PR 2002/64 - Income tax: WRF Kangaroo Island Plantations 2002 - Second Prospectus

Product Ruling
Income tax: WRF Kangaroo Island Plantations 2002 – Second Prospectus

Contents Para

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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.*

No guarantee of commercial success

The Australian Taxation Office (ATO) **does not** sanction or guarantee this product. 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 participants 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 this product fits an existing portfolio, etc. We recommend a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential participants 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, participants lose the protection of this Product Ruling. Potential participants may wish to seek assurances from the promoter that the arrangement will be carried out as described in this Product Ruling.

Potential participants 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

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax laws' identified below apply to the defined class of persons who take part in the arrangement to which this Ruling refers. In this Ruling this arrangement is sometimes referred to as the 'WRF Kangaroo Island Plantations 2002 - Second Prospectus' or simply as 'the Project'.

Tax law(s)

2. The tax laws 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);
- 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);
- Section 82KZMG (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.

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 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 '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 arrangement described in the Ruling is materially different from the arrangement that is actually carried out, the Ruling has no binding effect on the Commissioner. 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,

Date of effect

11. This Ruling applies prospectively from 15 May 2002, 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 2005. 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.

Arrangement

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

- Application for Product Ruling dated 19 April 2002;
- The WRF Kangaroo Island Plantations 2002 Second Prospectus dated 22 April 2002;
- **Draft Management Agreement between WRF Management Ltd (the 'Manager'), Primary**

Securities Ltd (the 'Responsible Entity') and the Grower undated;

- **Draft Lease and Sub-Lease Agreement between KI Plantations Ltd (the 'Lessor'), Primary Securities Ltd (the 'Responsible Entity') and the Grower, undated;**
- Draft Constitution for WRF Kangaroo Island Plantations 2002, undated;
- Draft Compliance Plan for WRF Kangaroo Island Plantations 2002 dated 28 November 2000;
- Draft Custodian Agreement dated 8 February 2000;
- Responsible Entity Services Agreement between WRF Management Ltd and Primary Securities Ltd, undated; and
- Additional correspondence from the Applicant dated 22 February 2001, 16 May 2001, 22 August 2001, 8 April 2002, 11 April 2002, 23 April 2002 and 24 April 2002.

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

15. The documents highlighted are those that the Growers enter into. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or an associate of the Grower will be a party to that are part of the arrangement to which this Ruling applies.

16. All Australian Securities and Investments Commission (ASIC) requirements are, or will be, complied with for the term of the agreements.

Overview

17. This arrangement is called WRF Kangaroo Island Plantations 2002 – Second Prospectus.

Location	Kangaroo Island in South Australia.
Type of business each participant is carrying on	Commercial growing, and cultivation of *Eucalyptus globulus* (Tasmanian Blue Gums) trees for the purpose of producing timber for woodchipping.
Number of hectares under	2,773 hectares

cultivation	
Size of each leasehold area	1 hectare
Number of trees per hectare	Approximately 1,000
The term of the Project	8-12 years
Initial cost per Woodlot	$6,710 per Woodlot plus $1,358.40 if shares are purchased in KI Plantations Ltd.
Initial cost per hectare	$6,710 or $8,068.40 if shares in KI Plantations Ltd are purchased.
Ongoing costs	Insurance (optional)

18. Growers participating in the arrangement will enter into a Management Agreement and a Lease and Sub-Lease Agreement for the Project. The Lease and Sub-Lease Agreement gives a Grower a lease or sub-lease from KI Plantations Ltd (the 'Lessor') over an identifiable area of land called a 'Woodlot' until 30 June 2013 or up until the trees are harvested and sold and net income distributed, which ever happens last. Each Woodlot is one hectare in size.

19. The Project Land is situated on Kangaroo Island in South Australia. KI Plantations Ltd will either lease or sub-lease land to the Growers to enable the Growers to carry on a long term commercial afforestation business. Growers are specifically granted rights to harvest timber on their Woodlots for this purpose.

20. The Prospectus states that there is no minimum subscription for this Project, however applications made under the Prospectus will not be accepted after 30 June 2002. Each Grower may subscribe for a minimum of one Woodlot, at a cost of $6,710 per Woodlot. For Growers who participate in this Project, an average of 1,000 trees will be planted per Woodlot (1,000 trees per hectare) within 12 months of allotment or by 29 June 2003 whichever is the earlier.

