



PR 2005/53 - Income tax: Gunns Plantations Winegrape Project 2005

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 This document has changed over time. This is a consolidated version of the ruling which was published on *20 April 2005*



Product Ruling

Income tax: Gunns Plantations Winegrape Project 2005

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Potential participants may wish to refer to the Tax Office website at www.ato.gov.au or contact the Tax Office directly to confirm the currency of this Product Ruling or any other Product Ruling that the Tax Office has issued.

Preamble

The number, subject heading, **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 IVA 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 Tax Office **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 and how the product fits an existing portfolio. 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 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, 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 Tax Office 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 Gunns Plantations Winegrape Project 2005, 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 of the ITAA 1997;
- section 17-5 of the ITAA 1997;
- section 25-25 of the ITAA 1997;
- Division 27 of the ITAA 1997;
- Division 35 of the ITAA 1997;
- Division 40 of the ITAA 1997;
- Subdivision 61-J of the ITAA 1997;
- Division 328 of the ITAA 1997;
- section 82KL of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 82KZME and 82KZMF of the ITAA 1936; and
- Part IVA of the ITAA 1936.

Goods and Services Tax

3. All fees and expenditure referred to in this Ruling include the 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. Although this Ruling deals with the laws 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 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 (that is, 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;
- persons who participate in the Project through offers made other than through the Product Disclosure Statement;
- persons who finance their participation in the Project with loans other than from Gunns Finance Pty Ltd and as described at paragraph 58 to 65 of this Product Ruling;
- Gunns Plantations Limited or its associates; and
- persons who are accepted to participate in the Project after 30 May 2005.

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.

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Date of effect

11. This Ruling applies prospectively from 20 April 2005, 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 2007. 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 25 January 2005, as constituted by the documents provided on 23 December 2004, 13 and 25 January 2005 and additional correspondence, emails, facsimiles and telephone conversations dated 7 and 10 February 2005, 3, 7, 8, 9, 10, 11, 15, 16, 20, 21, 22, 23, 24, 30 and 31 March 2005, 1, 4, 5, and 6 April 2005;
- Draft Product Disclosure Statement ('PDS') for Gunns Plantations Winegrape Project 2005 received 6 April 2005;
- Draft **Constitution** of the Gunns Plantations Winegrape Project 2005 received 11 March 2005;
- Draft Compliance Plan for the Gunns Plantations Winegrape Project 2005 to be adopted by Gunns Plantations Limited (as 'Responsible Entity') received 23 December 2004;
- Draft Custody Agreement for the Gunns Plantations Winegrape Project 2005 to be entered into by Gunns Plantations Limited and Gunns Limited received 23 December 2004;
- Draft Lease Agreement between Gunns Limited (as 'Landowner') and Gunns Plantations Limited in relation to land at 'Coombend' and North Slopes received 23 December 2004;
- Lease agreement dated 29 June 2004 between Gunns Limited (as 'Landowner') and Gunns Plantations Limited in relation to land at 'White-Hills', received 23 December 2004;
- Extension or Variation of Lease or Sub-lease in respect to land at 'White-Hills' received 23 December 2004;
- Draft **Vine Right Agreement** between Gunns Plantations Limited and the 'Grower' received 9 March 2005;
- Draft **Management Agreement** between Gunns Plantations Limited (as 'Manager') and the 'Grower' received 6 April 2005;
- Draft Initial and Additional Services Sub-contracting Agreement between Gunns Plantations Limited and Gunns Limited (as 'Sub-contractor') received 11 March 2005;

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- Draft Maintenance and Harvesting Sub-Contracting Agreement between Gunns Plantations Limited and Gunns Limited (as sub-contractor) received 23 December 2004; and
- Draft **Finance Package** for the Gunns Plantations Winegrape Project 2005 between Gunns Finance and 'Growers' entering into the Project on or before 30 May 2005, received 23 March 2005.

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 'Growers' may enter into. A Loan Agreement will be executed where a 'Grower' successfully applies for finance from Gunns Finance. For the purposes 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 a 'Grower', will be a party to, which are a part of the arrangement.

16. All Australian Securities and Investment Commission (ASIC) requirements are, or will be, complied with for the term of the agreements. The effect of these agreements is summarised as follows.

Overview

17. The main features of Gunns Plantations Winegrape Project 2005 are as follows:

Location – Existing vineyards	Northern Tasmania and, in particular, on the properties known as 'North Slopes' and 'White Hills'.
Location – New Vineyards	East Coast – Tasmania and, in particular, on the property known as 'Coombend'.
Type of business to be carried on by each participant	Commercial growing of wine grapes for the purpose of harvesting and selling the produce.
Number of hectares offered for cultivation	182 hectares and oversubscription will not be accepted.
Size of each interest	0.20 hectare 'Vinelot', of which 0.06 hectares will be an 'Existing Vineyard' and 0.14 hectares, will be a 'New Vineyard'.
Minimum allocation	One 'Vinelot'.
Number of vines per hectare	Approximately 2,424 vines per hectare.

Term of the Project	20 years.
Initial cost	\$17,325 (includes an amount for prepaid fees for the first two full years of operation, irrigation fee, vineguard fee and planting fee).
Initial cost per hectare	\$86,625 (includes an amount for prepaid fees for the first two full years of operation).
Ongoing costs per Vinelot	<ul style="list-style-type: none"> • Additional 'Maintenance and Harvest Fee'. • 'Vine Right Fee'. • 'Sales Commission' of 2.2% of 'Grape Sale Proceeds'.

18. The Project is registered as a Managed Investment Scheme under the *Corporations Act 2001*. Gunns Plantations Limited ('Gunns Plantations') has been issued with an Australian Financial Service Licence and will be the Responsible Entity for the Project.

19. An offer to participate in the Project will be made through a Product Disclosure Statement (PDS) for 910 'Vinelots' which comprises of a total of 182 hectares. Participants will be invited to subscribe in the Project on or before 30 May 2005. They will become 'Growers' of cool climate wine grapes by acquiring a 'Vine Right' over a 0.20 hectare 'Vinelot', of which 0.06 hectares will be an 'Existing Vineyard' and 0.14 hectares will be a 'New Vineyard'.

20. To participate in the Project participants must complete the Application and Power of Attorney Form in the PDS and pay the 'Application Fee'. The 'Application Fee' will be banked into the relevant 'Applications Portion'. These monies will be released to Gunns Plantations when certain specified criteria have been met in accordance with clause 7 and 8 of the Constitution.

