



PR 2001/130 - Income tax: Palandri 2000 Project - Second Offering

 This cover sheet is provided for information only. It does not form part of *PR 2001/130 - Income tax: Palandri 2000 Project - Second Offering*

 This document has changed over time. This is a consolidated version of the ruling which was published on *10 October 2001*



Product Ruling

Income tax: Palandri 2000 Project – Second Offering

Contents	Para
What this Product Ruling is about	1
Date of effect	11
Withdrawal	13
Previous Ruling	14
Arrangement	15
Ruling	45
Explanations	68
Example	128
Detailed contents list	129

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**, **Previous Ruling**, **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 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 and to ensure that the participants in the arrangement 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.

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.

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 refers. In this Ruling this arrangement is sometimes referred to as the Palandri 2000 Project, or simply as '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 17-5 (ITAA 1997);
 - Division 35 (ITAA 1997);
 - Division 70 (ITAA 1997);
 - Division 328 (ITAA 1997);
 - Section 82KL of the *Income Tax Assessment Act 1936* ('ITAA 1936');
 - Section 82KZL (ITAA 1936);
 - Section 82KZME (ITAA 1936);
 - Section 82KZMF (ITAA 1936); and
 - Part IVA (ITAA 1936).

Goods and Services Tax

3. In this Ruling all fees and expenditure referred to include Goods and Services Tax ('GST') where applicable. In order for an entity (referred to in this Ruling as a 'Member') to be entitled to claim input tax credits for the GST included in its expenditure, it must be registered or required to be registered for GST and hold a valid tax invoice.

Changes in the Law

4. The Government is currently evaluating further changes to the tax system in response to the *Ralph Review of Business Taxation* and continuing business tax reform is expected to be implemented over a number of years. Although this Ruling deals with the taxation legislation enacted at the time it was issued, later amendments may

impact on this Ruling. Any such changes will take precedence over the application of this Ruling and, to that extent, this Ruling will be superseded.

5. Taxpayers who are considering participating in the Project are advised to confirm with their taxation adviser that changes in the law have not affected this Product Ruling since it was issued.

Note to promoters and advisers

6. Product Rulings were introduced for the purpose of providing certainty about tax consequences for participants in projects such as this. In keeping with that intention, the Tax Office suggests that promoters and advisers ensure that potential participants are fully informed of any legislative changes after the Ruling is issued.

Class of persons

7. The class of persons to whom this Ruling applies is the persons who are more specifically identified in the Ruling part of this Product Ruling and who enter into the arrangement specified 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. In this Ruling these persons are referred to as 'Members'.

8. 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

9. The Commissioner rules on the precise arrangement identified in the Ruling. If the arrangement described in this Ruling is materially different from the arrangement that is actually carried out the Ruling has no binding effect on the Commissioner. The Ruling will be withdrawn or modified.

10. A Product Ruling may only be reproduced in its entirety. Extracts may not be reproduced. As each Product Ruling is copyright, apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to the Manager, Legislative Services, AusInfo, GPO Box 1920, Canberra ACT 2601.

Date of effect

11. This Ruling applies prospectively from 10 October 2001, 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).

12. If a taxpayer has a more favourable private ruling (which is legally binding), the taxpayer can rely on that private ruling if the income year to which it relates has ended or has commenced but not yet ended. However if the arrangement covered by the private ruling has not commenced, 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

13. This Product Ruling is withdrawn and ceases to have effect after 30 June 2004. 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 arrangement specified below. 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 person's involvement in the arrangement.

Previous Ruling

14. This Ruling replaces Product Ruling PR 2001/11, which is withdrawn on and from the date this Ruling is made (10 October 2001). Product Ruling PR 2001/11 will continue to apply to participants who entered into the arrangement before 10 October 2001.

Arrangement

15. The arrangement that is the subject of this Ruling is specified below. This arrangement incorporates the following documents:

- Application for Product Ruling dated 6 November 2000;
- The Margaret River Wine Business Project 2001 Prospectus dated 29 January 2001;

- The Margaret River Wine Business Project 2001 Supplementary Prospectus dated 29 June 2001;
- **Constitution for the Margaret River Wine Business Project 2001 between Palandri Wines Ltd [the ‘Responsible Entity’], and the Member, undated;**
- **Lease and Management Agreement between Palandri Wines Ltd [the ‘Responsible Entity’], Palandri Production Ltd [the Wine Production Company] and the Member, undated;**
- Vineyard Management and Maintenance Agreement between Palandri Wines Ltd and Quenby Viticultural Services Pty Ltd, undated;
- Vineyard Establishment Agreement between Palandri Production Ltd and Quenby Viticultural Services Pty Ltd, undated; and
- Additional correspondence dated 30 November 2000, 19 December 2000, 21 December 2000, 22 January 2001, 1 February 2001, 15 February 2001 and 16 July 2001.

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

16. The documents highlighted are those the Members enter into. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Member, or any associate of the Member, will be a party to, with the exception of finance agreements, to which paragraphs 41 to 43 apply. The effect of these agreements is summarised as follows.

Overview

17. These arrangements are called the Palandri 2000 Project.

Location	South West Region of Western Australia, 50 kms west of Mt Barker in the Frankland River wine region.
Type of business each participant is carrying on	A commercial viticulture and wine production business for a period of 18 years.
Number of hectares under cultivation	106 hectares
Size of each Vineyard Lot	0.023 hectares

PR 2001/130

Number of vines per hectare	1,852
The term of the investment in years	18 years
Initial cost	\$11,000
Initial cost per hectare	\$478,260
Ongoing costs	Annual Management Fees and Rent.

18. Members applying under the Supplementary Prospectus dated 29 June 2001 enter into a Lease and Management Agreement. Palandri Production Ltd agrees to sub-lease to the Member an identifiable area of land called a 'Vineyard Lot' until the Project is terminated on 30 June 2018. Each Vineyard Lot is 0.023 hectares in size.

19. The Project Land is situated in the South West Region of Western Australia, approximately 50kms west of Mt Barker. Palandri Production Ltd holds a Head Lease over the land.

20. Palandri Production Ltd will sub-lease the Vineyard Lot to the Member for the purpose of Cultivating Vines and Harvesting Grapes. The vines must be planted by Palandri Production Ltd at the rate of 42 vines per Vineyard Lot either at the commencement date or by 30 October 2001.

21. The Prospectus states that there is no minimum subscription for the Project. Each investor may subscribe for a minimum of one Vineyard Lot. Members may also acquire a minimum of 400 shares in Margaret River Wine Production Ltd at a cost of \$5 per share.

