



# ***PR 2001/73 - Income tax: Brooklyn Park Olive Groves Project No 2***

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 This document has changed over time. This is a consolidated version of the ruling which was published on *29 August 2001*



## Product Ruling

### Income tax: Brooklyn Park Olive Groves Project No 2

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#### **Preamble**

*The number, subject heading, and the **What this Product Ruling is about** (including **Tax law(s)**, **Class of persons and Qualifications** sections), **Date of effect**, **Withdrawal**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. Product Ruling PR 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.*

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

#### **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 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.

## What this Product Ruling is about

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1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates. In this Ruling this arrangement is sometimes referred to as the Brooklyn Park Olive Groves Project No2, 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 27 (ITAA 1997);
  - Division 35 (ITAA 1997);
  - Section 387-55 (ITAA 1997);
  - Section 387-125 (ITAA 1997);
  - Section 387-165 (ITAA 1997);
  - Section 388-55 (ITAA 1997);
  - Section 82KL of the *Income Tax Assessment Act 1936* ('ITAA 1936');
  - Section 82KZL (ITAA 1936);
  - Section 82KZM (ITAA 1936);
  - Section 82KZMB (ITAA 1936);
  - Section 82KZMC (ITAA 1936);
  - Section 82KZMD (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 Grower) 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.

### **Business Tax Reform**

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 laws enacted at the time it was issued, future tax changes may affect the operation of those laws and, in particular, the tax deductions that are allowable. Where tax laws change, those changes will take precedence over the application of this Ruling, and to that extent, this Ruling will be superseded.

5. Taxpayers who are considering investing 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 investors in projects such as this. In keeping with that intention, the Tax Office suggests that promoters and advisers ensure that potential investors are fully informed of any changes in tax laws that take place after the Ruling is issued. Such action should minimise suggestions that potential investors have been negligently or otherwise misled.

### **Class of persons**

7. 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'.

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 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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11. This Ruling applies prospectively from 23 May 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 the private ruling if the income year to which the private ruling relates has ended, or has commenced but not yet ended. However, if the arrangement covered by the private ruling has not begun to be carried out, and the income year to which it relates has not yet commenced, this Ruling applies to the taxpayer to the extent of the inconsistency only (see Taxation Determination TD 93/34).

## Withdrawal

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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 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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14. The arrangement that is the subject of this Ruling is described below. The relevant documents or parts of documents incorporated into this description of the arrangement are:

- Application for Product Ruling dated 20 February 2001;
- Draft Prospectus for Brooklyn Park Olive Groves Limited Project No. 2, undated;
- Constitution of Brooklyn Park Olive Groves Limited;
- Scheme Constitution and deed poll of Brooklyn Park Olive Groves Limited dated 8 February 2001;
- Registered Compliance Plan for the Brooklyn Park Olive Groves Managed Investment Scheme;
- **Draft Management Agreement** between Australian Green and Gold Limited (as the Manager) Brooklyn Park Olive Groves Limited and the Grower, undated;
- **Draft Licence to Occupy Agreement** between Brooklyn Park Olive Groves Limited and the Grower, undated;
- Executed Loan Agreement between Brooklyn Park Olive Groves (the borrower) and the Promoters;
- Registered lease between Brooklyn Park Olive Groves Limited and Australian Rural Group Limited;
- Registered Sublease between Australian Rural Group Limited and Brooklyn Park Olive Groves Limited;
- Executed Brooklyn Park Olive Groves **Water and Services Agreement**; and
- Correspondence received from the Applicant dated 5 March 2001, 2 May 2001, 4 May 2001 and 15 May 2001.

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

15. The documents highlighted are those that Growers enter into for the purpose of describing the arrangement to which this Ruling

applies. 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 a party to. The effect of these agreements is summarised as follows.

**Note:** In this Ruling ‘Associate’ has the meaning as defined in section 318 of the ITAA 1936.

### Overview of the Project

16. The arrangement is called the Brooklyn Park Olive Groves Project No. 2

Location	The Darling Downs Region of Queensland
Type of business each participant is carrying on	Commercial growing of olives for domestic and international sale.
Number of hectares under cultivation	150 hectares
Name used to describe the Product	Brooklyn Park Olive Groves Project No. 2.
Size of the licensed area	0.2 hectares
Number of trees per hectare	250
Number of trees per licensed area	50
Expected production	17500 kg per hectare ( 70 kg per tree).
The term of the investment in years	19 years
Initial costs per allotment	\$11,441.12 for the first 12 months, including \$1,000 for acquisition of A shares in Brooklyn Park Olive Groves Limited and \$22 for the Licence Fee.
Initial costs per hectare	\$57,205.60 for first 12 months.
Outgoing costs	Monthly Management fees for months 3 to 48, followed by Management Fees as a set percentage of Gross Harvest Proceeds, and Annual Licence Fees.

17. The arrangement is called the ‘Brooklyn Park Olive Groves Project’ and has been registered as a Managed Investment Scheme under the Corporations Law. In the Prospectus, participants are invited to conduct a business of commercially growing olives for domestic and international sale. The Project is to run for a period ending on 30 June 2020.

18. The business activity contemplated by the Project is the commercial growing, harvesting and selling of plantation olives. The

Project will be situated at Brooklyn Park, a property situated approximately 22km west of Inglewood in the Darling Downs region of southern Queensland. The life of the Project is expected to be nineteen (19) years.

19. Growers will participate in the Project by holding one or more parcels of 1,000 shares in Brooklyn Park Olive Groves Limited, the company which will own the land upon which the grove will be situated.

