



PR 2005/81 - Income tax: Port Robe Estate Vineyard Project Stage 3 (2006 Planting Season Vigneron, Post 30 September 2005)

 This cover sheet is provided for information only. It does not form part of *PR 2005/81 - Income tax: Port Robe Estate Vineyard Project Stage 3 (2006 Planting Season Vigneron, Post 30 September 2005)*

 This document has changed over time. This is a consolidated version of the ruling which was published on *25 May 2005*



Product Ruling

Income tax: Port Robe Estate Vineyard Project Stage 3 (2006 Planting Season Vigneron, Post 30 September 2005)

Contents	Para
What this Product Ruling is about	1
Date of effect	11
Withdrawal	13
Arrangement	14
Ruling	56
Explanation	79
Example	124
Detailed contents list	125

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 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 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 law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates. In this Ruling this arrangement is sometimes referred to as 'Port Robe Estate Vineyard Project Stage 3', or just 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;
- Division 27 of the ITAA 1997;
- Division 35 of the ITAA 1997;
- Division 40 of the ITAA 1997;
- Division 43 of the ITAA 1997;
- Subdivision 61-J of the ITAA 1997;
- Division 108 of the ITAA1997;
- Division 110 of the ITAA1997;
- section 44 of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 82KL of the ITAA 1936;
- section 82KZL of the ITAA 1936;
- section 82KZME of the ITAA 1936;
- section 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 'Vigneron') 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 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 more specifically identified in the Ruling part of this Product Ruling and who enter into the arrangement described below on or after the date this Ruling is made. They will have a purpose of staying in the arrangement until it is completed (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 'Vignerons'.

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; and
- Vignerons where a conditional allotment has been made under clause 4.6 of the Constitution and the approval process of an application subject to finance has not been completed by 30 June in the year of application (see paragraph 58).

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, apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to:

Commonwealth Copyright Administration
Attorney General's Department
Robert Garran Offices
National Circuit
Barton ACT 2600

or posted at: <http://www.ag.gov.au/ccca>

Date of effect

11. This Ruling applies prospectively from 25 May 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 the private ruling if the income year to which the private ruling relates has ended or has commenced but not yet ended. However, if the arrangement covered by the private ruling has not yet begun to be carried out, and the income year to which it relates has not yet commenced, this Ruling applies to the taxpayer to the extent of the inconsistency only (see Taxation Determination TD 93/34).

Withdrawal

13. This Product Ruling is withdrawn and ceases to have effect after 30 June 2008. The Ruling continues to apply, in respect of the tax law(s) ruled upon, to all persons within the specified class who enter into the specified arrangement during the term of the Ruling. Thus, the Ruling continues to apply to those persons, even following its withdrawal, who entered into the specified arrangement prior to withdrawal of the Ruling. This is subject to there being no change in the arrangement or in the persons' involvement in the arrangement.

Arrangement

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

- Application for a Product Ruling, received 27 January 2005;
- A draft Combined Disclosure Statement, issued by Vision Capital Management Ltd (the Responsible Entity) received 17 May 2005;
- A draft Constitution of the Port Robe Estate Vineyard Project, received 12 May 2005;
- **A Vineyard Management and Lease Agreement between Vision Capital Management Ltd, (Responsible Entity), Port Robe Management Ltd (Project Manager) and the Vigneron received 12 May 2005;**
- A Services Agreement between Vision Capital Management Ltd and Port Robe Management Ltd, received on 13 May 2005;
- A draft Compliance Plan for Vision Capital Management Ltd as the Responsible Entity, received 13 May 2005;
- A draft Second deed of Amendment to Declaration of Trust by the Project Manager, received 27 January 2005;
- **A Grape Sale Agreement between Vision Capital Management Ltd (Responsible Entity), Port Robe Management Ltd (Project Manager), Port Robe Estate Ltd (Winemaker) and the Vigneron received 27 January 2005;**
- A Vineyard Management Agreement between Port Robe Management Ltd and Cape Jaffa Viticulture Pty Ltd (Cape Jaffa), dated 30 June 2001;
- An Exclusive Licence of Plant Breeder's Rights between D and D E Mann (the Owners), Taurus Pty Ltd (Taurus), Surepoint Securities Pty Ltd and Port Robe Estate Ltd, dated 8 April 2003;
- Deed of Variation of Exclusive Licence between D and D E Mann (the Owners), Taurus Pty Ltd (Taurus), Surepoint Securities Pty Ltd and Port Robe Estate Ltd, dated 22 July 2004;
- A Port Robe Agreement between Port Robe Estate Ltd (the Licensee) and Port Robe Management Ltd, (the sub-licensee) dated 8 April 2003; and

- Various correspondence between the Applicant and the Taxation office received 1 February 2005, 14 April 2005, 20 April 2005, 11 May 2005, 12 May 2005, 13 May 2005 and 17 May 2005.

