required to make all payments specified above. Under the terms of the Grape Sale Agreement the Vendor is entitled to withhold payment of the proceeds of grape sales from the Grower where the Grower is in arrears of payments due.

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**Ruling****Goods and Services Tax**

33. A Grower who invests in the Project will, pursuant to section 27-5 or 27-30 of the ITAA 1997, be required to reduce the amount of any deduction claimed by the amount of any GST input tax credit to which the Grower is entitled or, in the case of section 27-5, a decreasing adjustment that the Grower has.

**Allowable Deductions**

34. A Grower who invests in the Project before 30 June 2000 and who makes the payments set out in the table below, will be able to claim the following deductions for the years ended 30 June 2000, 2001, 2002 and 2003.

	<b>Year ended 30.6.00</b>	<b>Year ended 30.6.01</b>	<b>Year ended 30.6.02</b>	<b>Year ended 30.6.03</b>
<b>Trellising</b>	0	5,352	4,768	3,814
<b>Establishing Grapevines</b>		4,178	6,267	6,267
<b>Irrigation</b>	9,016	9,016	9,016	
<b>Management and Operating Expenses</b>		22,500	28,900	19,640
<b>Community Expenses</b>		1,640	1,640	1,640
<b>Grape Harvesting Costs</b>				754
<b>Total</b>	<b>9,016</b>	<b>42,686</b>	<b>50,591</b>	<b>32,115</b>

**Carrying on the business of primary production**

35. In order for a Grower to be able to claim deductions for outgoings associated with the Project, they are required to be carrying on the business of primary production. A Grower who participates in this Project will meet the tests laid out in TR 97/11 for determining this and accordingly will be regarded as carrying on a business of primary production.

**Section 8-1 - recurrent expenses**

36. The expenses of the Project considered deductible under section 8-1 are the management and operating expenses, and the indirect expenses of the Community Corporation.

37. Section 8-1 denies deductions for expenditure of a capital nature, accordingly expenditure associated with the initial development of the vineyard will not be deductible pursuant to section 8-1. Specific deductions are available for some of this expenditure as detailed below.

**Section 387-305 - deduction for establishment of grapevine**

38. Section 387-305 provides for a deduction for expenditure incurred in establishing a grapevine. The deduction is available to the owner of the vines who uses the grapevine in a primary production business for the purposes of producing assessable income. The deduction is allowed over a four-year period commencing on the day the vine is established. The deduction is pro-rated in the first year.

**Subdivision 387-B - expenditure on irrigation**

39. Capital expenditure incurred by primary producers on the construction, acquisition and installation of plant and equipment and structural improvements to be used primarily and principally for the purpose of conserving or conveying water qualifies for 100% deduction over a three year period with no pro-rata required under Subdivision 387-B. Irrigation expenses of the kind proposed would be covered by this Subdivision.

40. The Growers in the Project will incur expenses in respect of the mains irrigation system that provides water to the vineyard development, and the sub irrigation system that provides water to their individual lots. These costs are deductible over a three year period commencing from the date the expenses are incurred. A deduction is available at a rate of 33.3% per annum for the cost for the irrigation system.

**Section 42-15 - expenditure on plant and equipment**

41. Capital expenditure on plant and equipment used in carrying on a viticulture business that is not subject to special write-off allowances discussed above, will be eligible for depreciation deductions pursuant to section 42-15.

42. The amount of the depreciation deduction is determined by the nature of the item of plant as well as the classification of the Grower.

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43. Trellising is the principal item of plant that qualifies for depreciation. Growers pay for the acquisition and installation of trellising which will be installed in July 2000.

44. A Grower who is a small business taxpayer will be able to depreciate trellising using accelerated depreciation. The amount shown as deductible in paragraph 34, has been calculated using the diminishing value method at a rate of 20% on the basis the trellising is installed ready to use by 31 July 2000.

45. A Grower who is not a small business taxpayer will determine depreciation in accordance with the effective life of the item of the plant.

## Section 6-5 - grape sale income

46. Gross sales derived from the sales of grape produce harvested from the Project will be assessable income of the Growers, under section 6-5.

## Sections 82KJ, 82KK, 82KL, 82KZM, 82KZMB; Part IVA

47. For a Grower who invests in the Project the following provisions have application as follows:

- Section 82KJ and 82KL do not apply to deny deductions otherwise allowable;
- Section 82KK does not apply to defer the deductions otherwise allowable;
- Section 82KZM and 82KZMB do not apply to defer the deductions otherwise allowable;
- The relevant provisions of Part IVA will not be applied to cancel a tax benefit obtained under a tax law dealt with in the ruling.