20. Growers will apply for a minimum parcel of 1,000 \$1 shares per interest in the Project. There is no minimum subscription for the Project however there is a maximum subscription of 750 interests. Once these shares are allotted, Growers will be required to enter into a Licence to Occupy. The shares, coupled with the Licence to Occupy, will entitle each Grower to a separate and distinct area ("an Allotment") of 0.20 hectares upon which the Grower can plant and maintain a grove of 50 olive trees. Each Allotment will be separately identifiable on a plan prepared by the Manager for that purpose.

21. Growers will have the option to enter into a Management Agreement with Australian Green & Gold Limited ("the Manager") whereby the Manager will establish and maintain each grove during the term of the Project.

22. Unless otherwise elected by the Growers, the Manager will harvest the olives and use its best endeavours to sell the produce at the best available price. The Manager markets the olives through Inglewood Olive Processors, the contracted buyers and marketers of the produce. Sales proceeds will be held on account by a custodian, Australian Rural Group Limited ("ARGL"), on behalf of the Growers, and the custodian will make annual distributions to the Growers. In its role as custodian, ARGL acts as agent for the Manager. Brooklyn Park Olive Groves Limited owns the Brooklyn Park Property which is then leased to ARGL which holds this interest as Head Lessee for the security of the Growers. The property is sub-leased back to Brooklyn Park Olive Groves Limited for administration of the Project.

23. In relation to the production forecasts for the olive grove, the expected yield, in kilograms per tree, is outlined in the following table:

<b>Year/s</b>	<b>0-3</b>	<b>4</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>10-19</b>
<b>Yield (KG per tree)</b>	0	10	20	30	40	50	60	70



**Monies Payable**

24. The minimum subscription for an investor is 1,000 shares of \$1 each, with further applications to be made in parcels of 1,000 shares. Each subscription must be accompanied by payment of \$1,022, which covers the purchase price of 1,000 \$1 shares and \$22 which represents the licence fee in relation to access of the Brooklyn Park property in year 1.

25. Growers are required to pay an annual access fee of \$1,000 to Brooklyn Park Olive Groves Limited if they choose to access their allotment and conduct their olive growing business themselves. This access fee will be waived if Growers choose to enter into the Management Agreement with the Manager. This Ruling does not apply to Growers who do not enter into the Management Agreement with the Manager.

26. Growers who choose to enter into the Management Agreement with the Manager are required to pay the amounts outlined below in the first year of the Project. All amounts are inclusive of GST unless otherwise specified.

- \$1,000 (GST exclusive) for the acquisition of 1,000 shares in Brooklyn Park Olive Groves Limited.
- A \$22 Licence fee for the right to occupy an Allotment on the Brooklyn Park property.
- A management fee of \$1,844.70 is payable on the “first invoice date”. The first invoice date is two months after a Grower enters into the Project. This management fee relates to services provided by the Manager from the time of execution of the agreement up until the first invoice date. No amount of the management fee is prepaid provided the Grower does not pay the management fee prior to the first invoice date.
- Further management fees are payable after the first invoice date for Growers who choose to enter into the Management Agreement with the Manager as follows:
  - \$337.08 payable in month 3;
  - \$315.08 payable in month 4;
  - \$315.08 payable in month 5;
  - \$315.08 payable in month 6;
  - \$315.08 payable in month 7;
  - \$315.08 payable in month 8;
  - \$315.08 payable in month 9;

- \$315.08 payable in month 10;
- \$315.08 payable in month 11;
- \$339.90 payable in month 12.

These management fees will relate to services provided by the Manager in the month prior to invoicing. Total Management Fees for a Grower for the first year of participation in the Project will be \$5,042.32 for each Allotment as outlined above.

27. In addition to the above mentioned services provided by the Manager for each Allotment:

- \$412.50 is payable on the first invoice date in relation to the supply and planting of fifty (50) olive trees.
- Land-care establishment costs of \$1,501.50 are payable when invoiced. For those Growers who are accepted into the Project on or before 30 June 2001, the invoice will issue on 30 June 2001. For those Growers accepted into the Project after 30 June 2001 the invoice date will be the earlier of two months after acceptance into the Project or 30 June 2002. These costs cover contouring, soil erosion and protection work. These costs relate to services provided from the execution of the relevant agreements to the first invoice date.
- Irrigation establishment costs of \$3,462.80 are payable when invoiced. For those Growers who are accepted into the Project on or before 30 June 2001, the invoice will issue on 30 June 2001. For those Growers accepted into the Project after 30 June 2001 the invoice date will be the earlier of two months after acceptance into the Project or 30 June 2002. These costs relate to services provided from the execution of the relevant agreements to the first invoice date.

28. Therefore, the amount required to be paid in the first year of participation in the Project by a Grower, who enters into a Management Agreement with the Manager, is \$11,441.12.

### **Managed Investment Scheme requirements**

29. The Project has been registered with ASIC as a Managed Investment Scheme under the Corporations Law. All of the resulting ASIC requirements are, or will be, complied with for the duration of the Project, including the requirements that the Project has a Scheme Constitution, a Responsible Entity and a Compliance Plan.

## **Scheme Constitution**

30. Upon entering into the Management Agreement, Growers become bound by the provisions of the Scheme Constitution. The Constitution primarily sets out the rights, powers, duties and obligations of the Manager. A summary of this document appears at Section 13 of the Prospectus entitled 'Significant Documents'.

## **Responsible Entity**

31. The Manager is the Responsible Entity for the Project and will have the primary responsibility for managing the Project, ensuring compliance with the Corporations Law, the Scheme Constitution and the Management Agreement.

## **Compliance Plan**

32. The Compliance Plan describes how the Responsible Entity will ensure its compliance with the Corporations Law and the Project Scheme Constitution. The Compliance Plan is designed to protect the rights of Growers.