21. 'Growers' will enter into a 'Vine Right Agreement' with Gunns Plantations. The 'Vine Right Agreement' will comprise contractual rights in relation a parcel of land of 0.20 hectares called a 'Vinelot'.

22. Each 'Vinelot' will comprise of 0.14 hectares which will be situated within the 'New Vineyard', on which the 'Vines' will be planted before 31 December 2005, and 0.06 hectares of fully established vines situated within the 'Existing Vineyard', which was established in November 2004.

23. 'Growers' will also enter into a Management Agreement to contract with Gunns Plantations as the 'Manager', to undertake the 'Initial Services' and the 'Additional Services'. Gunns Plantations will also provide 'Maintenance and Harvest Services' and arrange to market and sell the 'Grapes'.

24. Gunns Plantations will appoint Gunns Limited as subcontractor to perform the 'Initial Services' and 'Additional Services' under each Management Agreement on the terms contained in the Sub-Contracting Agreement.

25. Gunns Plantations will not accept oversubscriptions. There is no minimum amount that must be raised under the PDS.

Constitution

26. The Constitution for the Project sets out the general functions, powers and duties under which the Responsible Entity agrees to act for the 'Growers' and to manage the Project. The Vine Right Agreement and the Management Agreement are Schedules to the Constitution. These Agreements will be executed on behalf of each 'Grower' who has signed the 'Application and Power of Attorney Form' attached to the PDS and who is accepted into the Project on or before 30 May 2005. After acceptance and execution of the Agreements, 'Growers' are bound by the Constitution by virtue of their participation in the Project.

27. Upon acceptance of an application, the Responsible Entity will allocate the 'Vinelot'(s) to the 'Grower' and prepare the Vine Right Agreement and Management Agreement in accordance with clause 6.

28. Before authorising or instructing the Custodian to release the 'Application Money', the Responsible Entity must be satisfied among other things that:

- the Vine Right Agreements have all been duly completed and executed;
- it has the capacity to grant the rights referred to in the Vine Right Agreement;
- all necessary consents have been obtained;
- the property that is the subject of the rights referred to in the Vine Right Agreement is not subject to any encumbrance or restrictions which detrimentally affects the interests of 'Growers';
- the Leases are registered prior to, or immediately after the acceptance of an application in respect of the Vine Right Agreement; and
- the Leases are not deregistered while it is subject to any Vine Right Agreement and Management Agreement entered into under the Constitution, clause 7.

29. The Responsible Entity under clause 10 will arrange for the Agreements to be stamped and, on behalf of the relevant 'Grower', will retain each in a safe custody until termination of the Agreements. A 'Grower' may obtain a copy of its 'Vine Right Agreement' and 'Management Agreement' by written request to the Responsible Entity accompanied by a fee not exceeding \$50.

30. The Responsible Entity is entitled to receive fees according to clause 11 and may instruct the Custodian to invest all or part of the 'Proceeds Portion' and 'Application Portion' according to clause 12.

31. Among other things the Constitution sets out in detail the following:

- general functions, powers and duties and complaints, clauses 13 and 14;
- compliance committee requirement under the Corporations Act, clause 15;
- the requirement for the Responsible Entity to procure a written report from the Independent Viticulturist and for 'Growers' to receive copies of the Viticulturist's Report, clause 16;
- the transfer and transmission of a 'Grower's' interest, clauses 18 and 19;
- the retirement or removal of the Responsible Entity according to the Corporations Act, clause 22;
- the issue of a 'Vinelot' Statement and a register of 'Members' of the Project, clauses 23 and 24; and
- the collections and payments of all 'Grape Sale Proceeds', the distribution from the 'Proceeds Portion' of the 'Fund' and deductions from Income or Profit, clauses 26, 27 and 28.

Compliance Plan

32. 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.

Lease Agreements

Lease of 'New Vineyard'

33. Gunns Limited (the 'Landowner'), has acquired land on which the 'New Vineyard' will be established and has agreed to grant to the Responsible Entity a 'Lease' of the 'Land', together with all the rights described in clause 3.2 and 4, for the 'Term' of the Project.

34. The parties will sign the 'Lease' and arrange for it to be registered against the title or titles to the 'Land'.

35. The Landowner covenants and acknowledges it will complete all the 'Establishment Works' no later than 27 May 2005, clause 9. During the 'Term' of the 'Lease' the Landowner will, in the event of destruction or serious fault, replace all 'Vineyard Infrastructure' necessary for carrying out the Project.

36. The Landowner will also ensure the replanting of any of the 'Vines' in the 'New Vineyard' which die for any cause during the 'Term'. Replanting will be as close as is practically possible to 100% of the average initial planting density of the 'Developed Area', provided that replacement of the 'Vines' is commercially feasible.

Lease of 'Existing Vineyard'

37. The Landowner is the registered proprietor of the 'Land' on which the 'Existing Vineyards' are situated and has agreed to grant to the Responsible Entity a 'Lease' of the 'Land', together with all the rights described in clauses 3.2 and 4, for the 'Term' of the Project.

38. The parties have signed the 'Lease', and it has been registered against the relevant titles. A variation to the 'Lease' will be prepared to include the Gunns Plantations Winegrape Project 2005 in the terms of the 'Lease'.

39. During the 'Term' of the 'Lease' the Landowner will, in the event of destruction or serious fault, replace all 'Vineyard Infrastructure' necessary for carrying out the Project. In the event of destruction or death of the 'Vines', the Landowner will replant for the 'Term' (as close as is practically possible to 100% of the average initial planting density of the 'Developed Area') all 'Vines' necessary for carrying out the Project.

Vine Right Agreement

40. 'Growers' participating in the Project will enter into a 'Vine Right Agreement' with Gunns Plantations for the 'Term' of the Project. Gunns Plantations will grant to 'Growers' 'Vine Rights' over the 'Vinelot' which include the following:

- access to the 'Vinelot' and the 'Common Areas';
- access to and use of the 'Vineyard Infrastructure';
- an exclusive right to access, use and enjoy the benefit of the 'Vines';
- an exclusive right to 'Harvest' the 'Grapes'; and
- an exclusive right to take all right, title and interest in the 'Harvested Grapes'.

41. Clause 4 and 5 respectively set out the rights and obligations of the 'Grower' and of Gunns Plantations. This includes the 'Grower' having at all times full right, title and interest in the 'Harvested Grapes'.