## Proposed new laws

### Proposed changes to prepayment rules

48. The New Business Tax System (Integrity Measures) Bill 2000 that was introduced to Parliament on 13 April 2000 proposes changes to the prepayment rules. These changes propose that deductions for certain prepayments relating to tax shelter arrangements be deferred and spread over the period to which the prepayment relates. These rules should not affect the deductibility of management and operating fees paid by the Growers, as the fees are not prepaid.

**Note to Promoters and Advisers**

49. Product rulings were introduced for the purpose of providing certainty about tax consequences for investors in projects such as this. In keeping with that intention, the Australian Taxation Office suggests that promoters and advisers ensure that potential investors are fully informed of the announcements requiring prepayments in respect of 'tax shelter' arrangements to be deductible over the period services are provided. Such action should minimise suggestions that potential investors have been negligently or otherwise misled.

**Explanations****Sections 27-5 and 27-30 ITAA 1997 – Goods and Services Tax**

50. Section 27-30 of the ITAA 1997 operates to deny a deduction that would be otherwise available under section 8-1 for the year ended 30 June 2000 to the extent that the loss or outgoing (incurred after 30 November 1999 on or before 1 July 2000) includes an amount relating to an input tax credit to which a Grower will be entitled on or after 1 July 2000.

51. Section 27-5 of the ITAA 1997 operates to deny a deduction, that would be otherwise available under section 8-1, to the extent that the loss or outgoing incurred (on or after 1 July 2000) includes an amount relating to an input tax credit to which an Grower is entitled or a decreasing adjustment that a Grower has.

**Subdivision 960-Q - small business taxpayers**

52. In this Product Ruling the term 'small business taxpayer' is relevant for the purpose of depreciation of trellising.

53. Whether or not an Grower is a 'small business taxpayer' depends upon the individual circumstances of each Grower. It is the responsibility of each Grower to determine whether or not they are within the definition of a 'small business taxpayer'.

54. A 'small business taxpayer' is defined in section 960-335 of the ITAA 1997 as a taxpayer who is carrying on a business and either their 'average turnover' for the year is less than \$1,000,000 or their turnover recalculated under section 960-350 is less than \$1,000,000.

55. 'Average Turnover' is determined under section 960-340 by reference to the average of the taxpayer's 'group turnover'. The group turnover is the sum of the 'value of business supplies' made by the taxpayer and entities connected with the taxpayer during the year (section 960-345).

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## **Carrying on the business of primary production**

56. In order for an Grower to be able to claim certain deduction for outgoings associated with the Project, they are required to be carrying on the business of primary production. Growers in the Project will meet the tests used by the Courts and set out in TR 97/11 for determining this, on the basis that:

- The Project has a significant commercial purpose, and each Grower's interest in the overall development is significantly large to be a viable operation;
- Growers actually intend to undertake activities;
- The Project is intended to be profitable;
- The activities of the Project will be ongoing over a number of years;
- The Project has been set up and will be run in a professional and business-like manner;
- As a Grower acquires freehold title to the land and ownership of vineyard assets established on it, the size, scale and permanency of their interest is in accordance with a viable business venture;
- There is no scope for individual Growers to use the project for their own personal enjoyment and benefit. Residential development of the land is not permitted, and the size of the investment is such that it is beyond the scope of a hobby activity;
- Local experts in the viticulture industry are managing the Project. The practices adopted in the Project will be in line with normal commercial practices for vineyards.

57. Accordingly, a Grower will be treated as carrying on a primary production business, that of viticulture.

## **Section 8-1 - ITAA 1997 Recurrent expenses**

58. Section 8-1 provides for a deduction for costs incurred in gaining or producing assessable income, or necessarily incurred in carrying on a business.

59. The recurrent expenses must have a sufficient connection with the operations of activities that gain or produce assessable income for the taxpayer. Where the outgoing is incurred and the business has not commenced the deduction is not available.

60. There can be no doubt whether the relevant business has commenced and whether paragraph 8-1(1)(b) is applicable where the taxpayer contractually commits themselves to a venture that may not

turn out to be a business. However, paragraph 8-1(1)(a) would be applicable in determining whether the outgoing in question would have a sufficient connection with activities to produce the taxpayer's assessable income.