## **Rights of Shareholders in Brooklyn Park Olive Groves**

33. As an investor in the Project, a Grower must subscribe for a minimum of 1,000 A Shares in Brooklyn Park Olive Groves at a cost of \$1 per share, payable on application. The Grower subscribes by completing the 'Application for Shares' form attached to the Prospectus. Upon acceptance of the Grower's Application by the directors of Brooklyn Park Olive Groves, the Grower becomes bound by Brooklyn Park Olive Groves' Constitution.

34. As a holder of A Shares, the Grower also consents to, and agrees to be bound by, the terms and conditions of the Licence to Occupy Agreement. The rights, privileges, conditions and other obligations of A Shareholders are set out in Rule 4.3 of the Constitution of Brooklyn Park Olive Groves and are summarised in Section 13 of the Prospectus entitled 'Significant Documents'.

35. Brooklyn Park Olive Groves also has 250,000 Ordinary Shares on issue to the Promoters at 1 cent each, in consideration of services provided by them and 277,000 A Shares held by Growers in Stage One of the Brooklyn Park Olive Groves, at \$1 each. Ordinary Shares rank equally with A Shares with respect to voting rights, dividends and capital. Ordinary Shares differ from A Shares in that Ordinary Shares do not include any rights to occupy the Project Land. The occupancy rights attached to A Shares, by virtue of the Grower's licence to occupy, cease on 30 June 2020. After this date, holders of

A Shares will rank pari passu with holders of Ordinary Shares. The taxation consequences flowing from the events occurring at that time do not form part of this Ruling.

### **Licence to Occupy Agreement**

36. Each Grower enters into a Licence to Occupy Agreement with Brooklyn Park Olive Groves until 30 June 2020 (clause 2.2). Under the Agreement, Brooklyn Park Olive Groves grants the Grower a licence to occupy an Allotment on the Project Land for the purpose of conducting the 'Business' (clause 6.1). 'Business' is defined as planting, growing, cultivating, harvesting and marketing olives for domestic and overseas sale.

37. Each Allotment is 0.20 hectare in size and will have 50 olive trees planted on it, with row spacings approximately 8 metres by 5 metres (clause 3.2). Each Grower's Allotment will be a distinct area of the Project Land and will be identified on an Allotment Plan to be maintained by Brooklyn Park Olive Groves (clause 3.3). Each tree position will be numbered and shown in relation to the boundaries of the Project Land. This will enable Growers to identify their individual Allotment and tree holding. Brooklyn Park Olive Groves will advise Growers of the location of their individual Allotment(s) (clause 3.3).

38. The Agreement places certain obligations on the Grower to maintain the Allotment (clause 4). It also permits the Grower to use dams, irrigation systems, roads and other infrastructure located on the Project Land (clause 2.3).

39. The Grower is required to pay an annual Licence Fee for each year of the Agreement. The Fee is \$22 per year for the first 4 years (clause 8.1). From the fifth year onwards, the annual Fee will equal the Fee of the preceding year indexed by the All Groups Consumer Price Index for Brisbane ('CPI') in accordance with the formula in clause 7.2.

40. The Grower will pay all telephone, garbage, waste, electric light and power charges levied against the Land or the Allotment in respect of the Grower's use of the Allotment to conduct the Business. Brooklyn Park Olive Groves will pay for all charges and assessments levied on the Allotment, including water and municipal rates (clause 8).

41. The Agreement allows the Grower to delegate the conduct of all or part of the Business to the Manager or an approved contractor (clause 12). As a consequence, the Agreement allows delegates of the Grower to enter upon the Allotment for the purpose of conducting the Grower's Business (clause 10.4).

42. The Agreement may be terminated prior to 30 June 2020, where either party defaults or does not fulfil its obligations (clause 11). Growers are not entitled to assign the licence, except as set out in Brooklyn Park Olive Groves' Constitution (clause 10.1).

43. Upon termination of the Agreement, the Grower must remove any item brought onto the Allotment or any improvement constructed on the Allotment (clause 11.5(a)). Brooklyn Park Olive Groves will be legally entitled to any trees growing on the Allotment and things brought onto the Allotment by the Grower that are not removed within 14 days following termination of the Agreement (clause 11.5(b)).

## **Management Agreement**

44. Growers may elect to use the services of the Manager, Australian Green and Gold Limited, by entering into the Management Agreement. The parties to the Management Agreement are the Grower, the Manager and Brooklyn Park Olive Groves. The Management Agreement will terminate on 30 June 2020, subject to the valid terminations as set out in clause 16.

45. The Manager must carry out its duties under the Agreement in a manner consistent with best agricultural practice. In accordance with the Management Agreement, the Manager will carry out the following duties:

- properly prepare the Allotment, including the performance of soil conservation, irrigation and drainage work on the Land to the benefit of the Allotment;
- cause at least 50 trees to be planted on the Allotment; and
- identify the Grower's trees with appropriate markings.

46. The Manager will also provide additional services to the Grower as set out in clauses 5.2 and 5.3:

- procuring, planting and tending the trees on the Allotment;
- minimising soil erosion and maintaining soil quality on the Grove;
- keeping the Grove free from vermin, vegetation, insects and diseases that might inhibit the growth of the trees;
- maintaining and cultivating the trees, including watering, weeding and applying fertilisers, nutrients and herbicides;

- procuring all necessary plant, equipment, machinery and materials;
- maintaining windbreaks, access roads and tracks; and
- harvesting the trees and marketing and selling the olives produced (subject to the Grower's right to make an election regarding these services).

47. In general, the Manager will carry out the above services at or about the same time in respect of all Growers who have entered into the Management Agreement.