21. Growers may subscribe for 1,350 non-voting shares in KI Plantations Ltd (the 'Lessor') at a cost of $1,350 ($1 per share) plus stamp duty ($8.40). Growers will also receive 300 share options in WRF Securities Ltd (the parent company) per Woodlot. Each option entitles the holder to one fully paid share at an exercise price of $0.35 cents per share. The options are exercisable up until 30 June 2002.

Constitution

22. The Constitution for the Project sets out the terms and conditions under which the Responsible Entity agrees to act for the Grower and to manage the Project. Under the Constitution, Growers appoint Primary Securities Ltd as a sole and exclusive agent in relation to the Project. The Lease and Sub-Lease Agreement and Management Agreement will be executed on behalf of a Grower following them signing the Application Form in the Prospectus. Growers are bound by the Constitution by virtue of their participation in the Project.

Compliance Plan

23. The Responsible Entity has prepared a Compliance Plan in accordance with the *Corporations Act 2001*. Under the Compliance Plan, a Compliance Committee will monitor to what extent the Responsible Entity meets its obligations as the Responsible Entity of the Project and the rights of the Growers are protected.

Interest in Land

24. Growers participating in the arrangement will enter into a Lease and Sub-Lease Agreement between KI Plantations Ltd (the 'Lessor') and the Grower. Growers are granted an interest in land in the form of a lease or sub-lease to use their Woodlot for the purpose of conducting their afforestation business (cl 2.1). The term of a Grower's lease or sub-lease is until 30 June 2013.

25. Rent for years 1 to 10 of the Project is payable in advance at the time of application and will be placed in a trust bank account. The Responsible Entity will direct the Custodian to pay the yearly rent amount, which the Grower is liable to pay under the Lease and Sub-Lease Agreement, to the Lessor. Rent of $5.50 for the period from allotment until 30 June 2002 is payable on allotment under the Lease and Sub-lease Agreement. For each year thereafter each Grower must pay a fee for rent to the Lessor of an amount equal to $36.30 per Woodlot, payable in advance on 30 June of the preceding year (Part 5.4, Schedule to the Lease and Sub-Lease Agreement). This fee is indexed annually.

Management Agreement

26. Each Grower enters into a Management Agreement with WRF Management Ltd (the 'Manager') for each Woodlot. Growers contract with the Manager to establish and maintain the plantation until maturity.

27. Management fees for Years 1 to Year 10 of the Project are payable in advance at the time of application (cl 4 of the Constitution). The Responsible Entity will direct the Custodian to pay the management fees, which the Grower is liable to pay under the Management Agreement, to the Manager. The management fees include an amount of $4,339.50 which is payable on allotment to the Manager for landcare expenses and planting costs of $165 which is payable on 30 June 2002. Each Grower must pay to the Manager a management fee of $682 for the period from 1 July 2002 to 30 June 2003, payable in advance on 30 June 2002. A management fee of $148.50 is payable for the period 1 July 2003 to 30 June 2004 and for each year thereafter to be indexed annually from 1 July 2003 (Part 2(d) and 2(e), Schedule to the Management Agreement). These annual management fees are payable in advance on 30 June of the preceding year.

28. The services to be performed by the Manager in respect of the landcare expense and planting cost are:

- prepare and grade the Woodlots for the planting of the Trees (including the application of pesticides and fertilisers where necessary);
- select on behalf of the Grower trees, to the best of the Managers knowledge, are high yielding Eucalyptus globulus tree; and
- plant *Eucalyptus globulus* seedlings on the Woodlots.

29. The Manager will perform the following ongoing services under the Agreement :

- manage, maintain and cultivate the Woodlots, including growing, watering, weeding, pruning, selecting, procuring, and applying appropriate fertilisers, nutrients and herbicides and doing all other things necessary for the purpose of maintaining and cultivating the Woodlots in accordance with good and proper silvicultural practices;
- procure the use of all necessary plant, equipment, machinery, goods and materials for the purposes of performing the management services including suitable irrigation, fencing, drainage and shelter the trees and any other necessary fixtures required for the purposes of performing the management services;
- keep each Woodlot free of competitive weeds, vermin, noxious animals and insects;
- maintain the Woodlot according to good silvicultural and forestry practices; and

- harvest, remove, mill, market and sell the trees on behalf of the Grower (unless the Grower has elected to sell their own timber).