42. Under clause 6, Gunns Plantations is entitled to the 'Vine Right Fee' as described in Item 2 of Schedule 1 – Reference Table. In respect of the period from the Commencement Date to 30 June 2007, the 'Vine Right Fee' will be included in the 'Application Fee'. In respect of the year ended 30 June 2008, the 'Vine Right Fee' will be included in the 'Maintenance and Harvest Fee'. From 1 July 2008 the 'Vine Right Fee' will be deducted by the Custodian on behalf of Gunns Plantations from the 'Gross Proceeds Entitlement'. From July 2008, where a 'Grower's' obligation to pay the 'Total Fee Liability' (which includes the 'Vine Right Fee') exceeds their 'Gross Proceeds Entitlement', an Invoice will be sent to the 'Grower' for the shortfall in accordance with clause 12 of the Management Agreement.

43. At any time after the second anniversary of the 'Commencement Date', if 100% of the 'Vines' are destroyed or materially damaged by fire or any other cause, then Gunns Plantations may terminate this agreement by notice in writing to the 'Grower', clause 8.

Management Agreement

44. A Management Agreement is entered into between Gunns Plantations, as 'Manager' and each 'Grower'. The parties have agreed that the Manager will be appointed to perform the 'Services' in respect of the 'Grower's' 'Vinelot' in accordance with the terms and conditions set out in the agreement. The 'Grower' grants to the Manager for the 'Term', a licence to access the 'Grower's' 'Vinelot' to carry out the 'Initial Services', the 'Maintenance and Harvest Services' and the 'Additional Services' necessary in order to ensure that the 'Vinelot' is maintained in accordance with good viticultural practice.

45. The Manager must use its best endeavours to complete all of the 'Initial Services' in relation to the 'Grower's' 'Vinelot' before 30 June 2005, clause 4, for consideration of an 'Initial Service Fee'. The payment of the 'Application Fee' constitutes full payment of the 'Initial Services Fee'.

46. The Manager must also complete all of the following 'Additional Services' in relation to the 'Grower's' 'Vinelot', clause 5A:

- procuring and attaching dripper lines in respect of the 'New Vineyard' on or before 30 June 2005;
- planting 'Vines' in the 'New Vineyard' during the months of October to December 2005; and
- placing vineguards used in the vine establishment process of the 'New Vineyard' on or before 30 June 2006.

47. Payment of the 'Application Fee' constitutes full payment of the fees relating to the 'Additional Services' described in clause 5A.

48. The Manager will perform the 'Maintenance and Harvest Services' in a proper and efficient manner and in accordance with good viticultural practice. The Manager warrants to the 'Grower' that it has access to such staff, personnel, consultants and other specialists' services as may be reasonable necessary to perform the 'Maintenance and Harvest Services'.

49. The Manager will provide a written report in relation to the progress of the 'Vines' and the status of the 'Grower's' 'Vinelot' from the Independent Viticulturist by 31 December in the Project 'Years' 2, 3 and 4, and every second year from Year 4.

50. The Manager will be entitled to an annual 'Maintenance and Harvest Fee' in consideration for the performance of the 'Maintenance and Harvest Services', clause 9.2, subject to variations noted in paragraph 56.

51. Under this agreement the 'Grower' appoints the Manager as sole agent to market, enter into negotiations and sell the 'Grapes' on the 'Grower's' behalf on terms that are no less favourable to 'Growers' than those set out in the draft Grape Sale Agreement appended to the Management Agreement, clause 10.1.

52. The Manager will be responsible for insuring the 'Vineyard' against public risk. If requested in writing by the 'Grower', the Manager will endeavour to procure for the 'Grower' insurance cover against destruction or damage of the 'Grower's' 'Grapes'. If the Manager is able to effect insurance as requested, the Manager will Invoice the 'Grower' the relevant premium together with an administration charge of 10% of the amount of the premium in each 'Year' of the 'Term'. For 'Growers' that do obtain such insurance, and subsequently make a successful claim in relation to the policy, 35% of the insurance proceeds must be paid to the Manager in satisfaction of the 'Ongoing Fees' for that 'Vinelot', Clause 13.

53. 'Growers' who suffer financial hardship at any time after the fourth anniversary of the 'Commencement Date', may apply to the Manager to pay on the 'Grower's' behalf all 'Ongoing Fees' payable by the 'Grower' under the Management Agreement or the Vine Right Agreement, clause 16.

Pooling of 'Grapes' and distribution of proceeds

54. The Constitution sets out the circumstances relating to the pooling of 'Growers' 'Grapes' and the distribution of proceeds from that sale. This Product Ruling only applies where the following principles apply to those pooling and distribution arrangements:

- only 'Growers' who have contributed 'Grapes' from a 'Harvest' to the pool making up the proceeds are entitled to benefit from distributions from those proceeds; and

- 'Grapes' can only be pooled with the 'Grapes' of 'Growers' accepted to participate in the Gunns Plantations Winegrape Project 2005 on or before 30 May 2005.

Project Fees

55. The 'Grower' must pay an Application Fee of \$17,325 per 'Vinelot' payable on Application which will be applied towards the following:

- \$10,585 for the 'Initial Services' to be provided from the 'Commencement Date' to 30 June 2005;
- \$1,146 for 'Vine Right Fees' for the period from the 'Commencement Date' to 30 June 2007;
- \$4,070 for 'Maintenance and Harvest Fees' for the period from 1 July 2005 to 30 June 2007;
- \$534 as the 'Irrigation Fee';
- \$392 as the 'Vine Guard Fee'; and
- \$598 as the 'Planting Fee.'

56. Under clause 9.2 of the Management Agreement 'Growers' will make the following 'Maintenance and Harvest Fee' payments per 'Vinelot':

- from 1 July 2005 to 30 June 2007, a 'Maintenance and Harvest Fee' of \$4,070 is included in the 'Application Fee'.

For the year ending 30 June 2007:

- any 'Gross Proceeds Entitlement' will be retained by the Custodian, on behalf of the Manager, and paid to the Manager to offset 'Maintenance' and 'Harvest' costs; and
- in addition, 'Growers' will be invoiced an amount equal to 10% of any 'Gross Proceeds Entitlement', being for GST on that component of the 'Maintenance and Harvest Fee'.