48. The Manager guarantees survival of the Grower's trees to the commencement of the fourth year of the term of the Agreement. Thereafter, the Manager does not guarantee survival of the Grower's trees or that they will produce olives (clause 4.4).

49. Under the Management Agreement, Growers may elect not to use all the services provided by the Manager. Growers may elect to have the Manager harvest the trees on their Allotment separately (clause 6.1) or they may elect to harvest the trees on their Allotment themselves (clause 6.2). Growers may also elect to retain the olives harvested from their Allotment and market, sell or otherwise deal with as they see fit (clause 6.3). Any Grower who makes an election under clauses 6.1, 6.2 and 6.3 will be outside the arrangement to which this Ruling applies and will be unable to rely on this Ruling.

50. The Manager is entitled to delegate all or any of the functions to be performed by it under the Agreement (clause 20).

51. The Manager will pool the olives produced by the Grower's trees with those of each other Grower, and market and sell all such olives (clause 7.1). In the seventh year of the Project, or at the time when the trees reach maturity, olives from Stage One of the Brooklyn Park Olive Groves Project will be pooled with those from the Brooklyn Park Olive Groves Project No. 2. The proceeds of the sale of all olives will be paid to the Custodian, to be divided among all Growers. The allocation of gross sales proceeds to each Grower does not make reference to the quality, volume, prices or any other factor relating to the olives produced by the Grower's Allotment (clause 7.3).

52. The Custodian will establish an account for each Grower, to which the Grower's share of sale proceeds will be credited (clause 7.4). The Manager will account for the gross sale proceeds received and Management Fees payable and must provide each Grower with certain financial information in respect of the Grower's olives (clause 7.5). The Manager is also required to provide the Grower with various reports, including half yearly reports on the Management

Services provided and the progress and condition of the Grove (clause 14).

53. Growers are not entitled to assign their rights or obligations under the Management Agreement, except in certain circumstances. Where a Grower's interest is assigned, the Grower will no longer be entitled to rely on this Ruling.

54. In consideration of services provided, Growers who invest in the Project, will pay the Manager Fees as follows:

- In respect of the first project participation year from the commencement of the Agreement - \$5,042.32. This is comprised of \$1,844.70 payable on the first invoice date. The remaining payments are payable monthly beginning in the month following the first invoice date.
- In respect of the second project participation year from the commencement of the Agreement - \$1978.90; and
- In respect of the third project participation year from the commencement of the Agreement - \$1978.90; and
- In respect of the fourth project participation year from the commencement of the Agreement - \$1,551.04.
- In respect of Year 5 and subsequent years, the Fee will be calculated as a percentage of gross sales proceeds of olives harvested in the immediately preceding financial year in accordance with the following table:

<b>Year</b>	<b>Percentage</b>
5	80%
6	70%
7	60%
8	50%
9-19	40%

55. In order to ensure that the Management Fees are paid by the due date, the fees are to be funded by way of direct payment from each Grower. There is no financing facility offered by the Manager or any other party to the arrangement.

### **Water and Services Agreement**

56. Upon application, the Grower agrees to be bound by a Water and Services Agreement between the owner of the property adjoining the Project Land ('the Supplier'), the Manager and the Growers. The effect of this Agreement will be to supplement the water supply and infrastructure available to the Project. Infrastructure refers to accommodation and administration buildings, machinery service

sheds and storage sheds located on the adjoining property. The Agreement will run from the date of commencement of the Project until 30 June 2020. Under the Agreement the Manager will pay the Supplier the following fees:

- **Water Supply Fees:** for the first 4 years the Fee will be \$100 per megalitre of water supplied. For year 5 the Fee will be \$50,000. For years 6 to 20 the Fee in each year will equal the Fee in the previous year indexed by the CPI, in accordance with the formula in the Agreement; and
- **Infrastructure Fees:** for the first year the Fee will be \$30,000. The Fee for each subsequent year will equal the Fee of the previous year indexed by the CPI, in accordance with the formula in the Agreement.

57. If the Management Agreement is terminated, the Supplier will grant the Growers an option to enter into a Water and Services Agreement with the Supplier.

### **Planting and commercial harvesting**

58. Under the Management Agreement, the Manager undertakes to establish the Business of the Grower, including the planting of trees, as soon as is reasonably practicable. These services will begin to be performed and carried out by the Manager on behalf of the grower immediately after the Grower enters into the relevant agreements. It is anticipated that planting will commence soon after the acceptance of the Grower into the Project. The olive trees are expected to be ready for the first commercial harvesting in 2005.

### **Fee summary**

59. Pursuant to the Management Agreement, the amounts payable per Grove in years 1 to 4, are as follows:

<b>Fee type</b>	<b>First 12 Months</b> \$	<b>Second 12 Months</b> \$	<b>Third 12 Months</b> \$	<b>Fourth 12 Months</b> \$
Acquisition of 1,000 A Shares in Brooklyn Park Olive Groves	1,000.00			
Licence Fee	22.00	22.00	22.00	22.00
Olive Tree Establishment	412.50			



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Irrigation	3,462.80			
Landcare	1,501.50			
Management Fee	5,042.32	1,978.90	1,978.90	1,551.04
Total	11,441.12	2,000.90	2,000.90	1,573.04

The amounts outlined above are inclusive of GST with the exception of the \$1,000 payment for the acquisition of 1000 A shares in Brooklyn Park Olive Groves.

**Finance**

60. Growers can fund their investment in the Project themselves, or borrow from an independent lender.

61. This Ruling does not apply if a Grower enters into a finance agreement that 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; or
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers;
- entities associated with the Project, are involved or become involved, in the provision of finance to Growers for the Project.