22. Members will execute a Power of Attorney enabling the Responsible Entity, Palandri Wines Ltd, to act on their behalf as required when they make an application for a Vineyard Lot.

23. The Supplementary Prospectus expires on 31 October 2001. The services required to be performed in the initial period under the Lease and Management Agreement will be completed by 31 December 2001.

Constitution

24. The Constitution for the Project sets out the terms and conditions under which the Responsible Entity agrees to act for the Members and to manage the Project. The Responsible Entity will keep a register of Members. Members are entitled to assign their Member's Interest in certain circumstances. As stated in paragraph 7 above, this ruling only applies to those Members who have a purpose of staying in the arrangement for the full term of the Project. The Lease and Management Agreement will be executed on behalf of a Member following the Member signing the Application and a Power

of Attorney Form in the Prospectus. Members are bound by the Constitution and the Lease and Management Agreement by virtue of their participation in the Project.

Compliance Plan

25. The Responsible Entity has prepared a Compliance Plan in accordance with the Corporations Law. Its purpose is to ensure that the Responsible Entity meets its obligations as the Responsible Entity of the Project and that the rights of the Members are protected.

Interest in Land

26. A sub-lease is granted by the Head Lessor, Palandri Production Ltd, to the Members under the terms of the Management and Lease Agreement (cl.3.1). Members are granted an interest in land in the form of a sub-lease to use their Vineyard Lots for the purpose of cultivating Vines and Harvesting Grapes to produce, then market and distribute wine made from the grapes on their Vineyard Lot and additional grapes sourced from contract grape growers (Recital D). Members must pay rent to the Lessor of an amount of \$165 per Vineyard Lot on application for the initial period (from the date of application to 31 December 2001), \$165 on 1 January 2002 for the period 1 January 2002 to 30 June 2002, and thereafter on 1 July of each year. This fee will be indexed annually. The term of a Member's sub-lease is from the Commencement Date until 30 June 2018.

Lease and Management Agreement

27. Each Member enters into a Lease and Management Agreement with the Responsible Entity. The termination of the project is the date of completion of final harvest of the Grape Produce (Item 3 of Schedule). Members contract with the Responsible Entity to manage, maintain and harvest grapes from the vines and to produce and market wine on their behalf. Members pay a Management Fee of \$10,835 for services to be provided in the initial period (from the date of application to 31 December 2001).

28. A Management Fee of \$4,642 is payable for services to be completed during the period 1 January 2002 to 30 June 2002. An amount of \$4,010 is payable on 1 July 2002 for services to be completed during the period 1 July 2002 to 30 June 2003 and an amount annually thereafter which is the Members' proportion of the Management Costs (indexed) plus the Corporate Costs for performing the services under this agreement.

29. The Responsible Entity will carry out the following services under this agreement:

- Maintain a trickle irrigation system to the Vines on the relevant Vineyard Lot;
- Cultivate, tend, prune, fertilise, spray and otherwise care for the vines as when required;
- Use all reasonable measures to keep the relevant Vineyard Lot free from vermin, noxious weeds, pests and disease;
- At all times maintain the relevant Vineyard Lot according to good viticultural practice;
- take all reasonable steps to prevent and manage land degradation on the relevant Vineyard Lot and to attend to the maintenance and management of the soil quality on the relevant Vineyard Lot;
- harvest the Vines on the relevant Vineyard Lot and delivery of the Grape Produce to transport vehicles in accordance with good viticultural practice;
- purchase grapes and juice to supplement grapes grown on the relevant Vineyard Lot;
- arrange for the Wine to be bottled, corked and packaged and for the bottled wine to be placed in cartons;
- carry out the marketing strategy referred to in the Prospectus; and
- carry out the distribution and sales strategies referred to in the Prospectus.

30. The Responsible Entity will be responsible for paying the cost of public risk insurance in respect of the Vineyard Lot and insurance against destruction or damage from usual risks in accordance with approved wine industry practices in respect of the grape produce and the wine (cl.19.1).

31. A Member can terminate the Lease and Management Agreement where there has been a breach (of a substantial nature) by the Responsible Entity which has not been remedied after written notice by the Member to do so or where the Responsible Entity commits an act of bankruptcy or goes or is placed into liquidation (cl.13.2).

32. The Responsible Entity will provide a report to Members on or before 31 July and 31 January each financial year containing a

review of the operations of the Member's Wine Business during the relevant period (cl.17.1).

33. The Responsible Entity will tend to the Vines according to good viticultural practices. The services to be provided by the Responsible Entity over the term of the project are outlined in the Lease and Management (Item 11 of Schedule).

Harvesting

34. The Responsible Entity will be responsible for the harvesting of the grapes, and/or purchase of grapes and delivery of these grapes to the Winery and for production of Wine from those grapes and storage of the wine. Commencing from the date of the first commercially harvestable grape crop, or at such time or times as the Responsible Entity in its absolute discretion considers appropriate, the Responsible Entity will harvest or arrange for some other person to harvest the Grape Produce at such time or times as, in the opinion of the Responsible Entity, will result in Grape Produce suitable for the purposes of making quality wines.

35. The Receipts from the sale of Wine will be paid into the Proceeds Fund established by the Responsible Entity. Receipts received by the Responsible Entity are to be distributed in the following order of priority:

- Payment of any Annual Payments payable by the relevant Member;
- Payment of any other amounts payable by the relevant Member under the Lease and Management Agreement or any provision of the Constitution; and
- Distribution of the remainder to the relevant Member (cl.19.2 of the Lease and Management Agreement).

Fees

36. The total Fee payable on application under the Lease and Management Agreement for the Project is \$11,000 per Vineyard Lot. This fee includes a Management Fee of \$10,835 and a Rent Fee of \$165 and is payable either in full on application or under a Time Payment Option. Under the Time Payment Option, a first instalment of \$5,300 is payable on application and monthly payments of not less than \$600 are payable each month with any outstanding balance of the Fees due and payable on 15 November 2001. The services for these fees will be completed by 31 December 2001.

37. A Management Fee of \$4,642 is payable for services to be completed during the period 1 January 2002 to 30 June 2002. A

PR 2001/130

Management Fee of \$4,010 is payable for services to be carried out in the period commencing 1 July 2002 and continuing until 30 June 2003 and is payable on 1 July 2002.

38. For the years from 1 July 2003 to 30 June 2018, Management Fees are payable by the Member each year for the Member's proportion of the estimated management costs (indexed by the Inflation Adjustment Factor for the Relevant Financial Year) plus the Member's proportional interest of the estimated Corporate Costs.