Planting

30. The Manager will plant out on the Woodlots an average of no less than one thousand trees per Woodlot within 12 months from the commencement date or 29 June 2003, whichever is the earlier. After the planting has been completed, the Manager will maintain the trees in accordance with good silvicultural practice. The services to be provided by the Manager over the term of the Project is outlined in the Management Agreement (Part 3, Schedule to the Management Agreement).

Fees

31. For Growers who participate in the Project, the following fees (per Woodlot) are payable on application;

Expense	**Cost per Woodlot**
Landcare expenses	$4,339.50
Planting Fee	$ 165.00
Management Fees (relating to Years 1 – 10)	$1,787.50
Rent (relating to Years 1 – 10)	$ 418.00
Total	**$6,710.00**

32. The Application monies will be banked in the Application Fund trust bank account formed under the Project's Constitution (cl 3.7 of the Constitution). The Responsible Entity will direct the Custodian to pay the management fees and rent yearly from the trust bank account, after the Manager has given an estimate of the fees required for the following 12 months (cl 12 of the Constitution). If, for any reason, the Project is terminated prior to completion, the Responsible Entity shall refund the balance of the Project Fees to each Grower, including interest accrued, which have been paid in advance, after deducting any amounts due and payable by the Grower. This refund will occur on 30 June following the date of termination (cl 10.6 of the Constitution).

33. An amount of $4,339.50 is payable on allotment to the Manager for landcare expenses. The services in respect of this fee

will be performed within 12 months of the Commencement Date or by 29 June 2003, whichever is earlier.

34. A fee of $165 in relation to planting costs is payable on 30 June 2002 for planting services to be carried out within 12 months from the Commencement Date or 29 June 2003, whichever is the earlier.

35. Each Grower must pay to the Manager a management fee of $682 for period 1 July 2002 to 30 June 2003, and $148.50 for every year thereafter to be indexed annually from 1 July 2003 (Part 2(d) and 2(e), Schedule to the Management Agreement). The management fee of $682 for the period 1 July 2002 to 30 June 2003 is payable in advance on 30 June 2002. Annual management fees for subsequent years are payable in advance on 30 June of the preceding year.

36. Rent of $5.50 for the period from allotment until 30 June 2002 is payable on allotment. For each year thereafter, each Grower must pay a fee for rent to the Lessor of an amount equal to $36.30 per Woodlot (Part 5.4, Schedule to the Lease and Sub-Lease Agreement). This fee is indexed annually. Rent for subsequent years is payable in advance on 30 June of the preceding year.

37. Before harvest, the Grower must pay to the Manager a harvest fee, equal to the amount stated on the Harvesting quote. The Harvesting quote will be provided to the Grower 3 months prior to harvesting taking place. After harvest, Growers must pay the Manager a Co-ordination fee of 5.5% of the Net Sale Proceeds (cl 4.1 of the Management Agreement). These amounts will be withheld by the Responsible Entity from the Growers' Gross Sale Proceeds before the Harvest proceeds are paid out to the Growers.

Finance

38. All Growers are required to fund their involvement in the Project themselves or borrow from an independent lender.

39. This Ruling does not apply if the finance arrangement entered into by the Grower 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 are involved or become involved in the provision of finance to Growers for the Project.

Ruling

Application of this Ruling

40. This Ruling applies only to Growers who are accepted to participate in the Project on or before 30 June 2002 and who have executed Lease and Sub-Lease and Management Agreements before that date. The Grower's participation in the Project must constitute the carrying on of a business of primary production. A Grower is not eligible to claim any tax deductions until the Grower's application to enter the Project is accepted and the Project has commenced. This Ruling does not apply to those Growers who make an election under the Management Agreement to take delivery of and market the timber produced from their Woodlot(s).

The Simplified Tax System ('STS')

Division 328

41. For a Grower 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 Grower is an 'STS taxpayer'. To be an 'STS taxpayer' a Grower:

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

Qualification

42. This Product Ruling assumes that a Grower who is an 'STS taxpayer' is so for the income year in which their participation in the Project commences. A Grower may become an 'STS taxpayer' at a later point in time. Also, a Grower 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 Growers that cannot be accommodated in this Ruling. Such Growers can ask for a private ruling on how the taxation legislation applies to them.

Prepaid expenditure for Management Fees and Lease Fees

Sections 82KZME and 82KZMF

43. The following expenditure incurred by a Grower who is accepted into this Project is subject to the prepayment rules in sections 82KZME and 82KZMF:

- $1,787.50 being the annual Management Fees for Year 2 to the end of the Term; and
- $418 being the annual rent for the term of the Project.