61. The financial projections contained within the Information Memorandum show that in the longer term income from grape sales is expected to exceed the outgoings. Even if for some unforeseen reason the income did not exceed the outgoings, the expectation of the Grower prior to investing in the Project is that they would. Therefore the profit making intention of the Grower supports the view that the operating costs are incurred in gaining or producing assessable income and will be deductible in the year incurred notwithstanding that grape sales proceeds will not be received until future years of income. This is supported by the decisions in *Fletcher & Anor v. FC of Taxation* 91 ATC 4950 and *FCT v Brand* 95 ATC 4633.

62. The expenses of the Project considered deductible pursuant to Section 8-1 are the management and operating expenses and the indirect expenses of the Community Corporation.

63. Interest expenses would normally be deductible pursuant to section 8-1. The Project does not include a funding/finance arrangement for each Grower.

64. Section 8-1 denies deductions for expenditure of a capital nature. Thus, any expenditure 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. In this Project, the costs of irrigation, trellising and irrigation are considered to be capital in nature. However, expenditure of this nature can fall for consideration under specific capital write-off provisions of the ITAA 1997.

### **Section 82KZM**

65. Sections 82KZA and 82 KZMA operate to defer the deductibility of expenses so that the deduction is allowed in the year in which the service is provided is actually performed, rather than in the year in which payment for services are made.

66. The management and operation services provided to Growers in the Project are due for payment in the same year in which the services are performed. Accordingly, section 82KZB and 82 KZMB will not operate in respect of the management and operating fees.

67. Changes to the prepayment rules introduced into Parliament on 13 April 2000 in the New Business Tax System (Integrity Measures) Bill 2000 propose that deductions for certain prepayments relating to tax shelter arrangements be deferred and spread over the period to



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which the prepayment relates. These rules will not effect the deductibility of management fees paid by Growers, as they are not prepaid.

## **Subdivision 387-D ITAA 1997 – expenditure on establishing grapevines**

68. Section 387-305 provides for a deduction for expenditure incurred in establishing a grapevine. The deduction is available to the owner of the vines and is allowable over a four year period commencing on the day the vine is established. The deduction is pro-rated in the first year.

69. The costs of establishing a grapevine include the cost of acquiring the plants, the cost of establishing the plants and costs of ploughing, contouring, top-dressing and fertilising the land.

70. Growers in the development will pay \$25,066 for the supply and planting of grapevines and will own the vines and planted on their lot. The grapes are to be planted in October 2000. Accordingly, as Growers are in the business of primary production, a deduction of \$4,178 in the year ended 30 June 2001 based on a pro-rata calculation from that date. A deduction of \$6,267 is available in the next three years, with the remaining \$2,087 deductible in 2005.

## **Subdivision 387-B ITAA 1997 – expenditure on irrigation**

71. Subdivision 387-B allows a taxpayer, who is carrying on a business of primary production on land in Australia, to claim a deduction for capital expenditure on conserving or conveying water. The 100% deduction is allowed over a three-year period and applies to plant or structural improvement primarily or principally used for the purpose of conserving or conveying water for use in a primary production. No pro-rata is required.

72. The Growers in this Project are in a primary production business and pay \$12,600 for the mains irrigation system that provides water to the vineyard development. They also pay \$14,448 for the sub-irrigation system that provides water to their individual lots.

73. Accordingly, a deduction of \$9,016 is available to the Growers in respect of the years ending 30 June 2000, 2001, and 2002.

## **Section 42-15 ITAA 1997 – expenditure on trellising**

74. Capital expenditure on plant and equipment used in carrying on a viticulture business that is not subject to special write-off allowances discussed above, may be eligible for depreciation deductions pursuant to section 42-15.

75. The amount of the depreciation deduction is determined by the nature of the item of plant as well as the classification of the Grower.

76. Trellising is the principal item of plant that qualifies for depreciation as the expenditure is of a capital nature. Growers pay \$29,192 for the acquisition and installation of trellising which will be installed and ready for use by 31 July 2000.

77. Determining the amount of depreciation requires determining whether an Investor is a 'small business taxpayer' pursuant to section 960-Q. This can only be determined by each individual Grower.

### **Small Business Taxpayers**

78. A Grower who is a 'small business taxpayer' who meets the requirements of section 42-345 will be able to depreciate trellising using the rates in section 42-125 and the formulae in subsection 42-160(1) or subsection 42-165(1). The depreciation deduction is calculated using the cost of the trellising and a rate of 13% prime cost or 20% diminishing value. These accelerated rates of depreciation are shown in section 42-125 and apply to plant with an effective life of between 13 and 30 years. Trellising has an effective life of 20 years.

79. The Information Memorandum has adopted the diminishing value method at a rate of 20%. A deduction of \$5,352 will be available for the year ending 30 June 2001, \$4,768 for the year ending 30 June 2002 and \$3,814 for the year ending 30 June 2003. See pages 28-29 of the Information Memorandum.