## Ruling

### Assessable Income

62. A Grower's share of the gross sales proceeds from the Project, less any GST payable on these proceeds, will be assessable income under section 6-5. Section 17-5 excludes from assessable income an amount relating to GST payable on a taxable supply.

### Section 8-1

#### **Deductions where a Grower is accepted into the Project on or before 30 June 2001 and is not registered nor required to be registered for GST**

63. A Grower may claim tax deductions in the Tables below where the Grower:

- participates in the Project by 30 June 2001 to carry on the business of growing olives;
- incurs the fees shown in paragraph 59; and
- is not registered nor required to be registered for GST.

Fee Type	ITAA 1997 Section	Year ended 30/6/2001 deductions	Year ended 30/6/2002 deductions	Year ended 30/6/2003 deductions
<b>Management Fee</b>	8-1	Nil – See Note (i) (below)	See Note (i) (below)	See Note (i) (below)
<b>Licence Fee (Rent)</b>	8-1	\$22.00 – See Note (i) (below)	\$22.00 – See Note (i) (below)	\$22.00 – See Note (i) (below)
<b>Interest</b>		See Note (ii) (below)	See Note (ii) (below)	See Note (ii) (below)

#### **Notes:**

- (i) **The amount of management fees incurred will depend upon the date the Grower is accepted into the Project.** Where a Grower incurs the management fees and the licence fees as required by the Management Agreement and the Licence to Occupy Agreement those fees are deductible in full in the year incurred. However, if a Grower **chooses** to prepay fees for the doing of things (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, then the prepayments 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 paragraphs 107 to 111 unless the expenditure is 'excluded expenditure'. 'Excluded expenditure', being expenditure of less than \$1,000, is an 'exception' to any prepayment rules that apply and is deductible in full in the year in which it is incurred.

- (ii) The deductibility or otherwise of interest arising from agreements that Growers enter into to finance their participation in the Project is outside the scope of this Ruling. However, all Growers who enter into agreements to finance their participation in the Project should read carefully the discussion of the prepayment rules in paragraph 115 to 117 below as those rules may be applicable if interest is prepaid.

### **Tax deductions for capital expenses**

64. A Grower who participates in the Project will also be entitled to the following tax deductions:

<b>Fee type</b>	<b>ITAA 1997 section</b>	<b>Year ended 30/6/2001 deductions</b>	<b>Year ended 30/6/2002 deductions</b>	<b>Year ended 30/6/2003 deductions</b>
Landcare operations	387-55	\$1,501.50- see Notes (iii) and (v) below		
Irrigation costs	387-125	\$1,154.27- see Notes (iv) and (v) below	\$1,154.27- see Notes (iv) and (v) below	\$1,154.27- see Notes (iv) and (v) below
Establishment of horticultural plants	387-165	Nil - see Note (vi) below	Nil	Nil

#### **Notes:**

- (iii) A deduction is allowable under section 387-55 for capital expenditure incurred for landcare operations. The deduction is allowed in the year that the expenditure is incurred, provided the Grower has commenced a business of primary production at the time the expenditure in question is incurred. A Grower who applies for and is accepted into the Project in the year ended 30 June 2001 but for whom no services are

provided in that income year will not be considered to be carrying on such a business.

- (iv) A deduction is allowable under section 387-125 for capital expenditure incurred for acquisition and installation of the irrigation system. The deduction is calculated on the basis of one third of the capital expenditure in the year in which the expenditure is incurred, and one third in each of the next 2 years of income.
- (v) A tax offset is available to certain low income primary producers under section 388-55 in respect of expenditure incurred on landcare operations and/or facilities to conserve or convey water. This is an alternative to claiming deductions under sections 387-55 and 387-125.
- (vi) A deduction is allowable under section 387-165 for capital expenditure incurred for the acquisition and establishment of the olive trees for use in a horticultural business. The deduction is allowable when the olive trees, as horticultural plants, enter their first commercial season. If the olive trees have an 'effective life' for the purposes of section 387-185 of greater than 30 years', this results in a write-off rate of rate of 7% prime cost. The Project's manager will inform Growers of when the olive trees enter their first commercial season.

### **Deductions where a Grower is registered or is required to be registered for GST**

65. Where a Grower who is registered or is required to be registered for GST:

- participates in the Project by 30 June 2001 to carry on the business of growing olives;
- incurs the fees shown in paragraph 59; and
- is entitled to an input tax credit for the fees

then the tax deductions shown in the Tables above will exclude any amounts of input tax credit (Division 27 of the ITAA 1997). See Example 1 at paragraph 122.

**Deductions where a Grower is accepted into the Project after 30 June 2001 and is not registered nor required to be registered for GST**

66. A Grower may claim tax deductions in the Tables below where the Grower:

- participates in the Project after 30 June 2001 to carry on the business of growing olives;
- incurs the fees shown in paragraph 59; and
- is not registered nor required to be registered for GST.