44. In this context, a prepayment refers to advance expenditure incurred by a Grower in return for the doing of a thing that will not be wholly done in the year in which the expenditure is incurred. Other than expenditure deductible under section 82KZMG, where a Grower prepays expenditure that would otherwise be a general deduction under section 8-1 of the ITAA 1997 in the expenditure year, the Grower must apportion the prepayment over the period the prepayment covers unless it is 'excluded expenditure' (see Note (iii) below).

45. Subsection 82KZMF(1) provides the formula for determining how much of the prepaid expenditure a Grower can deduct for each income year. In that formula, which is shown below, the 'eligible service period' 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.

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

46. Sections 82KZME and 82KZMF are discussed in greater detail below at paragraphs 80 to 86.

Prepaid expenditure for 'seasonally dependent agronomic activities'

Section 82KZMG

47. Where certain advance expenditure, and the agreement under which that expenditure is incurred, meets the requirements of section 82KZMG, the formula in subsection 82KZMF(1) will not operate to determine the timing of the deduction allowable. The requirements of section 82KZMG are set out below in paragraphs 88 to 92.

48. Among other things, expenditure that complies with section 82KZMG must be for 'seasonally dependent agronomic activities' that are carried out by the manager during the Project's 'establishment period'. The 'eligible service period' relating to this expenditure must be 12 months or shorter and must end on or before the last day of the year of income after the expenditure year.

49. Under the Management Agreement, for each Woodlot, a Grower incurs $4,339.50 for landcare expenses and $165 for planting costs which are 'seasonally dependent agronomic activities'. This expenditure is deductible in the income year that the Grower incurs this amount.

Tax outcomes for Growers who are not 'STS taxpayers'

Assessable Income

Section 6-5

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

51. The Grower recognises ordinary income from carrying on the business of afforestation at the time that income is derived.

Deductions for Management Fees, Rent, Landcare Expenses and Planting Costs

Section 8-1

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

Fee Type	**ITAA 1997 Section**	**Year 1 Year ended 30/6/2002**	**Year2 Year ended 30/6/2003**	**Year3 Year ended 30/6/2004**	**Year 4 Year ended 30/6/2005**
Landcare Expenses	8-1	$4,339.50 – See Notes (i) & (ii) (below)			
Planting Costs	8-1	$165 – See Notes (i) & (ii) (below)			
Management Fees	8-1	Amount must be calculated – See Notes (i) & (iii) (below)	Amount must be calculated – See Notes (i) & (iii) (below)	Amount must be calculated – See Notes (i) & (iii) (below)	Amount must be calculated – See Notes (i) & (iii) (below)
Year 1 Rent	8-1	$5.50 – See Note (i) (below)			
Rent (ongoing)	8-1	Amount must be calculated – See Notes (i) & (iii) (below)	Amount must be calculated – See Notes (i) & (iii) (below)	Amount must be calculated – See Notes (i) & (iii) (below)	Amount must be calculated – See Notes (i) & (iii) (below)

Notes:

(i) If the Grower 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): Division 27. See Example 1 at paragraph 113.

(ii) Expenditure for 'seasonally dependent agronomic activities' is deductible in the income year in which it is incurred.

(iii) Although the Management Agreement and the Lease and Sub-Lease Agreement, respectively, require the second and subsequent year's management fees and the second and subsequent years rent to be prepaid, for a Grower who acquires the minimum allocation of one interest, the amount of those prepaid Management Fees and the prepaid rent is less than $1,000. For the purposes of this Project, an amount of less than $1,000 is 'excluded expenditure'. 'Excluded expenditure' is an 'exception' to the prepayment rules and, for a Grower who is not an 'STS taxpayer', is deductible in full in the year in which it is incurred (see Example 2 at paragraph 114). However, where a Grower acquires more than the minimum allocation in the Project, the amount of either or both of these prepaid fees may be $1,000 or more. Where this occurs, such Grower **MUST** determine the relevant deduction for the prepaid second and subsequent year management fees and the second and subsequent year prepaid rent, using the formula shown above in paragraph 45.

Tax outcomes for Growers who are 'STS taxpayers'

Assessable Income

Section 6-5 and section 328-105

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

54. The Grower recognises ordinary income from carrying on the business of afforestation at the time the income is received (paragraph 328-105(1)(a)).