### **Non Small Business Taxpayers**

80. A Grower who is not a 'small business taxpayer' will determine depreciation in accordance with subsection 42-160(3) 'diminishing value' or subsection 42-165(2A) 'prime cost' based on the effective life of the item of plant. Growers will be eligible for a depreciation deduction at a rate of 5% prime cost or 7.5% diminishing value.

81. If the Grower elects to use the diminishing value method the rate for calculating the deduction will be 7.5%. The deduction available in Years 2 and 3 will be \$2,189 and \$2,025 respectively. This is assuming that the trellising is owned for 365 days. However, the deduction will depend upon the number of 'days owned', being the number of days in the income year in which the Grower owned an interest in the trellising.

82. The deductions for Years 2 and 3 using the prime cost method on the assumption that the effective life of the trellising is 20 years is

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\$1,460. This is assuming that the trellising is owned for 365 days. The deduction will depend upon the number of 'days owned'.

## Section 6-5 ITAA 1997 - grape sale income

83. Proceeds from the sale of grapes will be assessable income pursuant to section 6-5.

84. Once harvested, a Grower's grapes will be trading stock of the Grower. Grapes will be harvested in April and will be delivered immediately to the end purchaser, Kingston Estate. The trading stock provisions of the ITAA should therefore not have any effect on the Grower as they will not have trading stock on hand at any year-end. However, in the event that grapes are on hand at year-end the Grower will need to account for that trading stock in accordance with the trading stock provisions in Part 2-25.

## Section 82KL

85. Other anti avoidance rules are contained in sections 82KJ, 82KK and 82KL. These rules have no application to the Project on the basis that:

86. Section 82KJ deals with prepayments associated with tax avoidance schemes. The Project does not involve any prepayments.

87. Section 82KK deals with tax deferral arrangements between associated parties. The arrangements are not between associated parties.

88. Section 82KL deals with recouped expenditure. The Project does not involve a Grower incurring expenditure and subsequently receiving a relevant benefit (as determined under the section) and so incurring no real loss or outgoing.

## Part IVA

89. The general anti avoidance provisions of ITAA 1936 contained in Part IVA will deny deductions otherwise allowable where a 'scheme' is entered into or carried out with the sole or dominant purpose of obtaining a tax benefit.

90. Section 177A provides a broad definition of a 'scheme'. Wrights Bay Vineyard - Stage 2 will be a scheme for the purposes of this Part. Tax benefits are obtained by entering into the development in the form of deductions for certain expenditure. However, it is not possible to conclude the scheme will be entered into or carried out for the sole or dominant purpose of obtaining this tax benefit.

91. Growers to whom this Ruling applies are likely to stay in the scheme for its full term and derive assessable income from harvesting and selling grapes. There are no factors that would suggest that Growers have the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There is no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing with each other at arms length. Having regard to the factors to be considered under paragraph 177D(b) it cannot be concluded, on the information available, that participants will enter into the scheme for the sole or dominant purpose of obtaining a tax benefit.

## **Detailed contents list**

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**Commissioner of Taxation**

21 June 2000

*Previous draft:*

Not previously issued in draft form

*Related Rulings/Determinations:*TR 92/20; TR 97/11; TR 98/22;  
TD 93/34*Subject references:*

- carrying on a business
- commencement of business
- primary production
- primary production expenses
- management fee expenses
- producing assessable income
- product rulings

- public rulings
- schemes and shams
- taxation administration
- tax avoidance
- tax benefits under tax
- avoidance schemes
- tax shelters

*Legislative references:*

- ITAA 1997 6-5
- ITAA 1997 8-1
- ITAA 1997 27-5
- ITAA 1997 27-30
- ITAA 1997 42-15
- ITAA 1997 42-125

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- ITAA 1997 42-160
- ITAA 1997 42-165
- ITAA 1997 42-345
- ITAA 1997 387-125
- ITAA 1997 387-305
- ITAA 1997 Subdiv. 960-Q
- ITAA 1997 960-335
- ITAA 1997 960-340
- ITAA 1997 960-345
- ITAA 1997 960-350

- ITAA 1936 82KJ
- ITAA 1936 82KK
- ITAA 1936 82KL
- ITAA 1936 82KZM

*Case References:*

- Fletcher & Anor v. FC of Taxation  
91 ATC 4950
- FC of Taxation v. Brand  
95 ATC 4633

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ATO references:

NO 2000/006979

BO

FOI number: I 1021527

ISSN: 1441-1172