39. Members must pay rent to the Lessor of an amount of \$165 per Vineyard Lot on application for the initial period (from the date of application to 31 December 2001), \$165 on 1 January 2002 for the period 1 January 2002 to 30 June 2002, and thereafter on 1 July of each year. This fee will be indexed annually.

40. The Application Monies will be held in the Trust Account by the Responsible Entity as Bare Trustee (cl.12.1).

Finance

41. Members can fund their involvement in the Project themselves, or borrow from Palandri Finance Ltd or United Pacific Finance Pty Ltd (lenders associated with the Responsible Entity) or borrow from an independent lender.

42. Where Members enter into finance arrangements with the lenders associated with the Responsible Entity, the following arrangements will apply.

43. Palandri Finance Ltd will borrow funds from a financial institution to on-lend to Members. Where Members obtain finance from United Pacific Finance Pty Ltd, Palandri Finance Ltd will provide a guarantee to United Pacific Finance Pty Ltd that, upon default by a Member, Palandri Finance will be responsible for the debt. The Directors of Palandri Finance Ltd have signed an undertaking that Palandri Finance Ltd will seek to recover all debts on normal commercial terms. All loans are fully recourse in nature.

44. This Ruling does not apply if the finance arrangement entered into by a Member includes or has any of the following features:

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL or the

funding arrangements transform the Project into a 'scheme' to which Part IVA may apply;

- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project other than Palandri Finance Ltd or United Pacific Finance Pty Ltd, are involved, or become involved, in the provision of finance to Members for the Project.

Ruling

Application of this Ruling

45. This Ruling applies only to Members who are accepted to participate in the Project on or before 31 October 2001 and who have executed a Management Agreement and a Lease Agreement before that date. The Member's participation in the Project must constitute the carrying on of a business of primary production.

46. A Member is not eligible to claim any tax deductions until the Member's application to enter the Project is accepted and the Project has commenced.

The Simplified Tax System ('STS')

Division 328

47. For a Member participating in the Project, the recognition of income and the timing of tax deductions, including those related to capital allowances, is different depending on whether the Member is an 'STS taxpayer'. To be an 'STS taxpayer' a Member:

- must be eligible to be an 'STS taxpayer'; and
- must have elected to be an 'STS taxpayer'.

Qualification

48. This Product Ruling assumes that a Member who is an 'STS taxpayer' is so for the income year in which their participation in the Project commences. A Member may become an 'STS taxpayer' at a later point in time. Also, a Member who is an 'STS taxpayer' may choose to stop being an 'STS taxpayer', or may cease to be eligible to be an 'STS taxpayer', during the term of the Project. These are contingencies relating to the circumstances of individual Members that cannot be accommodated in this Ruling. Such Members can ask for a private ruling on how the taxation legislation applies to them.

Tax outcomes for Members who are not 'STS taxpayers'***Assessable Income***

49. That part of the gross sales proceeds from the Project attributable to the Member's produce, less any GST payable on those proceeds (section 17-5), will be assessable income of the Member under section 6-5.

50. The Member recognises ordinary income from carrying on the business of growing grapes and producing and marketing wine at the time that income is derived.

51. Dividends received from Margaret River Wine Production Ltd will be assessable income of the Member under section 44.

Trading Stock***Section 70-35***

52. A Member who is not an 'STS taxpayer' may, in some years, hold grapes or grape juice or bottled wine that will constitute trading stock on hand. Where, in an income year, the value of trading stock on hand at the *end* of an income year exceeds the value of trading stock on hand at the *start* of an income year a Member must include the amount of that excess in assessable income.

53. Alternatively, where the value of trading stock on hand at the start of an income year exceeds the value of trading stock on hand at the end of an income year, a Member may claim the amount of that excess as an allowable deduction.

Deductions for Management fees, Rent, and Interest***Section 8-1***

54. A Member who is not an 'STS taxpayer' may claim tax deductions for the following revenue expenses:

PR 2001/130

Fee Type	ITAA 1997 Section	Year ended 30 June 2002	Year ended 30 June 2003	Year ended 30 June 2004
Management Fee	8-1	\$15,477 (\$10,835 + \$4,642) See Notes (i) & (ii) below	\$4,010 – See Notes (i) and (ii) (below)	See Notes (i), (ii) and (iv) (below)
Rent	8-1	\$330 (\$165 + \$165) - See Notes (i) & (ii)	\$165 (indexed) – See Notes (i), (ii) and (v) (below)	\$165 (indexed) – See Notes (i), (ii) and (v) (below)
Interest	8-1	As incurred See Note (iii) (below)	As incurred See Note (iii) (below)	As incurred See Note (iii) (below)

Notes:

- (i) If the Member is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (e.g., input tax credits). See example at paragraph 128.
- (ii) The Management fees and the Rent shown in the Lease and Management Agreement are deductible in full in the year that they are incurred. However, if a Member **chooses** to prepay fees for the doing of a thing (e.g., the provision of management services or the leasing of land) that will not be wholly done in the same income year as the fees are incurred, the prepayment rules of the ITAA 1936 may apply to apportion those fees. In such cases, the tax deduction for the prepaid fee **MUST** be determined using the formula shown in paragraph 104 unless the expenditure is ‘excluded expenditure’. ‘Excluded expenditure’ is an ‘exception’ to the prepayment rules and is deductible in full in the year in which it is incurred. For the purpose of this Ruling ‘excluded expenditure’ refers to an amount of expenditure of less than \$1,000.
- (iii) The deductibility or otherwise of interest arising from loan agreements entered into with financiers other than Palandri Finance Ltd or United Pacific Finance Pty Ltd is outside the scope of this Ruling. However, all Members, including those who finance their participation in the Project other than with Palandri Finance Ltd or United Pacific Finance Pty Ltd, should read carefully the discussion of the prepayment rules

in paragraphs 98 to 112 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant loan agreement or is at the Member's choice.

- (iv) For each year commencing from 1 July 2003 until 30 June 2018, Management Fees are payable by each Member yearly consisting of the Member's proportion of the estimated management costs (indexed by the Inflation Adjustment Factor for the Relevant Financial Year) plus the Member's proportional interest of the estimated Corporate Costs.
- (v) Rent of \$165, indexed annually by the Inflation Adjustment Factor for the relevant financial year, is payable on 1 July each year commencing on 1 July 2002.