Deductions for Management Fees, Rent, Landcare Expenses and Planting Costs

Section 8-1 and section 328-105

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

Fee Type	ITAA 1997 Section	Year 1 Year ended 30/6/2002	Year2 Year ended 30/6/2003	Year3 Year ended 30/6/2004	Year 4 Year ended 30/6/2005
Landcare Expenses	8-1	$4,339.50 – See Notes (iv), (v) & (vi) (below)			
Planting Costs	8-1	$165 – See Notes (iv), (v) & (vi) (below)			
Management Fees	8-1	Amount must be calculated – See Notes (iv), (v) & (vii) (below)	Amount must be calculated – See Notes (iv), (v) & (vii) (below)	Amount must be calculated – See Notes (iv), (v) & (vii) (below)	Amount must be calculated – See Notes (iv), (v) & (vii) (below)
Year 1 Rent	8-1	$5.50 – See Notes (iv) & (v) (below)			
Rent (ongoing)	8-1	Amount must be calculated – See Notes (iv), (v) & (vii) (below)	Amount must be calculated – See Notes (iv), (v) & (vii) (below)	Amount must be calculated – See Notes (iv), (v) & (vii) (below)	Amount must be calculated – See Notes (iv), (v) & (vii) (below)

Notes:

(iv) If the Grower 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): Division 27. See Example 1 at paragraph 113.

(v) 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 Grower 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 Grower. 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.

(vi) Expenditure for 'seasonally dependent agronomic activities' is deductible in the income year in which it is incurred.

(vii) Although the Management Agreement and the Lease and Sub-Lease Agreement, respectively, require the second and subsequent year's Management Fees and the second and subsequent years rent to be prepaid, for a Grower who acquires the minimum allocation of one interest, the amount of those prepaid Management Fees and the prepaid rent is less than $1,000. For the purposes of this Project, an amount of less than $1,000 is 'excluded expenditure'. 'Excluded expenditure' is an 'exception' to the prepayment rules and, for a Grower who is not an 'STS taxpayer', is deductible in full in the year in which it is incurred (see Example 2 at paragraph 114). However, where a Grower acquires more than the minimum allocation in the Project, the amount of either or both of these prepaid fees may be $1,000 or more. Where this occurs, such Grower **MUST** determine the relevant deduction for the prepaid second and subsequent year management fees and the second and subsequent year prepaid rent, using the formula shown above in paragraph 45.

Tax outcomes that apply to all Growers

Interest

56. The deductibility or otherwise 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. However all Growers who borrow funds in order to participate in the Project, should read the discussion of the prepayment rules in paragraphs 80 to 86 (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 Grower's choice.

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

Section 35-55 – Commissioner's discretion

57. For a Grower 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 years ending 30 June 2002 to 30 June 2012 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.

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

- the 'exception' in subsection 35-10(4) applies (see paragraph 101 in the Explanations part of this ruling, below);
- a Grower's business activity satisfies one of the tests in sections 35-30, 35-35, 35-40 or 35-45; or
- the Grower's business activity produces assessable income for an income year greater than the deductions attributable to it for that year (apart from the operation of subsection 35-10(2)).

59. Where, the exception in subsection 35-10(4) applies, the Grower's business activity satisfies one of the tests, or the discretion in subsection 35-55(1) is exercised, 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.

60. 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 commercially viable. An assessment of the Project or the product from this perspective has not been made.

Section 82KL and Part IVA

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

- 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

Is the Grower carrying on a business?

62. For the amounts set out in the Tables above to constitute allowable deductions the Grower's afforestation activities as a participant in WRF Kangaroo Island Plantations 2002 – Second Prospectus must amount to the carrying on of a business of primary production.

63. Where there is a business, or a future business, the gross proceeds from the sale of the wood produce 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.

64. For schemes such as that of WRF Kangaroo Island Plantations 2002 – Second Prospectus, Taxation Ruling TR 2000/8 sets out in paragraph 89 the circumstances in which the Grower's activities can constitute the carrying on of a business. As Taxation Ruling TR 2000/8 sets out, these circumstances have been established in court decisions such as *FCT v. Lau* 84 ATC 4929.

65. Generally, a Grower will be carrying on a business of afforestation, and hence primary production, if:

- the Grower has an identifiable interest (by lease or by licence) in the land on which the Grower's trees are established;
- the Grower has a right to harvest and sell the timber produce from those trees;
- the afforestation activities are carried out on the Grower's behalf;
- the afforestation activities of the Grower are typical of those associated with a afforestation business; and
- the weight and influence of general indicators point to the carrying on of a business.