Note: Certain information has been provided by the applicant 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 Vignerons enter into or become a party to. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Vigneron, or any associate of a Vigneron, will be a party to, which are part of the arrangements to which this Ruling applies. All Australian Securities and Investments 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

16. The salient features of the Port Robe Estate Vineyard Project Stage 3 are as follows:

Location	Mt Benson district, near Robe in South Australia
Type of Business	The growing and harvesting of wine producing grapes
Number of hectares in Project	75.45 hectares
Size of each Vigneron Lot	0.096ha
No. of vines per ha	178
Term of the Project	13 years
Minimum initial cost	\$9,390 per each Stapled Interest consisting of: <ul style="list-style-type: none"> • Vigneron Interest (\$7,370); • Vineyard Interest (\$770); and • Share Interest (\$1,250) of 2 shares in the Winemaker at \$625 per share.
Initial cost per hectare	\$76,770
Ongoing Fees	Management fees, Rent

17. The Project will be a registered Managed Investment Scheme under the *Corporations Act 2001*. Vision Capital Management Ltd will act as the Responsible Entity for the Project. Under the combined Product Disclosure Statement and Prospectus, Vision Capital Management Ltd will offer 786 interests called 'Vigneron Lots' of 0.096 hectares in size.

18. Vignerons who have their 'Applications' accepted during the period 1 October 2005 to 15 June 2006 will enter the Project as 2006 Planting Season Vignerons, post 30 September 2005. **This Ruling only applies in respect of these Post 30 September Vignerons.** Note that separate Product Rulings will issue for Vignerons who enter into the Project during the period up to 15 June 2005 and the period 1 July 2005 to 30 September 2005.

19. The Project involves the planting and cultivating of grapevines to be used in the production of wine. Produce from the vines will be harvested and sold by the Responsible Entity on behalf of the Vignerons in the Project.

20. The Project property has been purchased by Port Robe Management Ltd but pursuant to a Declaration of Trust, Port Robe Management Ltd holds a proportion of that part of the Vineyard Estate comprising the Vineyard on trust for the holders of the Vineyard Estate Interests.

21. Vignerons enter into a Vineyard Management and Lease Agreement with the Responsible Entity and Port Robe Management Ltd. Under the Vineyard Management and Lease Agreement, the Vigneron contracts with the Responsible Entity to establish and manage their Vigneron Lot.

22. Under an Exclusive Licence of Plant Breeders Rights, Port Robe Estate Ltd (The Winemaker) has obtained the rights to propagate the Cygne Blanc variety of grapes. The Winemaker has sub-licenced its Cygne Blanc rights to Port Robe Management Ltd (Project Manager) to allow the Project Manager to grow the variety on behalf of the Vignerons. Other varieties of red grapes may also be planted for the Project.

23. Vignerons will enter into a Grape Sale Agreement under which the Winemaker will purchase the grapes produced by the Vignerons and arrange for wine to be produced from the grapes. The Winemaker will then market the wines domestically and internationally.

24. The Term of the Project is for a minimum of 13 years.

25. Upon application, Vignerons will execute a Power of Attorney enabling Vision Capital Management Limited to act on their behalf.

Constitution

26. The Constitution sets out the terms and conditions under which the Responsible Entity agrees to act for the Vignerons and to manage the Project. Under the Constitution, each Vigneron shall have an interest in the relevant funds of the Project equal to their Proportional Interest. The Responsible Entity will keep a register of Vignerons, and Vignerons are entitled to assign their Interest in certain circumstances. Vignerons are bound by the Constitution by virtue of their participation in the Project.

27. No Vigneron has a right to withdraw from the Project and the Constitution places no obligation on the Responsible Entity to purchase, repurchase or buy-back a Vigneron Interest from a Vigneron.

28. The application monies payable by the Vignerons will be banked into an Application Fund created under the Constitution. These monies will be released from the trust account to the Responsible Entity when certain specified criteria have been met (clause 7).

Compliance Plan

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

Declaration of Trust

30. Port Robe Management Ltd will hold the legal title to the Vineyard Land. It will execute a Declaration of Trust whereby it will hold title to the Land as trustee for the Vignerons. Each Vigneron will have an undivided interest in the Land to the extent of 0.048 hectares for every Stapled Interest held.