Tax outcomes for Members who are 'STS taxpayers'

Assessable Income

55. That part of the gross sales proceeds from the Project attributable to the Member's produce, less any GST payable on those proceeds (section 17-5), will be assessable income of the Member under section 6-5.

56. The Member recognises ordinary income from carrying on the business of growing grapes and producing and marketing wine at the time the income is received (paragraph 328-105(1)(a)).

57. Dividends received from Margaret River Wine Production Ltd will be assessable as income under section 44.

Trading stock

Section 328-285

58. A Member who is an 'STS taxpayer' may, in some years, hold grape or grape juice or bottled wine that will constitute trading stock on hand. Where, for such a Member, for an income year, the difference between the value of all their trading stock at the start and a reasonable estimate of it at the end, is less than \$5,000, they do not have to account for that difference under the ordinary trading stock rules in Division 70 (subsection 328-285(1)).

59. Alternatively, a Member who is an 'STS taxpayer' may instead choose to account for trading stock in an income year under the provisions of Division 70 (subsection 328-285(2)).

Deductions for Management fees, Rent, and Interest*Section 8-1 and section 328-105*

60. A Member who is an 'STS taxpayer' may claim tax deductions for the following revenue expenses:

Fee Type	ITAA 1997 Sections	Year ended 30 June 2002	Year ended 30 June 2003	Year ended 30 June 2004
Management Fee	8-1 & 328-105	\$15,477 (\$10,8345 + \$4,642) – See Notes (vi) & (vii) (below)	\$4,010 – See Notes (vi), (vii) & (viii) (below)	See Notes (vi), (vii), (viii) & (x) (below)
Rent	8-1 & 328-105	\$330 (\$165 + \$165) – See Notes (vi) & (vii) (below)	\$165 (indexed) – See Notes (vi), (vii), (viii) & (xi) (below)	\$165 (indexed) – See Notes (vi), (vii), (viii) & (xi) (below)
Interest	8-1 & 328-105	When paid- See Note (ix) (below)	When paid – See Note (ix) (below)	When paid - See Note (ix) (below)

Notes:

- (vi) If the Member is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (e.g., input tax credits). See example at paragraph 128.
- (vii) If, for any reason, an amount shown in the Table above is not fully paid in the year in which it is incurred by a Member who is an 'STS taxpayer' then the amount is only deductible to the extent to which it has been paid, or has been paid for the Member. Any amount or part of an amount shown in the Table above, which is not paid in the year in which it is incurred, will be deductible in the year in which it is actually paid.
- (viii) Where a Member who is an 'STS taxpayer', pays the Management fees and the Rent in the relevant income years shown in the Lease and Management Agreement, those fees are deductible in full in the year that they are paid. However, if a Member chooses to prepay fees for the doing of a thing (e.g., the provision of management services or the leasing of land) that will not be wholly

done in the same income year as the fees are incurred, the prepayment rules of the ITAA may apply to apportion those fees. In such cases, the tax deduction for the prepaid fee must be determined using the formula shown in paragraph 104, unless the expenditure is 'excluded expenditure'. 'Excluded expenditure' is an 'exception' to the prepayment rules, and is deductible in full in the year in which it is incurred. For the purpose of this Ruling 'excluded expenditure' refers to an amount of expenditure of less than \$1,000.

- (ix) The deductibility or otherwise of interest arising from loan agreements entered into with financiers other than Palandri Finance Ltd or United Pacific Finance Pty Ltd, is outside the scope of this Ruling. However all Members, including those who finance their participation in the Project other than with Palandri Finance Ltd or United Pacific Finance Pty Ltd, should read carefully the discussion of the prepayment rules in paragraph 98 to 112 (below) as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is required under the relevant loan agreement or is at the Member's choice.
- (x) For each year commencing from 1 July 2003 until 30 June 2018, Management Fees are payable by each Member yearly consisting of the Member's proportion of the estimated management costs (indexed by the Inflation Adjustment Factor for the Relevant Financial Year) plus the Member's proportional interest of the estimated Corporate Costs.
- (xi) Rent of \$165, indexed annually by the Inflation Adjustment Factor for the relevant financial year, is payable on 1 July each year commencing on 1 July 2002.

Tax outcomes that apply to all Members

Division 35 – Deferral of losses from non-commercial business activities

Section 35-55 – Commissioner's discretion

61. For a Member who is an individual and who enters the Project during the year ended 30 June 2002 the rule in section 35-10 may apply to the business activity comprised by their involvement in this Project. Under paragraph 35-55(1)(b) the Commissioner will decide for the income year ending 30 June 2002 that the rule in section 35-10

does not apply to this activity provided that the Project is carried out in the manner described in this Ruling.

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

- a Member's business activity satisfies one of the objective tests in sections 35-30, 35-35, 35-40 or 35-45; or
- the 'Exception' in subsection 35-10(4) applies (see paragraph 116 in the Explanations part of this ruling, below).

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

64. Members are reminded of the important statement made on Page 1 of this Product Ruling. Therefore, Members should not see the Commissioner's decision to exercise the discretion in paragraph 35-55(1)(b) as an indication that the Tax Office sanctions or guarantees the Project or the product to be a commercially viable investment. An assessment of the Project or the product from this perspective has not been made.

Sections 82KZME – 82KZMF, 82KL, and Part IVA

65. For a Member who participates in the Project and incurs expenditure as required by the Lease and Management Agreement the following provisions of the ITAA 1936 have application as indicated:

- expenditure by a Member does not fall within the scope of sections 82KZME-82KZMF (but see paragraphs 98 to 112);
- section 82KL does not apply to deny the deductions otherwise allowable; and
- the relevant provisions in Part IVA will not be applied to cancel a tax benefit obtained under a tax law dealt with in this Ruling.

Part 3-1: Capital Gains Tax

66. Each Member has the right to subscribe for 400 shares in Margaret River Wine Production Ltd at a cost of \$5 per share. Unless any shares in that company are trading stock of the Member or otherwise assessable on the revenue account, a capital gain or loss will arise on the sale of those shares.

67. In the event that Margaret River Wine Production Ltd is liquidated at the conclusion of the Project, further taxation considerations arise for the Member holding shares in the company. Any distribution made to a Member on liquidation of the company would be deemed to be a dividend to the Member, to the extent of the company's undistributed profits. This dividend would be assessable as a normal dividend and may have franking credits attached. Further, a capital gain or loss could arise, based on the difference between the Member's cost base and the amount distributed in accordance with the provisions of Part 3-1 of the ITAA 1997.

Explanations

Is the Member carrying on a business?