66. In this Project, each Grower enters into a Sub-Lease and Lease Agreement and a Management Agreement.

67. Under the Sub-Lease and Lease Agreement each individual Grower will have rights over a specific and identifiable area of 1 hectare of land. The Sub-Lease and Lease Agreement provides the Grower with an ongoing interest in the specific trees on the Woodlot(s). Under the lease or sub-lease the Grower must use the land in question for the purpose of carrying out afforestation activities, and

for no other purpose. The lease or sub-lease allows the Manager to come onto the land to carry out its obligations under the Management Agreement.

68. Under the Management Agreement the Manager is engaged by the Grower to establish and maintain a Woodlot on the Grower's identifiable area of land during the term of the Project. The Manager has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the Woodlot on the Grower's behalf.

69. The Manager is also engaged to harvest and sell, on the Grower's behalf, the timber produce grown on the Grower's Woodlot unless the Grower is a Non-Participating Grower under the Management Agreement.

70. 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 Project's description for all the indicators.

71. The activities that will be regularly carried out during the term of the Project demonstrate a significant commercial purpose. Based on reasonable projections, a Grower in the Project will derive assessable income from the sale of the timber produce 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.

72. The pooling of timber produce from trees grown on the Grower's Woodlot with the timber produce of other Growers is consistent with general afforestation practices. Each Grower's proportionate share of the sale proceeds of the pooled timber produce will reflect the proportion of the trees contributed from their Woodlot.

73. The Manager's services are also consistent with general silvicultural practices. They are of the type ordinarily found in afforestation ventures that would commonly be said to be businesses. While the size of a Woodlot is relatively small, it is of a size and scale to allow it to be commercially viable. (see Taxation Ruling IT 360)

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

75. The afforestation activities, and hence the fees associated with their procurement, are consistent with an intention to commence regular activities that have an 'air of permanence' about them. For the purposes of this Ruling, the Growers' afforestation activities in WRF

Kangaroo Island Plantations 2002 – Second Prospectus will constitute the carrying on of a business.

The Simplified Tax System

Division 328

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

77. The question of whether a Grower 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 the Landcare Expenses, Planting Costs, Management Fees and Rent

Section 8-1

78. Consideration of whether the landcare expenses and planting costs 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.

79. The landcare expenses, planting costs, management fees and rent associated with the afforestation activities will relate to the gaining of income from the Grower's business of afforestation (see above), and hence have a sufficient connection to the operations by which income (from the harvesting and sale of timber produce) 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 fees is identifiable from the arrangement. The fees appear to be reasonable. There is no capital component of the landcare expenses. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

Prepayment provisions

Sections 82KZL to 82KZMF

80. The prepayment 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.

81. 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(1). 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

82. 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)).

83. 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;

- 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.

84. 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 Grower in this Project who, in order to participate in the Project may borrow funds from a financier. 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 Grower prepays interest under such financing arrangements, the deductions allowable will be subject to apportionment under section 82KZMF.

85. There are a number of exceptions to these rules, but for Growers 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 Growers in this Project, 'excluded expenditure' is prepaid expenditure incurred under the arrangement that is less than $1,000. Such expenditure is immediately deductible.

86. 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.

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

87. 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.

Section 82KZMG

88. Under section 82KZMG(1), expenditure is excluded from the prepayment rules that would otherwise apply, to the extent that the prepaid amount satisfies the requirements of subsections 82KZMG(2) to (4).

89. Subsection 82KZMG(2) requires that the expenditure is:

- incurred on or after 2 October 2001 and on or before 30 June 2006;
- the eligible service period must be 12 months or shorter and must end on or before the last day of the year of income after the expenditure year; and
- for the doing of a thing under the agreement that is not to be wholly done within the expenditure year.

90. To satisfy subsection 82KZMG(3) the agreement must satisfy the following requirements:

- it must be an agreement for planting and tending trees for felling;
- be an agreement where the taxpayer does not have day to day control over the operations arising out of the agreement. (A right to be consulted or to give directions does not equate to day to day control for the purposes of this requirement); and
- either:
  - (i) there must be more than one participant in the agreement in the same capacity as the taxpayer who incurs the expenditure; or
  - (ii) the manager manages, arranges or promotes the agreement, or an associate of the manager, manages, arranges or promotes similar agreements.