For the year ending 30 June 2008:

- any 'Gross Proceeds Entitlement' will be retained by the Custodian, on behalf of the Manager, and paid to the Manager to offset Maintenance and Harvest costs; and
- in addition, 'Growers' will be invoiced an amount equal to 10% of any 'Gross Proceeds Entitlement', being for GST on that component of the 'Maintenance and Harvest Fee'.

For Years 4 to 20:

- in all other years, the 'Maintenance and Harvesting Fee' will be equal to the cost of performing the Maintenance and Harvest Services plus a 21% mark-up as an administration charge. This fee is subject to a cap of \$3,300 per 'Vinelot';
- the Manager is entitled to a 'Sales Commission' of 2.2% of the 'Grape Sale Proceeds'; and
- the 'Maintenance and Harvest Fee', and 'Sales Commission' will be deducted by the Custodian on behalf of the Manager from the 'Gross Proceeds Entitlement' and paid to the Manager in accordance with the Constitution. Where a 'Grower's' obligation to pay the 'Maintenance and Harvest Fee' exceeds their 'Gross Proceeds Entitlement', an 'Invoice' will be sent to the 'Grower' for the shortfall.

57. Under clause 6 of the 'Vine Right Agreement' 'Growers' will make the following 'Vine Right Fee' payments per 'Vinelot':

- from the 'Commencement Date' to period ending 30 June 2007 a 'Vine Right Fee' of \$1,146 is included in the 'Application Fee';
- for each subsequent year after 30 June 2007, a 'Vine Right Fee' of \$550 per year (indexed annually for CPI from the 12 months ended 30 March 2006);
- for the period from 1 July 2007 to 30 June 2008 the Manager will retain the 'Gross Proceeds Entitlement' in lieu of a 'Vine Right Fee'; and
- from 1 July 2008 until the 'Term' of the Project, the 'Vine Right Fee' will be deducted by the Custodian on behalf of the Manager from the 'Gross Proceeds Entitlement' and paid to the Manager in accordance with the Constitution. Where a 'Grower's' obligation to pay the 'Vine Right Fee', exceeds their 'Gross Proceeds Entitlement', an 'Invoice' will be sent to the 'Grower' for the shortfall.

Finance

58. 'Growers' cannot rely on this Product Ruling if they enter into a finance arrangement, with Gunns Finance that materially differs from those provided to the Tax Office by Gunns Plantations with the application for this Product Ruling. These finance packages are summarised below.

Finance for the Application Fee

59. A number of finance packages will be offered on commercial terms by Gunns Finance. 'Growers' can borrow from Gunns Finance provided that the conditions precedent in clause 3 of Part B of the 'Loan Terms' is satisfied.

60. The loans offered are a 12 month interest free option, or for periods of 3, 5, or 10 years. 'Growers' may also choose a 10 year loan that consists of 5 years of interest only payments followed by 5 years of principal and interest payments.

61. Common features contained in each of these finance packages are that:

- the 'Grower's' application to participate in the Project has been accepted by Gunns Plantations;
- the 'Grower' pays a loan 'Establishment Fee' of \$150, which is to be paid at the time that the loan is established;
- Gunns Finance will take security over the 'Grower's' Vinelot;
- finance is available for between 70% and 90% of the Application Fee, depending on the finance package the 'Grower' obtains;
- an additional 2% interest per annum applies to overdue repayments; and
- the 'Grower' may repay the 'Outstanding Balance' in whole or in part in any time. However, where the loan is repaid early, the 'Grower' will pay to Gunns Finance a break cost of \$400 in accordance with clause 6.2 of the 'Loan Terms'.

62. The deposit required to fund the 'Loan' will vary, between 10 to 30% of the 'Application Fee' at the absolute discretion of Gunns Finance. Similarly the interest rate of the 'Loan' may also be varied within good commercial terms at the absolute discretion of Gunns Finance.

63. The 'Grower' agrees to repay the 'Loan', and pay interest and all other 'Outstanding Monies' to Gunns Finance. The 'Grower' will pay the 'Repayment Amount' on the 'Repayment Date' of each month during the 'Term' of the 'Loan' as detailed in Part J – Loan Schedule.

64. The specific features of each of the finance arrangements 'Growers' may enter into are as follows:

Standard Finance Package:

Principal only loan:

'Growers' may apply to enter into a non-interest bearing loan with Gunns Finance to fund the 'Application Fee'.

'Growers' who enter into this finance arrangement will be required to pay a deposit of 10% of the 'Application Fee', and the balance must be repaid in 12 equal monthly instalments, commencing July 2005.

Principal and interest loans:

'Growers' may apply to enter into an interest bearing loan with Gunns Finance to fund the 'Application Fee'. The terms of these loans are as follows:

- the 'Term' of the 'Loan' will be for 3, 5 or 10 years;
- a deposit of 20% of the Application Fee is required;
- an interest rate of 10.5% will apply for the first 5 years of the loan. For 10 year loans the interest rate will be reviewed after 5 years and fixed at 4% points above the ANZ Banking Group Ltd's 5 year swap reference rate; and
- 'Growers' will be required to make equal monthly repayments of the outstanding balance, commencing July 2005. The repayments relating to each loan are set out in Part J of the Finance Package.

5 year interest only, 5 year principal and interest:

Gunns Finance also offers 'Growers' a 5 year interest only loan, with interest and principal repayments being required to repay the loan from years 6 to 10 inclusive. The terms of this loan are as follows:

- the 'Term' of the 'Loan' is 10 years;
- a deposit of 30% of the 'Application Fee' is required;
- an interest rate of 10.5% will apply for the first 5 years of the loan. The interest rate will be reviewed after 5 years and fixed at 4% points above the ANZ Banking Group Ltd's 5 year swap reference rate;
- the 'Repayment Amounts' are set out in Part J of the Finance Package; and
- all payments under this loan are payable monthly in arrears.

65. 'Growers' cannot rely on any part of this Product Ruling if the 'Application Fee', other than an 'Application Fee' payable subject to a finance arrangement, is not paid in full by 30 May 2005. Where an application is accepted by Gunns Plantations, subject to finance approval by any lending institution, 'Growers' cannot rely on this Ruling if written evidence of that approval has not been given to Gunns Plantations by 30 May 2005.

66. This Ruling also 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 other than Gunns Finance are involved or become involved in the provision of finance to 'Growers' for the Project.

Ruling

Application of this Ruling

67. Subject to paragraph 8, this Ruling applies only to 'Growers' who are accepted to participate in the Project on or before 30 May 2005 and who have executed a 'Vine Right Agreement' and a 'Management Agreement' on or 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.