68. For the amounts set out in the Tables above to constitute allowable deductions the Member's viticulture activities as a participant in the Palandri 2000 Project must amount to the carrying on of a business of primary production.

69. Where there is a business, or a future business, the gross proceeds from the sale of the grape produce and the wine will constitute gross assessable income in their own right. The generation of 'business income' from such a business, or future business, provides the backdrop against which to judge whether the outgoings in question have the requisite connection with the operations that more directly gain or produce this income.

70. For schemes such as that of the Palandri 2000 Project, Taxation Ruling TR 2000/8 sets out the circumstances in which the Member's activities can constitute the carrying on of such a business (see paragraph 89 of Taxation Ruling TR 2000/8). As Taxation Ruling TR 2000/8 discusses, these have been established in court decisions such as *FCT v. Lau* 84 ATC 4929.

71. Generally, a Member will be carrying on a business of viticulture, and hence primary production, if:

- the Member has an identifiable interest (by lease or by licence) in the land on which the Member's grapevines are established;

- the Member has a right to harvest and sell the grapes each year from those grapevines and to sell the wine produced;
- the viticulture activities are carried out on the Member's behalf; and
- the viticulture activities of the Member are typical of those associated with a viticulture business; and
- the weight and influence of general indicators point to the carrying on of a business.

72. In this Project, each Member enters into a Lease and Management Agreement with Palandri Wines Ltd (the Responsible Entity) and Palandri Production Ltd (the Wine Production Company).

73. Under the Lease and Management Agreement each individual Member will have rights over a specific and identifiable area of 0.023 hectares of land consistent with the intention to carry on a business of growing grapes and the production, marketing and sale of wine. The Lease and Management Agreement provides the Member with an ongoing interest in the specific grapevines on the sub-leased area for the term of the Project. Under the sub-lease the Member must use the land in question for the purpose of carrying out viticultural activities, and for no other purpose. The sub-lease allows the Responsible Entity come onto the land to carry out its obligations under the Lease and Management Agreement.

74. Under the Lease and Management Agreement the Responsible Entity is engaged by the Member to maintain a Vineyard Lot on the Member's leasehold land during the term of the Project. The Responsible Entity has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to maintain the Vineyard Lots on the Member's behalf.

75. Under the Lease and Management Agreement Members engage the Responsible Entity, Palandri Wines Ltd, to cultivate, tend, train, prune, fertilise, replant, spray and otherwise care for the grape vines as and when required that is consistent with Good Viticultural Practice and to use all reasonable measures to keep the Vineyard Lot free from vermin, noxious weeds, pests and diseases. The Responsible Entity is also engaged to harvest and sell, on the Member's behalf, the grapes grown on the Member's Vineyard Lot.

76. The general indicators of a business, as used by the Courts, are described in Taxation Ruling TR 97/11. Positive findings can be made from the arrangement's description for all the indicators.

77. The activities that will be regularly carried out during the term of the Project demonstrate a significant commercial purpose. Based on reasonable projections, a Member in the project will derive

assessable income from the sale of the grape produce and wine that will return a 'before-tax' profit, i.e., a 'profit' in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

78. The pooling of grapes grown on the Member's Vineyard Lots with the grapes of other Members does not detract from a view that the Member is carrying on a business of viticulture. Each Member's proportionate return from the sale of the pooled grapes will reflect the number of Vineyard Lots held by that Member.

79. The Responsible Entity's services are based on accepted viticulture practices. They are of the type ordinarily found in viticulture ventures that would commonly be said to be businesses. While the size of the Member's allotment is relatively small, it is of a size and scale that would allow it to be commercially viable, particularly when it is part of a larger overall project such as the Palandri 2000 Project (see Taxation Ruling IT 360).

80. The Member's degree of control over the Responsible Entity as evidenced by the Lease and Management Agreement, and supplemented by the Corporations Act, is sufficient. During the term of the Project, the Manager will provide the Member with regular progress reports on the Member's Vineyard Lots and the activities carried out on the Member's behalf. Members are able to terminate arrangements with the Responsible Entity in certain instances, such as cases of default or neglect.

81. 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. For the purposes of this Ruling, the Member's viticulture activities in the Palandri 2000 Project will constitute the carrying on of a business.

The Simplified Tax System

Division 328

82. Subdivision 328-F sets out the eligibility requirements that a Member must satisfy in order to enter the STS and Subdivision 328-G sets out the rules for entering and leaving the STS.

83. The question of whether a Member is eligible to be an 'STS taxpayer' is outside the scope of this Product Ruling. Therefore, any Grower who relies on those parts of this Ruling that refer to the STS will be assumed to have correctly determined whether or not they are eligible to be an 'STS taxpayer'.

Deductibility of management fees and rent fees***Section 8-1***

84. Consideration of whether the initial management fees and the rent are deductible under section 8-1 begins with the first limb of the section. This view proceeds on the following basis:

- the outgoing 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 is contractually committed to a venture that may not turn out to be a business, there can be doubt about whether the relevant business has commenced, and hence, whether the second limb applies. However, that does not preclude the application of the first limb in determining whether the outgoing in question has a sufficient connection with activities to produce assessable income.

85. The rent and management fees associated with the viticulture activities will relate to the gaining of income from the Member's business of viticulture (see above), and hence have a sufficient connection to the operations by which income (from the regular sale of grape produce and wine) is to be gained from this business. They will thus be deductible under the first limb of section 8-1. Further, no 'non-income producing' purpose in incurring the fee is identifiable from the arrangement. The fee appears to be reasonable. There is no capital component of the management fee. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

Possible application of prepayment provisions

86. Under the Lease and Management Agreement neither the management fees nor the rent are for things to be done beyond 30 June in the year in which the relevant amounts are incurred. In these circumstances, the prepayment provisions in sections 82KZME and 82KZMF have no application to these fees.

87. However, where a Member chooses to prepay these fees for a period beyond the income year in which the expenditure is incurred, the prepayment provisions (see paragraphs 98 to 112) will apply to determine the amount and timing of the deductions regardless of

whether the Member is an 'STS taxpayer' or not. These provisions apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes 'STS taxpayers' from the operation of section 82KZMF. This is subject to the 'excluded expenditure' exception. For the purpose of this Ruling 'excluded expenditure' refers to an amount of expenditure of less than \$1,000.

Timing of deductions

88. In the absence of any application of the prepayment provisions, the timing of deductions for the management fees or the rent will depend upon whether a Member is an 'STS taxpayer' or is not an 'STS taxpayer'.

89. If the Member is not an 'STS taxpayer', the management fees and the rent are deductible in the year in which they are incurred.