91. Under subsection 82KZMG(4) the expenditure incurred by the taxpayer must be paid for seasonally dependent agronomic activities undertaken by the manager during the 'establishment period' for the relevant planting of trees for felling.

92. Subsection 82KZMG(5) defines the 'establishment period' to commence at the time that the first seasonally dependent agronomic activity is performed in relation to a specific planting of trees and to conclude with the planting of trees. Where it is necessary to apply a fertiliser or herbicide to the trees at the same time as planting then those activities fall within the establishment period. Planting of trees refers to the main planting of the particular plantation and expressly

excludes specific planting to replace existing seedlings that have not survived.

Application of the prepayment provisions to this Project

93. Under the Management Agreement, a Grower incurs landcare expenses of $4,339.50 and planting costs of $165 consisting of expenditure of $4,504.50 for 'seasonally dependent agronomic activities'. As the requirements of section 82KZMG have been met, a deduction is allowable in the income year ended 30 June 2002 for the expenditure incurred under the Management Agreement for 'seasonally dependent agronomic activities'.

94. The Management Agreement also requires that a Grower incurs management fees of $682 in Year 1 and $148.50 per year during Years 2 to 11 for the performance of maintenance services during the term of the Project. Under the Lease and Sub-Lease Agreement a Grower incurs rent of $418 to lease land during the term of the Project.

95. This expenditure incurred under the Management Agreement and the Lease and Sub-Lease Agreement meets the requirements of subsections 82KZME(1) and (2) and is incurred under an 'agreement' as described in subsection 82KZME(3). Therefore, unless one of the exceptions to section 82KZME applies, the amount and timing of tax deductions for those fees are determined under section 82KZMF.

96. The prepaid Years 2 to 11 management fee and the prepaid rent, being amounts of less than $1,000 in each expenditure year, constitute 'excluded expenditure' as defined in subsection 82KZL(1). Under Exception 3 (subsection 82KZME(7)) 'excluded expenditure' is specifically excluded from the operation of section 82KZMF. A Grower who is an 'STS taxpayer' can, therefore, claim an immediate deduction for each of the relevant fees in the income year in which the fee is paid. A Grower who is not an 'STS taxpayer' can claim an immediate deduction for each of the relevant fees in the income year in which the fee is incurred.

97. However, where a Grower acquires more than the minimum investment of one interest in the Project and the quantum of the prepaid Year 2 to 11 management fee and/or the prepaid rent is $1,000 or more, the deduction allowable for those amounts will instead be subject to apportionment according to the formula in subsection 82KZMF(1).

Deferral of losses from non-commercial business activities

Division 35

98. Division 35 applies to losses from certain business activities for the income year ended 30 June 2001 and subsequent years. Under the rule in subsection 35-10(2) a deduction for a loss made by an individual from certain business activities will not be taken into account in an income year unless:

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

99. 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.

100. Losses that cannot be taken into account in a particular year of income, because of subsection 35-10(2), can be applied to the extent of future profits from the business activity, or are deferred until one of the tests is passed, the discretion is exercised, or the exception applies.

101. For the purposes of applying Division 35, 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.

102. In broad terms, the 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, or an interest in real property, (excluding any private dwelling) 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 (excluding cars, motor cycles and similar vehicles) are used on a continuing basis in carrying on the business activity in that year (section 35-45).

103. 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 allocation of one Woodlot in the Project is unlikely to ever pass one of the tests.

104. Therefore, 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.

105. 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;

(ii) because of its nature, it has not yet met one of the tests set out in Division 35; and

(iii) there is an expectation that the business activity of an individual taxpayer will either pass one of the tests or produce a taxation profit within a period that is commercially viable for the industry concerned.

106. Information provided with this Product Ruling indicates that a Grower who acquires the minimum investment of one Woodlot in the Project is expected to be carrying on a business activity that will either pass one of the tests, or produce a taxation profit, for the year ended 30 June 2013. The Commissioner will decide for such a Grower that it would be reasonable to exercise the second arm of the discretion until the year ended 30 June 2012.

107. This Product Ruling is issued on a prospective basis (i.e., before an individual Grower'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 106), in the manner described in the Arrangement (see paragraphs 14 to 39). 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). Growers may need to apply for private rulings on how paragraph 35-55(1)(b) will apply in such changed circumstances.

108. 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 forester and additional expert or scientific evidence provided with the application by the Manager; and
- independent, objective, and generally available information relating to the afforestation industry which substantially supports cash flow projections and other claims, including prices and costs, in the Product Ruling application submitted by the Manager.