<b>Fee Type</b>	<b>ITAA 1997 Section</b>	<b>Year ended 30/6/2002 deductions</b>	<b>Year ended 30/6/2003 deductions</b>	<b>Year ended 30/6/2004 deductions</b>
<b>Management Fee</b>	8-1	See Note (i) (above)	See Note (i) (above)	See Note (i) (above)
<b>Licence Fee (Rent)</b>	8-1	\$22.00 – See Note (i) (above)	\$22.00 – See Note (i) (above)	\$22.00 – See Note (i) (above)
<b>Interest</b>		See Note (ii) (above)	See Note (ii) (above)	See Note (ii) (above)

**Tax deductions for capital expenses**

67. A Grower who participates in the Project will also be entitled to the following tax deductions:

<b>Fee type</b>	<b>ITAA 1997 section</b>	<b>Year ended 30/6/2002 deductions</b>	<b>Year ended 30/6/2003 deductions</b>	<b>Year ended 30/6/2004 deductions</b>
Landcare operations	387-55	\$1,501.50- see Notes (iii) and (v) above	Nil	Nil
Irrigation costs	387-125	\$1,154.27- see Notes (iv) and (v) above	\$1,154.27- see Notes (iv) and (v) above	\$1,154.27- see Notes (iv) and (v) above
Establishment of horticultural plants	387-165	Nil - see Note (vi) above	Nil - see Note (vi) above	Nil

**Deductions where a Grower is registered or is required to be registered for GST**

68. Where a Grower who is registered or is required to be registered for GST:

- participates in the Project after 30 June 2001 to carry on the business of growing olives;
- incurs the fees shown in paragraph 59; and
- is entitled to an input tax credit for the fees

then the tax deductions shown in the Tables above will exclude any amounts of input tax credit (Division 27 of the ITAA 1997). See Example 1 at paragraph 122.

**Division 35 – Deferral of losses from non-commercial business activities****Section 35-55 – Commissioner’s discretion**

69. For a Grower who is an individual and who enters the Project during the years ended 30 June 2001 or 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 years ending 30 June 2001 to 30 June 2006 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.

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

- a Grower’s business activity satisfies one of the objective tests in sections 35-30, 35-35, 35-40 or 35-45; or
- the ‘Exception’ in subsection 35-10(4) applies (see paragraph 96 in the Explanations part of this ruling, below).

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

72. Growers are reminded of the important statement made on Page 1 of this Product Ruling. Therefore, Growers should not see the Commissioner’s decision to exercise the discretion in paragraph

35-55(1)(b) as an indication that the Tax Office sanctions or guarantees the Project or the product to be a commercially viable investment. An assessment of the Project or the product from this perspective has not been made.

**Sections 82KZM, 82KZMB – 82KZMD, 82KZME, 82KZMF, 82KL and Part IVA**

73. For a Grower who participates in the Project and incurs expenditure as required by the Management Agreement and the Licence to Occupy Agreement the following provisions of the ITAA 1936 have application as indicated:

- expenditure by the Grower does not fall within the scope of section 82KZM (but see paragraphs 107 to 111);
- expenditure by the Grower does not fall within the scope of sections 82KZMB-82KZMD (but see paragraphs 107 to 111);
- expenditure by the Grower does not fall within the scope of sections 82KZME and 82KZMF (but see paragraphs 107 to 111);
- 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.

## **Explanations**

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### **Section 8-1**

74. Consideration of whether the management fees and the licence fees 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 contractually commits themselves to a venture

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

### **Is the Grower carrying on a business?**

75. An olive growing scheme can constitute the carrying on of a business. Where there is a business, or a future business, the Gross Harvest Proceeds each year from olives from groves comprising the Project will constitute gross assessable income in their own right. The generation of 'business income' from such a business, or future business, provides the backdrop against which to judge whether the outgoings in question have the requisite connection with the operations that more directly gain or produce this income. These operations will be the planting, tending, maintaining and harvesting of the olives each year from the grove. Generally, a Grower will be carrying on a business of olive growing where:

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

76. For this Project Growers have rights under the Licence to Occupy Agreement in the form of a licence over an identifiable area of land consistent with the intention to carry on a business of growing olives. Under the Management Agreement Growers engage the Project Managers to acquire and plant olive trees on the licensed land and to provide ongoing services to care and maintain the olive trees. Growers are considered to have control of their operations.

77. The Licence to Occupy Agreement provides Growers with more than a chattel interest in the olive trees. The Project documentation contemplates Growers will have an ongoing interest in the olive trees.

78. Growers have the right to use the land in question for olive growing purposes and to have the Project Manager come onto the land to carry out its obligations under the Management Agreement. The Growers' degree of control over the Project Manager as evidenced by



the Management Agreement, and supplemented by the Corporations Law, is sufficient. Under the Project, Growers are entitled to receive regular progress reports on the Project Manager's activities. Growers are able to terminate arrangements with the Project Manager in certain instances, such as cases of default or neglect. The olive growing activities described in the Management Agreement are carried out on the Growers' behalf.

79. 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. Growers to whom this Ruling applies intend to derive assessable income from the Project. This intention is related to projections contained in the Prospectus that suggest the Project should return a 'before-tax' profit to the Growers, i.e., a 'profit' in cash terms that does not depend in its calculation, on the fees in question being allowed as a deduction.

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

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

82. The licence fees and management fees associated with the olive growing activities will relate to the gaining of income from this business, and hence have a sufficient connection to the operations by which income (from the regular sale of olives) 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.

### **Expenditure of a capital nature**

83. Any part of the expenditure of a Grower entering into an olive growing business that is attributable to acquiring an asset or advantage of an enduring kind is generally capital or capital in nature and will not be an allowable deduction under section 8-1. In this Project, the costs of, landcare, irrigation and the establishment of the olive trees

are considered to be capital in nature. The fees for these expenditures are not deductible under section 8-1. However, this expenditure falls for consideration under specific write-off provisions of the ITAA 1997.

### **Subdivision 387-A - Expenditure for landcare operations**

84. Section 387-55 allows a taxpayer a deduction for capital expenditure incurred on a landcare operation for land used to carry on a primary production business. Growers need not own the land to qualify for the deduction, so long as it is used by them to carry on a primary production business.

85. 'Landcare operation for land', under subsection 387-60(1), includes the following:

"(b) erecting a fence ...