The Simplified Tax System ('STS')

Division 328

68. To be an 'STS taxpayer' a Grower must be eligible to be an 'STS taxpayer' and must have elected to be an 'STS taxpayer'. For a Grower participating in the Project, the recognition of income and the timing of tax deductions is different under the STS where the Grower uses the cash accounting method.

Qualification

69. 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.

25% Entrepreneurs tax offset

Subdivision 61-J

70. For the first income year starting on or after 1 July 2005, Subdivision 61-J of the ITAA 1997 provides a 25% tax offset of income tax liability related to the business income of a business in the STS with annual group turnover of less than \$75,000. Entitlement to the offset varies depending on the type of entity and is therefore outside the scope of this Ruling.

Assessable income

Section 6-5

71. 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.

72. Other than 'Growers' referred to in paragraph 73, for the 2005-06 income year and later years, a 'Grower' will be assessable on ordinary income from carrying on their business of viticulture in the income year in which that income is derived.

73. For the 2005-06 income year and later years, a 'Grower' who is an 'STS taxpayer' using the cash accounting method will be assessable on ordinary income from carrying on their business of viticulture in the income year in which that income is received.

Deductions for the 'Initial Service Fee', the 'Maintenance and Harvest Fee', the 'Vine Right Fee', 'Interest' and the 'Loan Establishment Fee'

Section 8-1, section 328-105 and section 25-25

74. A 'Grower' who is accepted to participate in the Project or on before 30 May 2005 may claim deductions, on a per 'Vinelot' basis, for the following expenditure.

75. However, if for any reason, an amount shown or referred to in the Table below is not fully paid in the year in which it is incurred by a 'Grower' who is an 'STS taxpayer' using the cash accounting method, 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 below which is not paid in the year in which it is incurred will be deductible in the year in which it is actually paid.

Fee Type	Year ended 30 June 2005	Year ended 30 June 2006	Year ended 30 June 2007
'Initial Service Fee'	\$10,269 – See Notes (i) & (ii)	Nil	Nil
'Maintenance and Harvest Fee'	Nil	\$2,035 – See Notes (i) & (iii)	\$2,035 – See Notes (i), (iii) & (iv)
'Vine Right Fee'	\$46 – See Notes (i) & (iii)	\$550 – See Notes (i) & (iii)	\$550 – See Notes (i) & (iii)
Interest	As incurred (Non-STs taxpayers) Or as paid (STs taxpayers) See Note (v)	As incurred (Non-STs taxpayers & STs taxpayers using accruals accounting) Or as paid (STs taxpayers using cash accounting) See Note (v)	As incurred (Non-STs taxpayers & STs taxpayers using accruals accounting) Or as paid (STs taxpayers using cash accounting) See Note (v)
'Loan Establishment Fee'	Amount must be calculated – See Note (vi)	Amount must be calculated – See Note (vi)	Amount must be calculated – See Note (vi)

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 (for example, input tax credits): Division 27. See Example 1 at paragraph 125.
- (ii) For the year ended 30 June 2005, the 'Initial Services Fee' payable on application is deductible to the extent shown in the Table above in the year that it is incurred (where the Grower is not an 'STS taxpayer') or the year in which it is paid (where the Grower is an 'STS taxpayer'). The Initial Services Fee payable on application is not deductible in full under section 8-1 as it consists of an amount of \$316 relating to landcare operations, which is capital in nature (see paragraphs 76 or 77).
- (iii) The 'Maintenance and Harvest Fee' and the 'Vine Right Fee' payable on application are prepayments and **not** deductible in full in the year incurred (where the 'Grower' is **not an 'STS taxpayer'**) or the year in which they are paid (where the 'Grower' is an **'STS taxpayer'**). Deductions for these amounts **must** be determined using the formula in subsection 82KZMF(1) (see paragraphs 99 to 108). This provision operates to apportion expenditure over the eligible service period. The eligible service period for the 'Maintenance and Harvest Services' commences from 1 July 2005 to 30 June 2007. Therefore an amount of \$2,035 per 'Vinelot' is deductible for 'Maintenance and Harvest Fee' in the year ending 30 June 2006 and 30 June 2007. The eligible service period for the 'Vine Right Fee' commences from 30 May 2005 to 30 June 2007. Therefore, an amount of \$46 per 'Vinelot' in the year ending 30 June 2005 and \$550 per 'Vinelot' for each of the years ending 30 June 2006 and 30 June 2007 is deductible. (See Example 2 at paragraph 125).
- (iv) For the year ending 30 June 2007, Growers will be invoiced for an additional amount equal to 10% of any 'Gross Proceeds Entitlement' being the GST on that component of the 'Maintenance and Harvest Fee'. Where a Grower is **not** an 'STS taxpayer' or is an 'STS taxpayer' using the accruals accounting method, this amount is fully deductible under section 8-1 in the year the expenditure is incurred. Where a Grower is an 'STS taxpayer' who uses the cash accounting method this expenditure is deductible under section 8-1 in the year it is paid.

- (v) The deductibility or otherwise of interest arising from loan agreements entered into with financiers other than Gunns Finance is outside the scope of this Ruling. However all 'Growers', including those who finance their participation in the Project other than with Gunns Finance, should read the discussion of the prepayment rules in paragraphs 99 to 106 as those rules may be applicable if interest is prepaid. A 'Grower' who chooses, or who is required to prepay interest under a loan agreement is outside the scope of this rulings and may request a private ruling on the taxation consequences of their participation in the Project.
- (vi) The 'Loan Establishment Fee' payable to Gunns Finance is a borrowing expense and is deductible under section 25-25. It is incurred for borrowing moneys that are used, or are to be used during that income year solely for income producing purposes. The deduction is spread over the period of the loan or 5 years, whichever is the shorter. The deductibility or otherwise of borrowing costs arising from loan agreements entered into with financiers other than Gunns Finance is outside the scope of this Ruling.

Deductions for capital expenditure (non-'STS taxpayers')

Division 40

76. A 'Grower' who is not an 'STS taxpayer' will also be entitled to tax deductions relating to vineyards, water facilities (for example irrigation), landcare operations and 'Vines'. All deductions shown in the following Table are determined under Division 40.