Section 82KL - recouped expenditure

109. 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

110. 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).

111. WRF Kangaroo Island Plantations 2002 – Second Prospectus 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 52 and 55 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.

112. 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 wood produce. 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 at arm's length or, if any parties are not dealing 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 GST input tax credits

113. Susan, who is a sole trader and registered for GST, contracts with a manager to manage her afforestation 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	$2,200*
Total due and payable by 1 January 2002 (includes GST of $600)	$6,600

*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:

$$^{1}/_{11} \text{ x } \$4,400 = \$400.$$

Hence her outgoing for the management fee is effectively $4,400 *less* $400, or $4,000.

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

$$^{1}/_{11} \text{ x } \$2,200 = \$200.$$

Hence her outgoing for the power upgrade is effectively $2,200 *less* $200, or $2,000.

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 $4,000 (not $4,400).

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 $2,000 only, not one tenth of $2,200).

Example 2 – Apportionment of fees where there is a contractual 'eligible service period' and the fees include expenditure that is 'excluded expenditure'

114. On 1 June 2002 Kevin applies for an interest into the Western Bluegum Project, a prospectus based afforestation project of 12 years. Kevin is accepted into the project and executes a lease and management agreement with the Responsible Entity for the provision of management services and the lease of his Woodlot. The terms of the lease and management agreement require Kevin to prepay the management fees and the lease fee on or before the 30 June each year for the lease of his 1 hectare Woodlot and the provision of management services between the 1 July and 30 June in the following income year. On 15 June 2002 Kevin pays the Year 1 lease fee of $400 and the Year 1 management fee of $8,600. The Year 1 management fee is made up of $7,500 for 'seasonally dependent agronomic activities' undertaken by the manager during the 'establishment period' and $1,100 for other management services.

Kevin, who is not an 'STS taxpayer' is not registered, nor required to be registered for GST.

He calculates his tax deduction for management fees and the lease fee for the **2002 income year** as follows:

Management fee

Even though he paid the $8,600 in the 2002 income year, Kevin is only able to claim a deduction of $7,500 for the 'seasonally dependent agronomic expenditure' in that income year. Because there are no 'days of eligible service period' in the 2002 income year, Kevin is unable to claim any part of the management fees paid to the manager for other management services, as a tax deduction in his tax return for the year ended 30 June 2002.

Lease fee

Because the $400 lease fee is less than $1,000 it is 'excluded expenditure' and can be claimed in full as a tax deduction in Kevin's tax return for the year ended 30 June 2002.

In the **2003 income year** Kevin can claim a tax deduction for that part of his first year's management fees that was not deductible in the 2002 income year. The tax deduction is calculated as follows:

$$\$1{,}100 \times \frac{365}{365}$$

= **$1,100** (this represents the whole of that part of the first year's management fee prepaid in the 2002 income year for management services that are not 'seasonally dependent agronomic activities' undertaken by the manager in the 'establishment period'. Although this amount was incurred in the 2002 income year it is not deductible until the 2003 income year).

For the term of the Project Kevin continues to calculate his tax deduction for prepaid fees using this method.

Detailed contents list

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

Commissioner of Taxation
15 May 2002

Previous draft:

Not previously issued in draft form

Related Rulings/Determinations:

TR 2000/8; PR 1999/95; TR 92/1; TR 92/20;TR 97/11; TR 97/16; TD 93/34; TR 98/22; IT 360;

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:

- TAA 1953 Pt IVAAA
- ITAA 1997 6-5
- ITAA 1997 8-1
- ITAA 1997 17-5
- ITAA 1997 Div 27
- ITAA 1997 Div 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 Div 70
- ITAA 1997 Div 328
- ITAA 1997 Subdiv 328-F
- ITAA 1997 Subdiv 328-G
- ITAA 1997 328-105
- ITAA 1997 328-105(1)(a)
- ITAA 1997 328-105(1)(b)
- 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)
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- ITAA 1936 82KZMG(1)
- ITAA 1936 82KZMG(2)
- ITAA 1936 82KZMG(3)
- ITAA 1936 82KZMG(4)
- ITAA 1936 82KZMG(5)
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)
- Copyright Act 1968
- Corporations Act 2001

Case references:
- FCT v. Lau 84 ATC 4929

ATO references:
NO 2001/008126
ISSN: 1441 1172