90. If the Member is an 'STS taxpayer' the management fees and the rent are deductible in the income year in which they are paid, or are paid for the Member (paragraph 328-105(1)(b)). If any amount that is properly incurred in an income year remains unpaid at the end of that income year, the unpaid amount is deductible in the income year in which it is actually paid or is paid for the Member.

Interest deductibility

Section 8-1

(i) Members who use Palandri Finance Ltd or United Pacific Pty Ltd as the finance provider

91. Some Members may finance their participation in the Project through a loan facility with Palandri Finance Ltd or United Pacific Finance Pty Ltd. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of rent and management fees.

92. The interest incurred for the year ended 30 June 2002 and in subsequent years of income will be in respect of a loan to finance the Grower's business operations of growing grapes and producing wine and is therefore directly connected with the gaining of 'business income' from the Project. Such interest will, therefore, have a sufficient connection with the gaining of assessable income to be deductible under section 8-1.

93. As with the management fees and rent, in the absence of any application of the prepayment provisions (see paragraphs 94 to 108), the timing of deductions for interest will again depend upon whether a Member is an 'STS taxpayer' or is not an 'STS taxpayer'.

94. If the Member is not an ‘STS taxpayer’, interest is deductible in the year in which it is incurred.

95. If the Member is an ‘STS taxpayer’ interest is not deductible until it has been both incurred and paid, or is paid for the Member. If interest that is properly incurred in an income year remains unpaid at the end of that income year, the unpaid amount is deductible in the income year in which it is actually paid, or is paid for the Member.

(ii) Members who DO NOT use Palandri Finance Ltd or United Pacific Finance Pty Ltd as the finance provider

96. The deductibility of interest incurred by Members who finance their participation in the Project through a loan facility with a bank or financier other than Palandri Finance Ltd or United Pacific Finance Pty Ltd is outside the scope of this Ruling. Product Rulings only deal with arrangements where all details and documentation have been provided to, and examined by the Tax Office.

97. While the terms of any finance agreement entered into between relevant Members and such financiers are subject to commercial negotiation, those agreements may require interest to be prepaid. Alternatively, a Member may choose to prepay such interest. Unless such prepaid interest is ‘excluded expenditure’ any tax deduction that is allowable will be subject to the prepayment provisions of the ITAA 1936 (see paragraphs 94 to 108).

Prepayment provisions

Sections 82KZL to 82KZMF

98. The prepayments provisions contained in Subdivision H of Division 3 of Part III of the ITAA 1936 affect the timing of deductions for certain prepaid expenditure. These provisions apply to certain expenditure incurred under an agreement in return for the doing of a thing under the agreement (e.g., the performance of management services or the leasing of land) that will not be wholly done within the same year of income as the year in which the expenditure is incurred. If expenditure is incurred to cover the provision of services to be provided within the same year, then it is not expenditure to which the prepayment rules apply.

99. For this Project only section 82KZL (an interpretative provision) and sections 82KZME and 82KZMF are relevant. Where the requirements of sections 82KZME and 82KZMF are met, taxpayers determine deductions for prepaid expenditure under section 82KZMF using the formula in subsection 82KZMF. These provisions also apply to ‘STS taxpayers’ because there is no specific exclusion

contained in section 82KZME that excludes 'STS taxpayers' from the operation of section 82KZMF.

Sections 82KZME and 82KZMF

100. Where the requirements of subsections 82KZME(2) and (3) are met, the formula in subsection 82KZMF(1) (see below) will apply to apportion expenditure that is otherwise deductible under section 8-1 of the ITAA 1997. The requirements of subsection 82KZME(2) will be met if expenditure is incurred by a taxpayer in return for the doing of a thing that is not to be wholly done within the year the expenditure is made. The year in which such expenditure is incurred is called the 'expenditure year' (subsection 82KZME(1)).

101. The requirements of subsection 82KZME(3) will be met where the agreement (or arrangement) has the following characteristics:

- the taxpayer's allowable deductions under the agreement for the 'expenditure year' exceed any assessable income attributable to the agreement for that year; and
- the taxpayer does not have effective day to day control over the operation of the agreement. That is, the significant aspects of the arrangement are managed by someone other than the taxpayer; and
- either :
 - (a) there is more than one participant in the agreement in the same capacity as the taxpayer; or
 - (b) the person who promotes, arranges or manages the agreement (or an associate of that person) promotes similar agreements for other taxpayers.

102. For the purpose of these provisions, the agreement includes all activities that relate to the agreement (subsection 82KZME(4)). This has particular relevance for a Member in this Project who, in order to participate in the Project may borrow funds from a financier other than Palandri Finance Ltd or United Pacific Finance Pty Ltd.

Although undertaken with an unrelated party, that financing would be an element of the arrangement. The funds borrowed and the interest deduction are directly related to the activities under the arrangement. If a Member prepays interest under such financing arrangements, the deductions allowable will be subject to apportionment under section 82KZMF.

103. There are a number of exceptions to these rules, but for Members participating in this Project, only the 'excluded expenditure'

exception in subsection 82KZME(7) is relevant. 'Excluded expenditure' is defined in subsection 82KZL(1). However, for the purposes of Members in this Project, 'excluded expenditure' is prepaid expenditure incurred under the arrangement that is less than \$1,000. Such expenditure is immediately deductible.

104. Where the requirements of section 82KZME are met, section 82KZMF applies to apportion relevant prepaid expenditure. Section 82KZMF uses the formula below, to apportion prepaid expenditure and allow a deduction over the period that the benefits are provided.

$$\text{Expenditure X} = \frac{\text{Number of days of eligible service period in the year of income}}{\text{Total number of days of eligible service period}}$$

105. In the formula 'eligible service period' (defined in subsection 82KZL(1)) means, the period during which the thing under the agreement is to be done. The eligible service period begins on the day on which the thing under the agreement commences to be done or on the day on which the expenditure is incurred, whichever is the later, and ends on the last day on which the thing under the agreement ceases to be done, up to a maximum of 10 years.

Application of the prepayment provisions to this Project

106. In this Project, an initial Vineyard Lot Management Fee of \$10,835 and Rent of \$165 per Vineyard Lot will be incurred on execution of the Lease and Management Agreement. The Management Fee and the Rent are charged for providing management services or leasing land to a Member by 30 June of the year of execution of the Agreements. Under the agreements, further annual expenditure is required each year during the term of the Project for the provision of management services and land until 30 June in those years.