Fee Type	ITAA 1997 section	Year ended 30 June 2005	Year ended 30 June 2006	Year ended 30 June 2007
Vineyards	40-25	Nil	Amount must be calculated – See Notes (vii) & (viii)	Amount must be calculated – See Notes (vii) & (viii)
Water facility (eg dam, irrigation)	40-515	\$178 – See Notes (vii) & (ix)	\$178 – See Notes (vii) & (ix)	\$178 – See Notes (vii) & (ix)
Landcare Operation	40-630	\$316 – See Notes (vii) & (x)		
Establishment of horticultural plants ('Vines')	40-515	Nil – See Notes (vii) & (xi)	Nil – See Notes (vii) & (xi)	Nil – See Notes (vii) & (xi)

Notes:

- (vii) If the 'Grower' is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted as relevant for GST (for example input tax credits): Division 27. See Example 1 at paragraph 125.
- (viii) A vineyard is a 'depreciating asset'. Each 'Grower' holds an interest in each vineyard which is a 'low-cost asset' and can be allocated to a 'low-value pool'. Once any 'low-cost asset' of a 'Grower' is allocated to a 'low-value pool', all other 'low-cost assets' the 'Grower' start to 'hold' in that year or a later year must be allocated to that pool. If the 'Grower' has already allocated an asset to a 'low-value pool', the vineyard assets would also have to be allocated to that pool. Otherwise, the 'Grower' must decide whether to create a 'low-value pool'. If the assets are allocated to a 'low-value pool', the capital expenditure on the vineyards will be deducted under the diminishing value methodology of the pool based on a rate of 18.75% in the year the vineyards are first used and a rate of 37.5% in subsequent years (section 40-440). If the assets are not allocated to a 'low-value pool', they can be written off based on the 'effective life' of the vineyards. As there has been no determination of the 'effective life' of a vineyard by the Commissioner, 'Growers' must self-assess an 'effective life'. Vineyards are not installed until after the 'Vines' are planted and no deduction for the decline in value is available until this installation occurs. The Manager will advise 'Growers' of that date to enable them to calculate the deduction.
- (ix) Any irrigation system, dam or bore is a 'water facility' as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. A deduction is available under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one third of the capital expenditure incurred by each 'Grower' on the installation of the 'water facility' in the year in which it is incurred and one third in each of the next 2 years of income (section 40-540).
- (x) Any capital expenditure incurred for a 'landcare operation' (as defined in section 40-635) is fully deductible in the year it is incurred under Subdivision 40-G, section 40-630.

- (xi) 'Vines' are a 'horticultural plant' as defined in subsection 40-520(2). As 'Growers' hold a 'Vine Right' over the land, one of the conditions in subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the 'Vines' is determined using the formula in section 40-545 and is based on the capital expenditure incurred by the 'Grower' that is attributable to their establishment. If the 'Vines' have an 'effective life' of greater than 13 but fewer than 30 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 13%. The deduction is allowable when the 'Vines' enter their first commercial season (section 40-530, item 2). The Manager will inform 'Growers' of when the 'Vines' enter their first commercial season.

Deductions for capital expenditure ('STS taxpayers')

Subdivision 328-D and Subdivisions 40-F and 40-G

77. A 'Grower' who is an 'STS taxpayer' will also be entitled to tax deductions relating to vineyards, water facilities (for example, irrigation), a 'landcare operation' and 'Vines'. Deductions relating to the 'cost' of vineyards must be determined under Division 328. An 'STS taxpayer' may claim deductions in relation to water facilities under Subdivision 40-F and in relation to a 'landcare operation' under Subdivision 40-G. If the 'water facility' or 'landcare operation' expenditure is on a 'depreciating asset' used to carry on the business, they may choose to claim deductions under Division 328. Deductions for the 'Vines' must be determined under Subdivision 40-F.

78. The deductions shown in the following table assume, for representative purposes only, that a 'Grower' has either chosen to or can only claim deductions for expenditure on water facilities or a 'landcare operation' under Subdivisions 40-F or 40-G and not under Division 328. If the expenditure has been incurred on 'depreciating assets' and is claimed under Division 328, the deduction is determined as discussed in Note (xiii).

79. Under Division 328, if the 'cost' of a 'depreciating asset' at the end of the income year is less than \$1,000 (a 'low-cost asset'), it can be claimed as an immediate deduction when first used or 'installed ready for use'. This is so provided the 'Grower' is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income.

PR 2005/53

Fee Type	ITAA 1997 section	Year ended 30 June 2005	Year ended 30 June 2006	Year ended 30 June 2007
Vineguards	328-180	Nil	Amount must be calculated See Notes (xii) & (xiii)	Amount must be calculated See Notes (xii) & (xiii)
Water facility (eg irrigation, dam, bore, etc)	40-515	\$178 – see Notes (xii) & (xiv)	\$178 – see Notes (xii) & (xiv)	\$178 – see Notes (xii) & (xiv)
Landcare Operation	40-630	\$316 – See Notes (xii) & (xv)		
Establishment of horticultural plants ('Vines')	40-515	Nil – see Notes (xii) & (xvi)	Nil – see Notes (xii) & (xvi)	Nil – see Notes (xii) & (xvi)

Notes:

- (xii) If the 'Grower' is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted as relevant for GST (for example input tax credits): Division 27. See Example 1 at paragraph 125.
- (xiii) A vineyard is a 'depreciating asset'. Each 'Grower' holds an interest in each vineyard which is a 'low-cost asset' as defined in subsection 40-425(2). It cannot be allocated to the 'general STS pool' (section 328-180). A deduction equal to the amount of the 'Grower' expenditure for the vineyards is available in the income year in which they are used or 'installed ready for use'. This is so provided the 'Grower' is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income. Vineyards are not installed until after the 'Vines' are planted. The Project Manager will advise when that has occurred.
- (xiv) Any irrigation system, dam or bore is a 'water facility' as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. If the expenditure is on a 'depreciating asset' (the underlying asset), the 'Grower' may choose to claim a deduction under either Division 328 or Subdivision 40-F. For the purposes of Division 328, each 'Grower's' interest in the underlying asset is itself deemed to be a 'depreciating asset'. If the 'cost' apportionable to that deemed 'depreciating asset' is less than \$1,000, the deemed asset is treated

as a 'low-cost asset' and that amount is deductible in full when the underlying asset is first used or 'held' ready for use. This is so provided the 'Grower' is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income. If the deemed asset is not treated as a 'low-cost asset', the tax deduction allowable in the year ended 30 June 2005 is determined by multiplying its 'cost' by half the relevant STS pool rate. At the end of the year, it is allocated to the relevant STS pool and in subsequent years the full pool rate will apply. If the expenditure is not on a 'depreciating asset', or if they choose to use Subdivision 40-F, 'Growers' must claim deductions under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one third of the capital expenditure incurred by each 'Grower' on the installation of the 'water facility' in the year in which it is incurred and one third in each of the next 2 years of income (section 40-540).