(i) to prevent or limit extension or worsening of land degradation in the area; and

(ii) to help reclaim the area; or ..."

"(d) constructing surface or subsurface drainage works on the land, if the construction is primarily and principally for the purpose of controlling salinity or assisting in drainage control; or.."

"(f) an extension of an operation described in paragraph (a), (b), (c), (d) or (e)."

Subsection 387-60(2) states: "Paragraph 1(d) does not apply to an operation draining swamp or low-lying land."

86. Under the Management Agreement a Grower incurs expenditure for the construction of surface and subsurface drainage works on the land, the completion of a comprehensive soil survey, as well as pegging and construction of water drainage areas on the olive groves. In this Project there will be no delay between the execution of the relevant agreements and the commencement of 'business operations' on the Grower's behalf. Accordingly, a Grower's primary production business will have commenced at the time the expenditure in question has been incurred, and the requirements of section 387-55 will have been satisfied. However, where all that occurs in an income year, is that a person has been accepted into the Project as a Grower but no business operations have been commenced on his/her behalf, he/she will not be accepted as having commenced a primary production business and no deduction under Subdivision 387-A will be allowable for that, or any other, year of income.

87. A deduction under section 387-55 is also denied where the Grower is entitled to claim a landcare tax offset under section 388-55

and chooses to do so. A Grower can only choose a landcare tax offset where:

- had the Grower chosen a deduction instead of the tax offset, the Grower's taxable income for the income year would have been \$20,000 or less; and
- the expenditure is incurred before the end of the 2000-01 income year.

### **Subdivision 387-B – Irrigation expenditure**

88. Section 387-125 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 deduction is allowed over a three-year period and applies to plant or a structural improvement primarily or principally used for the purpose of conserving or conveying water for use in a primary production business. Irrigation systems of the kind proposed would be covered by this Subdivision.

89. As the taxpayer who can claim the deduction does not have to actually own the land but can be a tenant, a lessee or licensee who is conducting a primary production business on land in Australia, a deduction would be available to a Grower in the Project at a rate of 33.3 per cent per annum for the cost of the irrigation system.

90. However, a deduction under section 387-125 is denied where the Grower is entitled to claim a water facility tax offset under section 388-55 and chooses to do so. A Grower can only choose a water facility tax offset where:

- had the Grower chosen a deduction instead of the tax offset, the Grower's taxable income for the income year would have been \$20,000 or less; and
- the expenditure is incurred before the end of the 2000-01 income year.

### **Subdivision 387-C - Olive trees and horticultural provisions**

91. Section 387-165 allows capital expenditure on establishing horticultural plants owned and used, or held ready for use, in Australia in a business of horticulture to be written off for tax purposes. A lessee or licensee of land carrying on a business of horticulture is taken to own the plants growing on that land rather than the actual owner of the land (section 387-210).

92. Under this Subdivision, if the effective life of the plant is less than three years, the expenditure can be written off in full. If the

effective life of the plant is more than three years, an annual deduction is allowable on a prime cost basis during the plant's maximum write-off period. The period starts from the time the plant enters its first commercial season. The write-off rate is detailed in section 387-185. For a plant, such as the olive trees in this Project, with an effective life of 30 years or more, that rate is 7%.

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

93. 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.

94. 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.

95. 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.

96. 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 Growers who participate in the Project they are beyond the scope of this Product Ruling and are not considered further.

97. 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).

98. A Grower 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 Grower who acquires the minimum investment of one interest in the Project during the years ended 30 June 2001 or 30 June 2002 is unlikely to pass one of the objective tests until the income year ended 30 June 2009. Growers who acquire more than one interest in the Project may however, pass one of the tests in an earlier income year.

99. 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 Grower's participation in the Project.

100. 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, for an individual Grower who acquires an interest(s) in the Project, the Commissioner will decide that it would be unreasonable not to exercise the second arm of the discretion in paragraph 35-55(1)(b) for the years ended 30 June 2001 to 30 June 2006.

101. 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) 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.

102. This Product Ruling is issued on a prospective basis (i.e., before an individual Grower's business activity starts to be carried on). Therefore, if the Project fails to be carried on during the income years specified above (see paragraph 69), in the manner described in the Arrangement (see paragraphs 14 to 61), the Commissioner's discretion will not have been exercised, because one of the key conditions in paragraph 35-55(1)(b) will not have been satisfied.

103. 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 horticulturist and additional expert and scientific evidence provided with the application by the Responsible Entity; and
- independent, objective, and generally available information relating to the olive industry which substantially supports cash flow projections and other claims, including prices and costs, in the Product Ruling application submitted by the Responsible Entity.

**Prepayments provisions – sections 82KZM, 82KZMA – 82KZMD, 82KZME and 82KZMF**

104. The prepayments provisions of the ITAA 1936 operate to spread over more than one income year, a deduction for prepaid expenditure that would otherwise be immediately deductible, in full, under section 8-1. 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 is not wholly done within the same year of income as the year in which the expenditure is incurred.

105. In this Project, the Management Fee of \$1,844.70 per Olive Grove will be incurred two months after the execution of the Management Agreement and further amounts will be incurred monthly thereafter. A Licence Fee of \$22 will be incurred on the execution of the Licence to Occupy Agreement and annually thereafter. The Management Fees are charged for providing management services for the first two month period and for the subsequent monthly periods of the Management Agreement. No explicit conclusion can be drawn from the description of the arrangement that the Management Fees have been inflated to result in reduced fees being payable for subsequent years.

106. Provided a Grower incurs expenditure as required by the agreements as set out in paragraph 59 then the basic precondition for the operation of the prepayment provisions is not satisfied and fees will be deductible in the year in which they are incurred.