107. In particular, the Management Fee is expressly stated to be for a number of specified services. No explicit conclusion can be drawn from the description of the arrangement that the initial Management Fee has been inflated to result in reduced fees being payable for management fees in subsequent years.

108. There is also no evidence that might suggest the management services covered by the fee could not be provided within the relevant expenditure year. Thus, for the purposes of this Ruling, it can be accepted that no part of the initial management fee, and the fees for subsequent years, is for the Manager doing 'things' that are not to be wholly done within the expenditure year. Under the Lease and Management Agreement, rent is payable annually in advance for the sub-lease of the land during the expenditure year. Similarly, under the loan agreements to be executed between Members and Palandri

Finance Ltd or United Pacific Finance Pty Ltd interest is payable monthly in arrears.

109. On this basis, provided a Member incurs expenditure as required under the Project agreements, as set out in paragraphs 36 to 39, then the basic precondition in subsection 82KZME(2) not satisfied and, in these circumstances, section 82KZMF will have no application.

Members who choose to pay fees for a period in excess of that required by the Project's agreements

110. Although not required under either the Lease and Management Agreement or the Loan Agreement with Palandri Finance Ltd or United Pacific Finance Pty Ltd, a Member participating in the Project may **choose** to prepay fees/interest for a period beyond the 'expenditure year'. Similarly, Members who use financiers other than Palandri Finance Ltd or United Pacific Pty Ltd may either choose, or be required to prepay interest. Where this occurs, contrary to the conclusion reached in paragraph 109 above, section 82KZMF will apply to apportion the expenditure and allow a deduction over the period in which the prepaid benefits are provided.

111. For these Members, the amount and timing of deductions for any relevant prepaid Management Fees, prepaid Rent, or prepaid interest will depend upon when the respective amounts are incurred and what the 'eligible service period' is in relation to these amounts.

112. However, as noted above, prepaid fees of less than \$1,000 incurred in an expenditure year will be 'excluded expenditure' and will be not subject to apportionment under section 82KZMF.

Deferral of losses from non-commercial business activities

Division 35

113. Under the rule in subsection 35-10(2) a deduction for a loss incurred by an individual (including an individual in a general law partnership) from certain business activities will not be allowable in an income year unless:

- the 'Exception' in subsection 35-10(4) applies;
- one of four objective tests in sections 35-30, 35-35, 35-40 or 35-45 is met; or
- if one of the objective tests is not satisfied, the Commissioner exercises the discretion in section 35-55.

114. Generally, a loss in this context is, for the income year in question, the excess of an individual taxpayer's allowable deductions

attributable to the business activity over that taxpayer's assessable income from the business activity.

115. Under the loss deferral rule in subsection 35-10(2) the relevant loss is not able to be taken into account in the calculation of taxable income in the year that loss arose. Instead, in a later year it may be offset against any income from the same or similar business activity, or, if one of the objective tests is passed, or the Commissioner's discretion exercised, against other income.

116. For the purposes of applying the objective tests, subsection 35-10(3) allows taxpayers to group business activities 'of a similar kind'. Under subsection 35-10(4), there is an 'Exception' to the general rule in subsection 35-10(2) where the loss is from a primary production business activity and the individual taxpayer has other assessable income for the income year from sources not related to that activity, of less than \$40,000 (excluding any net capital gain). As both subsections relate to the individual circumstances of Members who participate in the Project they are beyond the scope of this Product Ruling and are not considered further.

117. In broad terms, the objective tests require:

- (a) at least \$20,000 of assessable income in that year from the business activity (section 35-30);
- (b) the business activity results in a taxation profit in 3 of the past 5 income years (including the current year)(section 35-35);
- (c) at least \$500,000 of real property is used on a continuing basis in carrying on the business activity in that year (section 35-40); or
- (d) at least \$100,000 of certain other assets are used on a continuing basis in carrying on the business activity in that year (section 35-45).

118. A Member who participates in the Project will be carrying on a business activity that is subject to these provisions. Information provided with the application for this Product Ruling indicates that a Member who acquires the minimum investment of one Vineyard Lot in the Project is unlikely to have their activity pass one of the objective tests until the income year ended 30 June 2005. Members who acquire more than one interest in the Project may however, find that their activity meets one of the tests in an earlier income year.

119. Therefore, prior to this time, unless the Commissioner exercises an arm of the discretion under paragraphs 35-55(1)(a) or (b), the rule in subsection 35-10(2) will apply to defer to a future income year any loss that arises from the Member's participation in the Project.

120. The first arm of the discretion in paragraph 35-55(1)(a) relates to 'special circumstances' applicable to the business activity, and has no relevance for the purposes of this Product Ruling. However, the second arm of the discretion in paragraph 35-55(1)(b) may be exercised by the Commissioner where:

- (i) the business activity has started to be carried on; and
- (ii) because of its nature, it has not satisfied one of the objective tests; and
- (iii) there is an objective expectation that the business activity of an individual taxpayer will either pass one of the objective tests or produce a taxation profit within a period that is commercially viable for the industry concerned.

121. Information provided with this Product Ruling indicates that a Member who acquires the minimum investment of one Vineyard Lot in the Project is expected to be carrying on a business activity that will either pass one of the objective tests, or produce a taxation profit, for the year ended 30 June 2003. The Commissioner will decide for such a Member that it would be reasonable to exercise the second arm of the discretion until the year ended 30 June 2002. Subsection 35-55(2) prevents the Commissioner exercising the discretion beyond this year.

122. This Product Ruling is issued on a prospective basis (i.e., before an individual Member's business activity starts to be carried on). The Project, however, may fail to be carried on during the income years specified above (see paragraph 61), in the manner described in the Arrangement (see paragraphs 15 to 44). If so, this Ruling, and specifically the decision in relation to paragraph 35-55(1)(b), that it would be unreasonable that the loss deferral rule in subsection 35-10(2) not apply, may be affected, because the Ruling no longer applies (see paragraph 9). Members may need to apply for private rulings on how paragraph 35-55(1)(b) will apply in such changed circumstances.

123. In deciding that the second arm of the discretion in paragraph 35-55(1)(b) will be exercised on this conditional basis, the Commissioner has relied upon:

- the report of the independent viticulturist; and
- independent, objective, and generally available information relating to the viticultural industry.

Section 82KL - recouped expenditure

124. The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefits(s)'.

Insufficient 'additional benefits' will be provided to trigger the application of section 82KL. It will not apply to deny the deduction otherwise allowable under section 8-1.

Part IVA - general tax avoidance provisions

125. 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).