- (xv) Any capital expenditure incurred for a 'landcare operation' (as defined in section 40-635) is fully deductible in the year it is incurred under Subdivision 40-G, section 40-630. If the expenditure is on a 'depreciating asset' (the underlying asset), the 'Grower' may choose to claim a deduction under either Division 328 or Subdivision 40-G (although expenditure on some items of plant can only be deducted under Division 328). For the purposes of Division 328, each 'Grower's' interest in the underlying asset is itself deemed to be a 'depreciating asset'. If the 'cost' apportionable to that deemed 'depreciating asset' is less than \$1,000, the deemed asset is treated as a 'low-cost asset' and that amount is deductible in full when the underlying asset is first used or 'held' ready for use. This is so provided the 'Grower' is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income. If the deemed asset is not treated as a 'low-cost asset', the tax deduction allowable is determined by multiplying its 'cost' by half the relevant STS pool rate. At the end of the year, it is allocated to the relevant STS pool and in subsequent years, the full pool rate will apply. If the expenditure is not on a 'depreciating asset', the expenditure is fully deductible under Subdivision 40-G.

- (xvi) 'Vines' are a 'horticultural plant' as defined in subsection 40-520(2). As 'Growers' hold the land under a licence, one of the conditions in subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the 'Vines' is determined using the formula in section 40-545 and is based on the capital expenditure incurred by the 'Grower' that is attributable to their establishment. If the 'Vines' have an 'effective life' of greater than 13 but fewer than 30 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 13%. The deduction is allowable when the 'Vines' enter their first commercial season (section 40-530, item 2). The Project Manager will inform 'Growers' of when the 'Vines' enter their first commercial season.

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

Section 35-55 – exercise of Commissioner's discretion

80. A 'Grower' who is an individual accepted into the Project by 30 May 2005 may have losses arising from their participation in the Project that would be deferred to a later income year under section 35-10. Subject to the Project being carried out in the manner described above, the Commissioner will exercise the discretion in paragraph 35-55(1)(b) for these 'Growers' for the income years ending **30 June 2005 to 30 June 2008**. This conditional exercise of the discretion will allow those losses to be offset against the 'Grower's' other assessable income in the income year in which the losses arise.

Section 82KL and Part IVA

81. For a 'Grower' who participates in the Project and incurs expenditure as required by the Management Agreement and the Lease 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.

Explanation

Is the Grower carrying on a business?

82. For the amounts set out in the Tables above to constitute allowable deductions the 'Grower's' viticulture activities as a participant in the Gunns Plantations Winegrape Project 2005 must amount to the carrying on of a business of primary production. These viticulture activities will fall within the definitions of 'horticulture' and 'commercial horticulture' in section 40-535 of the ITAA 1997.

83. For schemes such as that of the Gunns Plantations Winegrape Project 2005, 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 *Commissioner of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

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

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

85. In this Project, each 'Grower' enters into a Vine Right Agreement and a Management Agreement.

86. Under the Vine Right Agreement each individual 'Grower' will have rights over the land on which the Vines will be planted. The Vine Right Agreement provides the 'Grower' with an ongoing right to the 'Vines' for the term of the Project. Under the 'Vine Right' the 'Grower' must use the land in question for the purpose of carrying out viticultural activities and for no other purpose. 'Vine Right' allows the Manager to come onto the land to carry out its obligations under the Management Agreement.

87. Under the Management Agreement the Manager is engaged by the 'Grower' to establish and maintain a 'Vinlot' 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 'Vinlot' on the 'Grower's' behalf.

88. In establishing the 'Vinelot', the 'Grower' engages the Manager to install vineyards and procuring and attaching dripper lines, carry out 'landcare operation' and to plant the 'Vines on the 'Grower's' 'Vinelot'. During the term of the Project, these assets will be used wholly to carry out the 'Grower's' viticulture activities. The Manager is also engaged to harvest and sell, on the 'Grower's' behalf, the 'Grapes' grown on the 'Grower's' 'Vinelot'.

89. 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.

90. 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 its 'Grapes' that will return a before-tax profit, that is, a profit in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

91. The pooling of 'Grapes' grown on the 'Grower's' 'Vinelot' with the 'Grapes' of other 'Growers' is consistent with general viticulture practices. Each 'Grower's' proportionate share of the sale proceeds of the pooled 'Grapes' will reflect the proportion of the 'Grapes' contributed from their 'Vinelot'.

92. The Manager's services and the installation of assets on the 'Grower's' behalf are also consistent with general viticulture practices. The assets are of the type ordinarily used in carrying on a business of viticulture. While the size of a 'Vinelot' is relatively small, it is of a size and scale to allow it to be commercially viable (see Taxation Ruling IT 360).

93. 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' 'Vinelot' 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.

94. The viticulture activities, and hence the fees associated with their procurement, are consistent with an intention to commence regular activities that have an 'air of permanence' about them. For the purposes of this Ruling, the 'Growers' viticulture activities in the Gunns Plantations Winegrape Project 2005 will constitute the carrying on of a business.

The Simplified Tax System

Division 328

95. 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.

96. 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'.

Deductions for the 'Initial Service Fee' and the 'Vine Right Fee'

Section 8-1

97. Consideration of whether the 'Initial Service Fee' and 'Vine Right Fee' 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.

98. The 'Initial Service Fee' and 'Vine Right Fee' associated with the viticulture activities will relate to the gaining of income from the 'Grower's' business of viticulture (see above), and hence have a sufficient connection to the operations by which income (from the regular sale of 'Grapes') 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. Other than the Landcare expenditure, there is no capital component found in the 'Initial Service Fee' and 'Vine Right Fee'. 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***

99. 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 (for example, 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.

100. For this Project, only section 82KZL (an interpretive 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 them from the operation of section 82KZMF.

Sections 82KZME and 82KZMF

101. 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)).

102. 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.

103. 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 other than Gunns Finance. 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.

104. 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.

105. 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.