Vineyard Management and Lease Agreement

31. A Vineyard Management and Lease Agreement will be entered into between the Responsible Entity, the Project Manager (Port Robe Management Ltd) and the Vigneron for each of the Vineyard Interests. The term of the Agreement is 13 years from the commencement date of the Agreement. Under the Agreement, Vignerons contract with the Responsible Entity to establish and maintain the vineyard and to harvest the grapes for the duration of the Project. The Responsible Entity will engage Port Robe Management Ltd as the Project Manager to provide the services on its behalf.

32. Vignerons will pay a fee on Application for capital expenditure and services to be carried out during the Initial Period of the Project. An annual management fee will be payable to the Responsible Entity for each year thereafter. Rent will be payable annually for each year following the Initial Period. The fees for Year 5 and subsequent years will be deducted from each Vigneron's share of the gross income from the Project. The Vignerons remain liable for these fees regardless of the income of the Project.

33. The services to be provided during the Initial Period up to 30 June 2006 include:

- (a) prepare Rootstock for planting on the Vigneron's Lots and prepare the Vigneron's Lots;
- (b) ensure and maintain that the Vigneron's Lots have adequate drainage and water resources, including dams, bores, pumps, filters, controllers, driplines and electrical connections;
- (c) ensure that appropriate expenditure is undertaken to maintain, as required, roads, shedding to house machinery, chemicals and staff amenities, and offices and accommodation where appropriate;
- (d) maintain all necessary fencing and firebreaks as and when required;
- (e) apply appropriate fertilisers as required;
- (f) process the Vigneron's Application and provide administrative services including the filing, reporting, printing, postage and handling of the Vigneron's documentation;
- (g) cause the Vigneron's Lot to be identified and allocated to the Vigneron, prepare all Agreements and documents to allow the Vigneron to occupy the Vigneron's Lot pursuant to this Agreement and ensure that all Vigneron's legal obligations under this Agreement are complied with;
- (h) administer the Vigneron's activities including obtaining all necessary approvals and consents required;
- (i) undertake all pest, fungicide control and vine disease measures as necessary including controlling rabbits and other vermin by fumigating and poisoning and complying with the provisions of all Statutes, Regulations and By-laws thereto and any other Statutes, Rules or Regulations relating to or affecting the Vigneron Lot or the Vigneron in respect thereof;
- (j) keep the Vigneron's Lots free from weeds and unwanted growth; and
- (k) effect and maintain insurance of all improvements and public liability insurance for an amount of at least \$5,000,000 in respect of any one claim.

34. The ongoing services that will be provided after the Initial Period include:

- (l) plant the Vigneron's Lots with Root Stock after all proper preparation of the Vignerons Lots;
- (m) ensure that adequate trellising is installed and maintained in good repair and condition;
- (n) use its best endeavours to conduct the Vigneron's activities in a commercial manner in keeping with accepted wine industry standards;
- (o) maintain all necessary fencing and firebreaks as and when required;
- (p) apply appropriate fertilisers as required;
- (q) provide administrative services including the filing, reporting, printing, postage and handling of the Vigneron's documentation;
- (r) undertake all pest, fungicide control and vine disease measures as necessary including controlling rabbits and other vermin by fumigating and poisoning and complying with the provisions of all Statutes, Regulations and By-laws thereto and any other Statutes, Rules or Regulations relating to or affecting the Vigneron Lot or the Vigneron in respect thereof;
- (s) keep the Vigneron's Lots free from weeds and unwanted growth; and
- (t) notify the Winemaker when the grapes are ready for harvest, have the grapes assessed by the Winemaker for compliance with the quality, quantity and contamination standards set out in the Grape Sale Agreement and harvest the grapes in accordance with the Grape Sale Agreement.

35. Under the terms of the Lease, the Vignerons agree they:

- will not use, or permit to be used, the Lot for a purpose other than commercial viticulture;
- will not use, or permit to be used, the Lot for residential, recreational or tourist purposes;
- must pay annual insurance premiums;
- shall keep the Lot in good and substantial repair; and
- must not install upon or remove anything from the Lot.

36. Not later than three months prior to the end of the project term, the Vignerons will collectively decide to either continue the Project under the management of the Responsible Entity or to sell the vineyard.

Harvesting and Sale

37. The Responsible Entity will be responsible for harvesting and selling the grapes to the Winemaker on the Vignerons' behalf.