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

107. Although not required under either the Management Agreement or the Lease Agreement, a Grower participating in the Project may choose to prepay fees. Where this occurs, contrary to the

conclusion reached in paragraph 106 above, the prepayments provisions of the ITAA 1936 will operate to apportion the expenditure and allow an income tax deduction over the period that the prepaid benefits are provided.

108. The amount and timing of tax deductions for any prepaid Management Fees or prepaid Licence Fees otherwise deductible under section 8-1 will depend upon when the respective amounts are incurred and what the 'eligible service period' is, as defined in subsection 82KZL(1), in relation to these amounts. The 'eligible service period' means generally, the period over which the services are to be provided. The relevant provision of the ITAA 1936 will depend on a number of factors including the amount and timing of the prepayment and, where the 'eligible service period' exceeds 13 months, whether the Grower is a 'small business taxpayer'.

109. Where a Grower participating in this Project incurs expenditure in respect of an eligible service period that ends 13 months or less from the time the expenditure was incurred, but also in respect of the doing of a thing not to be wholly done within the income year in which that expenditure has been incurred, and the other tests in section 82KZME are met, then section 82KZMF will apply in the manner set out in the formula below.

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

In the formula, the 'eligible service period' means, generally, the period to which the services are to be provided.

110. Where a Grower participating in this Project incurs expenditure in respect of a period that ends more than 13 months after that expenditure has been incurred, then section 82KZM will apply if the Grower is a 'small business taxpayer' or section 82KZMD if the Grower is not a 'small business taxpayer'. For a 'small business taxpayer' (see paragraphs 112 to 114) the amount and timing of the allowable deductions will then be calculated using the formula in subsection 82KZM(1) and for non-small business taxpayers using the formula in subsection 82KZMD(2). Both formulae are the same, or effectively the same as that shown in paragraph 109 above, concerning section 82KZMF.

111. A prepaid management fee and/or a prepaid licence fee of less than \$1,000 incurred in an expenditure year is 'excluded expenditure' as defined in subsection 82KZL(1). Subsections 82KZM(1), 82KZME(7) and 82KZMA(4) all provide that 'excluded expenditure' is an exception to the prepayment rules discussed above. Therefore, a prepaid fee of less than \$1,000 is deductible in full in the year in which it is incurred. However, where a Grower acquires more than one interest in the Project and the quantum of a prepaid management fee or a prepaid licence fee is \$1,000 or more, then the amount and

timing of the deduction allowable must be determined using the formula shown above.

### **Subdivision 960-Q - Small business taxpayers**

112. 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.

113. '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).

114. Whether a Grower is a 'small business taxpayer' depends upon the circumstances of each Grower and is beyond the scope of this Product Ruling. It is the responsibility of each Grower to determine whether or not they are within the definition of a 'small business taxpayer'.

### **Interest deductibility**

115. The deductibility of interest incurred by Growers who finance their participation in the Project through a loan facility with a bank or other financier 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.

116. While the terms of any finance agreement entered into between relevant Growers and such financiers are subject to commercial negotiation, those agreements may require interest to be prepaid. Under the prepayment rules contained in sections 82KZME, 'agreement' (defined in subsection 82KZME(4)) is a broad concept and includes all activities that relate to the agreement including those that give rise to deductions or assessable income. It will encompass activities not described in the Arrangement or otherwise dealt with in the Product Ruling, such as a loan to finance participation in the Project.

117. Therefore, unless the prepaid interest is 'excluded expenditure', where such a loan facility requires interest to be prepaid and the requirements of section 82KZME are met, relevant Growers will be required to use the formula in subsection 82KZMF(1) to determine any tax deduction that may be allowable. Where a prepayment is for more than 13 months, any tax deduction that may be allowable must be determined under section 82KZM (for a 'small business taxpayer') or section 82KZMD (for a taxpayer who is not a



‘small business taxpayer’). The relevant formula is the same, or effectively the same as that shown above in paragraph 109.

### **Section 82KL - recouped expenditure**

118. 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**

119. 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).

120. The Brooklyn Park Olive Groves Project No 2 will be a ‘scheme’. A Grower will obtain a ‘tax benefit’ from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 63, 64, 66 and 67 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.

121. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the olives. There are no facts 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 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.

## **Examples**

### **Example 1 – Entitlement to ‘input tax credit’**

122. Margaret, who is registered for GST, invests in the Green Circle Bluegums Project. The management fees are payable on 1 July each year for management services to be provided over the following 12 months. On 1 July 2000 Margaret pays her first year’s management fees of \$5,500 and is eligible to claim a tax deduction for the fees in the income year ended 30 June 2001. The extent of her

deduction for the management fees however, is reduced by the amount of any 'input tax credit' to which she is entitled. The Project Manager provides Margaret with a 'tax invoice' showing its ABN and the 'price of the taxable supply' for management services as \$5,500. Using the details shown on the valid tax invoice, Margaret calculates her input tax credit as:

$$1/11 \times \$5,500 = \$500$$

Therefore, the tax deduction for management fees that she can claim in her income tax return for the year ended 30 June 2001 is \$5,000 (\$5,500 *less* \$500).

## **Detailed contents list**

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23 May 2001

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<i>Previous draft:</i>	- ITAA 1997 35-10
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	- ITAA 1997 35-10(3)
<i>Related Rulings/Determinations:</i>	- ITAA 1997 35-10(4)
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<i>Subject references:</i>	- ITAA 1997 35-55
- carrying on a business	- ITAA 1997 35-55(1)
- commencement of business	- ITAA 1997 35-55(1)(a)
- crops as trading stock	- ITAA 1997 35-55(1)(b)
- fee expenses	- ITAA 1997 Div 35
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