126. The Palandri 2000 Project will be a 'scheme'. A Member will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 54 and 60 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.

127. Members to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting of the grapes and sale of the wine. There are no facts that would suggest that Members 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 arm's length, or, if any parties are not at arm's length, that any adverse tax consequences result. Further, 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 dominant purpose of obtaining a tax benefit.

Example

Entitlement to GST input tax credits

128. Susan, who is a sole trader and registered for GST, contracts with a manager to manage her viticulture business. Her manager is registered for GST and charges her a management fee payable every six months in advance. On 1 December 2001 Susan receives a valid tax invoice from her manager requesting payment of a management fee in advance, and also requesting payment for an improvement in the connection of electricity for her vineyard that she contracted him to carry out. The tax invoice includes the following details:

Management fee for period 1/1/2002 to 30/6/2002	\$4 400*
Carrying out of upgrade of power for your vineyard as quoted	<u>\$2 200*</u>

PR 2001/130

Total due and payable by 1 January 2002 \$6 600
(includes GST of \$600)

*Taxable supply

Susan pays the invoice by the due date and calculates her input tax credit on the management fee (to be claimed through her Business Activity Statement) as:

$$1/11 \times \$4400 = \$400.$$

Hence her outgoing for the management fee is effectively \$4400 *less* \$400, or \$4000.

Similarly, Susan calculates her input tax credit on the connection of electricity as:

$$1/11 \times \$2200 = \$200.$$

Hence her outgoing for the power upgrade is effectively \$2200 *less* \$200, or \$2000.

In preparing her income tax return for the year ended 30 June 2002, Susan is aware that the management fee is deductible in the year incurred. She calculates her management fee deduction as \$4000 (not \$4400).

Susan is aware that the electricity upgrade is deductible 10% per year over a 10 year period. She calculates her deduction for the power upgrade as \$200 (one tenth of \$2000 only, not one tenth of \$2200).

Detailed contents list

129. Below is a detailed contents list for this Product Ruling:

	Paragraph
What this Product Ruling is about	1
Tax law(s)	2
Goods and Services Tax	3
Changes in the Law	4
Note to promoters and advisers	6
Class of persons	7
Qualifications	9
Date of effect	11
Withdrawal	13
Previous Ruling	14

Arrangement	15
Overview	17
Constitution	24
Compliance plan	25
Interest in Land	26
Lease and Management Agreement	27
Harvesting	34
Fees	36
Finance	41
Ruling	45
Application of this Ruling	45
The Simplified Tax System ('STS')	47
Division 328	47
Qualification	48
Tax Outcomes for Members who are not 'STS taxpayers'	49
<i>Assessable Income</i>	49
<i>Trading Stock</i>	52
<i>Section 70 – 35</i>	52
<i>Deductions for Management fees, Rent, and Interest</i>	54
<i>Section 8-1</i>	54
Tax outcomes for Members who are 'STS taxpayers'	55
<i>Assessable Income</i>	55
<i>Trading Stock</i>	58
<i>Section 328-285</i>	58
<i>Deductions for Management fees, Rent, and Interest</i>	60
<i>Section 8-1 and section 328-105</i>	60
Tax Outcomes that apply to all Members	61
<i>Division 35 – Deferral of losses from non-commercial business activities</i>	61
<i>Section 35-55 – Commissioner's discretion</i>	61
Sections 82KZME – 82KZMF, 82KL, and Part IVA	65
Part 3-1: Capital Gains Tax	66
Explanations	68

PR 2001/130

Is the Member carrying on a business?	68
The Simplified Tax System	82
<i>Division 328</i>	82
Deductibility of management fees and rent fees	84
<i>Section 8-1</i>	84
<i>Possible application of prepayment provisions</i>	86
<i>Timing of deductions</i>	88
Interest deductibility	91
<i>Section 8-1</i>	91
(i) <i>Members who use Palandri Finance Ltd or United Pacific Finance Pty Ltd as the finance provider</i>	91
(ii) <i>Members who DO NOT use Palandri Finance Ltd or United Pacific Finance Pty Ltd as the finance provider</i>	96
Prepayment Provisions	98
<i>Sections 82KZL to 82KZMF</i>	98
Sections 82KZME and 82KZMF	100
<i>Application of the prepayment provisions to this Project</i>	106
<i>Members who <u>choose</u> to pay fees for a period in excess of that required by the Project's agreements</i>	110
Deferral of losses from non-commercial business activities	113
<i>Division 35</i>	113
Section 82KL – recouped expenditure	124
Part IVA – general tax avoidance provisions	125
Example	128
Entitlement to GST input tax credit	128
Detailed contents list	129

Commissioner of Taxation

10 October 2001

Previous draft:

Not previously issued in draft form

TR 97/11; TR 97/16;

TD 93/34; TR 98/22; IT 360; IT 175;
IT 2001*Related Rulings/Determinations:*TR 2000/8; PR 2000/93; PR 1999/95;
PR 2000/114; TR 92/1; TR 92/20;*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 8-1(1)(a)
- ITAA 1997 8-1(1)(b)
- ITAA 1997 17-5
- ITAA 1997 Division 27
- ITAA 1997 Division 35
- ITAA 1997 35-10
- ITAA 1997 35-10(2)
- ITAA 1997 35-10(3)
- ITAA 1997 35-10(4)
- ITAA 1997 35-30
- ITAA 1997 35-35
- ITAA 1997 35-40
- ITAA 1997 35-45
- ITAA 1997 35-55
- ITAA 1997 35-55(1)
- ITAA 1997 35-55(1)(a)

- ITAA 1997 35-55(1)(b)
- ITAA 1997 35-55(2)
- ITAA 1997 Div 70
- ITAA 1997 70-35
- ITAA 1997 Div 328
- ITAA 1997 Subdiv 328-F
- ITAA 1997 Subdiv 328-G
- ITAA 1997 328-105
- ITAA 1997 328-105(1)(b)
- ITAA 1997 328-285
- ITAA 1997 328-285(1)
- ITAA 1997 328-285(2)
- ITAA 1936 82KL
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
- ITAA 1936 82KZME
- ITAA 1936 82KZME(1)
- ITAA 1936 82KZME(2)
- ITAA 1936 82KZME(3)
- ITAA 1936 82KZME(4)
- ITAA 1936 82KZME(7)
- ITAA 1936 82KZMF
- ITAA 1936 82KZMF(1)
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)

Case references:

- FCT v. Lau 84 ATC 4929

ATO references:

NO T2001/16377
 BO
 FOI number: I 1023644
 ISSN: 1441-1172