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

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

Application of the prepayment provisions to this Project

107. The expenditure incurred by a 'Grower' in the Project for the 'Maintenance and Harvest Fees' and 'Vine Right Fees' 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.

108. The prepaid 'Management and Harvest Fees' and 'Vine Right Fees' incurred by 'Growers' do not fall within any of the 5 exceptions to section 82KZME. Therefore, the deduction for each year is determined using the formula in subsection 82KZMF(1). Section 82KZMF will apportion the deduction for prepaid 'Management and Harvest Fees' and 'Vine Right Fee' over the period that the services for which the prepayment is made are provided.

Interest deductibility**Section 8-1***(i) 'Growers' who use Gunns Finance as the finance provider*

109. Some 'Growers' may finance their participation in the Project through a loan facility with Gunns Finance. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of the 'Management and Harvest' and 'Vine Right Fees'.

110. The interest incurred for the year ended 30 June 2006 and in subsequent years of income will be in respect of a loan to finance the 'Grower's' business operations – the cultivation and growing 'Grapes' and the lease (or licence) of the land on which the 'Vines' will have been planted – that will continue to be directly connected with the gaining of 'business income' from the Project. Such interest will, therefore, have a sufficient connection with the gaining of assessable income to be deductible under section 8-1.

111. As with 'Maintenance and Harvest' and 'Vine Right Fees', in the absence of any application of the prepayment provisions (see paragraphs 99 to 106), the timing of deductions for interest will again depend upon whether a 'Grower' is an 'STS taxpayer' or is not an 'STS taxpayer'.

112. If the 'Grower' is not an 'STS taxpayer', interest is deductible in the year in which it is incurred.

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

(ii) 'Growers' who prepay interest or DO NOT use Gunns Finance as the finance provider

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

115. 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. Alternatively, a 'Grower' may choose to prepay such interest. All 'Growers', including those who finance their participation in the Project other than with Gunns Finance, who choose, or who is required to prepay interest under a loan agreement is outside the scope of this rulings and may request a private ruling on the taxation consequences of their participation in the Project.

Expenditure of a capital nature***Division 40 and Division 328***

116. Any part of the expenditure of a 'Grower' 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, expenditure attributable to vineyards, water facilities, a 'landcare operation', and the establishment of the 'Vines' is of a capital nature. This expenditure falls for consideration under Division 40 or Division 328 of the ITAA 1997.

117. The application and extent to which a 'Grower' claims deductions under Division 40 and Division 328 depends on whether or not the 'Grower' is an 'STS taxpayer'.

118. The tax treatment of capital expenditure has been dealt with in a representative way in paragraphs 76 and 77 in the Tables and the accompanying Notes.

Division 35 – deferral of losses from non-commercial business activities***Section 35-55 – exercise of Commissioner's discretion***

119. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income years **30 June 2005 to 30 June 2008** the Commissioner has applied the principles set out in Taxation Ruling TR 2001/14 Income tax: Division 35 – non-commercial business losses. Accordingly, based on the evidence supplied, the Commissioner has determined that for those income years ended 30 June 2005 up to and including 30 June 2008:

- it is because of its nature the business activity of a 'Grower' will not satisfy one of the four tests in Division 35;
- there is an objective expectation that within a period that is commercially viable for the viticulture industry, a 'Grower's' business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit; and
- a 'Grower' who would otherwise be required to defer a loss arising from their participation in the Project under subsection 35-10(2) until a later income year is able to offset that loss against their other assessable income.

120. The exercise of the Commissioner's discretion under paragraph 35-55(1)(b) is conditional on the Project being carried on in the manner described in this Ruling during the income years specified. If the Project is carried out in a materially different way to that described in the Ruling a 'Grower' will need to apply for a private ruling on the application of section 35-55 to those changed circumstances.

Section 82KL – recouped expenditure

121. 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

122. 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).

123. The Gunns Plantations Winegrape Project 2005 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 74 to 79 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.

124. ‘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 ‘Grapes’. 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

125. Susan, who is a sole trader and registered for GST, contracts with a manager to manage her viticulture business. Her manager is registered for GST and charges her a management fee payable every six months in advance. On 1 December 2004, 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 1/1/2005 to 30/6/2005	\$4,400*
Carrying out of upgrade of power for your vineyard as quoted	<u>\$2,200*</u>
Total due and payable by 1 January 2005 (includes GST of \$600)	<u>\$6,600</u>

*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:

$$\frac{1}{11} \times \$4,400 = \$400.$$

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:

$$\frac{1}{11} \times \$2,200 = \$200.$$

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 2005, 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

126. Murray decides to participate in the ABC Winegrape Project which is offering 500 interests of 0.5ha in a wine grape project of 25 years. The management fees are \$5,000 in the first year and \$1,200 for years 2 and 3. From year 4 onwards the management fee will be the previous year's fee increased by the CPI. The first year's fees are payable on execution of the agreements for services to be provided in the following 12 months and thereafter, the fees are payable in advance each year on the anniversary of that date. The project is subject to a minimum subscription of 300 interests. Murray provides the Project Manager with a 'Power of Attorney' allowing the Manager to execute his Management Agreement and the other relevant agreements on his behalf. On 5 June 2004 the Project Manager informs Murray that the minimum subscription has been reached and the Project will go ahead. Murray's agreements are duly executed and management services start to be provided on that date.

Murray is an 'STS taxpayer' who is not registered, nor required to be registered for GST. He calculates his tax deduction for management fees for the **2004 income year** as follows:

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

$$\$5,000 \times \frac{26}{365}$$

= **\$356** (this is Murray's total tax deduction in 2004 for the Year 1 prepaid management fees of \$5,000. It represents the 26 days for which management services were provided in the 2004 income year).

In the **2005 income year** Murray will be able to claim a tax deduction for management fees calculated as the sum of two separate amounts:

$$\$5,000 \times \frac{339}{365}$$

= **\$4,644** (this represents the balance of the Year 1 prepaid fees for services provided to Murray in the 2005 income year).

$$\$1,200 \times \frac{26}{365}$$

= **\$85** (this represents the portion of the Year 2 prepaid management fees for the 26 days during which services were provided to Murray in the 2005 income year).

\$4,644 + \$85 = \$4,729 (The sum of these two amounts is Murray's total tax deduction for management fees in 2005).

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

Detailed contents list

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Commissioner of Taxation

20 April 2005

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NO 2004/16890
ISSN 1441-1172