38. The Responsible Entity will notify the Winemaker when the grapes are ready for harvest, have the grapes assessed by the Winemaker for compliance with the quality, quantity and contamination standards set out in the Grape Sale Agreement.

39. On behalf of the Vigneron, the Responsible Entity will collect all proceeds of sale of grapes made to the Winemaker in respect of the harvest of the grapes in accordance with the Grape Sale Agreement, and hold the proceeds until applied in accordance with the Constitution.

40. Grape sale proceeds and costs will be pooled. The Constitution provides that the gross proceeds are to be paid into a Proceeds Fund and that each Vigneron is entitled to their Proportional Interest in the Proceeds Fund.

Grape Sale Agreement

41. A Vigneron will enter into a Grape Sale Agreement with the Responsible Entity, the Project Manager and the Winemaker. Under the terms of the Agreement, Vignerons will sell their grapes to the Winemaker. The Winemaker will pay a commission on wine sales from the wine produced from the grapes grown on the Vigneron's Lot. The Grape Price and Wine Commission will be paid to the Responsible Entity by the Winemaker.

42. When purchasing the Vigneron's grapes, the Winemaker will agree to pay to the Vigneron the Grape Price as follows:

- For grapes of the Cygne Blanc variety – a price per tonne equal to 110% of the prevailing market price for premium chardonnay produced in the Limestone Coast Region of South Australia for the current vintage as published in the South Australian Winegrape Utilisation and Pricing Survey by the Phylloxera and Grape Industry Board of South Australia; and
- For grapes of other varieties – the average price per tonne for the particular variety equal to the prevailing market price of that variety produced in the Limestone Coast Region of South Australia for the current vintage as published in the South Australian Winegrape Utilisation and Pricing Survey by the Phylloxera and Grape Industry Board of South Australia.

43. Wine Commission is defined in this Agreement to mean '...an amount equivalent to 50% (or such other amount as the Winemaker and the Project Manager may agree from time to time) of the net profit made by the Winemaker on the wholesale selling price of wine produced from grapes'.

Exclusive Licence of Plant Breeders Rights

44. Pursuant to this Licence, Port Robe Estate Ltd has been granted an exclusive world wide licence to cultivate the Cygne Blanc grape variety on the Port Robe Estate Project land to produce and market wine made from the grapes. The licence permits Port Robe Estate Ltd to grant a sub-licence of its rights under the licence to Port Robe Management Ltd. The rights are exclusive and will be for the duration of the Project.

Port Robe Agreement

45. Under the terms of the Port Robe Agreement, Port Robe Estate Ltd grants to Port Robe Management Ltd an exclusive sub-licence of some of the rights under the exclusive licence to grow the Cygne Blanc grape variety on behalf of the Vignerons. Under this Agreement, the Vigneron is permitted to grow the Cygne Blanc grapes on their Lot. The sub-licence is granted for the same term as the exclusive licence pursuant to which the sub-licence is granted.

Vineyard Management Agreement

46. Under this agreement, the Project Manager will contract with Cape Jaffa Viticulture Pty Ltd to provide for the establishment and maintenance of the Project vineyard.

Fees

47. The subscription fee payable to Vision Capital Management Ltd on application is \$9,390. This fee consists of:

- **A Vigneron Interest** of \$7,370 for services to be provided in the establishment of the vineyard;
- **A Vineyard Estate Interest** of \$770 for a beneficial interest in the whole of the vineyard; and
- **A Share Interest** of \$1,250 for 2 ordinary shares in the Winemaker, Port Robe Estate Ltd.

48. The interest in the Project is a Stapled Interest and cannot be acquired separately. However applicants may hold the Vigneron Interest and the Vineyard Estate Interest components of the Stapled Interest under one individual or entity and apply for the Share Interest component under a different name.

49. The fee of \$7,370 for the Vigneron Interest consists of the following components:

- Establishment of grapevines \$768
- Irrigation \$893
- Trellising \$822
- Roads & Buildings \$226
- Vineyard Management \$4,661

50. A Vigneron may choose to pay the full subscription fee of \$9,390 on application or to make an initial payment of \$2,347.50 on application and then three equal payments of \$2,347.50 in each of the following three months. The payments will be made by direct debit.

51. Vignerons are required to pay annual ongoing **Management Fees** for each Vigneron Lot as follows:

Amount	Period ending	Date Payable
\$1980.00	30 June 2007	30 Nov 2006
\$1210.00	30 June 2008	30 Nov 2007
\$1210.00	30 June 2009	30 Nov 2008
\$1210.00	30 June 2010	30 Nov 2009
\$1416.80	30 June 2011	30 Nov 2010
Previous year indexed at 3%	30 June for each subsequent year	30 November of each year

52. **Rent** is payable annually for each Vigneron Lot as follows:

Amount	Period ending	Date Payable
\$110.00	30 June 2007	30 Nov 20056
\$110.00	30 June 2008	30 Nov 2007
\$110.00	30 June 2009	30 Nov 2008
\$110.00	30 June 2010	30 Nov 2009
\$128.70	30 June 2011	30 Nov 2010
Previous year indexed at 3%	30 June for each subsequent year	30 November of each year

Shares

53. Each Vigneron must also subscribe for 2 shares in the Winemaker, Port Robe Estate Ltd, for each Stapled Interest. The cost of each share is \$625 with \$1,250 payable on application.

Finance

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

55. This Ruling does not apply if a Vigneron enters into a finance agreement that includes or has any of the following features:

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' 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 terms are of a non-arm's length nature;
- repayments of the principal and 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) back to the lender or any associate;
- 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 for the Project.

Ruling

Application of this Ruling

56. This Ruling applies only to Vignerons who are accepted to participate in the Project during the period 1 October 2005 to 15 June 2006 and who have executed a Vineyard Management and Lease Agreement during this period.

57. A Vigneron's participation in the Project must constitute the carrying on of a business of primary production. A Vigneron is not eligible to claim any tax deductions until their application to enter the Project is accepted and the Project has commenced.

58. This Ruling does not apply to Vignerons who:

- are accepted to participate in the Project before the date the Ruling is made;

- have their application conditionally accepted by the Responsible Entity subject to finance for the payment of the initial fee, where the finance has not been approved by the lender by 15 June 2006 and the funds have not been made available to the Responsible Entity by 30 June 2006;
- are accepted to participate in the Project before 1 October 2005 or after 15 June 2006;
- intend to terminate their involvement in the arrangement prior to Project's completion; and
- do not intend to derive assessable income from the Project.

The Simplified Tax System ('STS')

Division 328

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

60. Changes to the STS rules apply from 1 July 2005. The question of whether a Vigneron is eligible to be an 'STS taxpayer' is outside the scope of this Product Ruling. Therefore, any Vigneron 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'.

25% Entrepreneurs Tax Offset

Subdivision 61-J

61. For the first income year starting on or after 1 July 2005, Subdivision 61-J of the ITAA 1997 provides for a tax offset of up to 25% 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

Sections 6-5, 328-105 and 44

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

63. Other than Vignerons referred to in paragraph 64, for the 2005-06 income year and later years, a Vigneron will be assessable on ordinary income from carrying on their business of viticulture in the income year in which that income is derived.

64. For the 2005-06 income year and later years, a Vigneron 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.

65. Dividends received from Port Robe Estate Ltd will be assessable income of the Vigneron under section 44.

Deductions for Management Fees and Rent

Section 8-1 and 328-105

66. A Vigneron may claim tax deductions for the following revenue expenses on a per Vigneron Lot basis:

Fee Type	ITAA 1997 Section	Year 1 Year ending 30 June 2006	Year 2 Year ending 30 June 2007	Year 3 Year ending 30 June 2008
Management Fee	8-1 & 328-105	See Notes (i), (ii) & (iii)	\$1,980 See Notes (i), (iv) & (v)	\$1,210 See Notes (i), (iv) & (v)
Rent	8-1 & 328-105	Nil	\$110 See Notes (i), (iv) & (v)	\$110 See Notes (i), (iv) & (v)

Notes:

- (i) If the Vigneron 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 the Example at paragraph 124.
- (ii) For the 2005-06 income year, the Management Fees and Rent shown in the Vineyard Management and Lease Agreement are deductible in full in the year they are incurred where the Vigneron is **not an STS taxpayer or is an STS taxpayer using the accruals accounting method** or in the year in which they are paid where the Vigneron is **an STS taxpayer using the cash accounting method**. Accordingly, where the Vigneron is **not an 'STS taxpayer' or is an STS taxpayer using the accruals accounting method**, the Initial Vineyard Management Fee of \$4,661 will be deductible in Year 1, as it will be incurred in this year.

- (iii) If a Vigneron who is an **'STS taxpayer' using the cash accounting method** chooses to pay the Initial Management Fee in full on application, then this amount will be fully paid in the year in which it is incurred. Therefore, the Initial Vineyard Management Fee of \$4,661 will be deductible in Year 1 as it is fully paid in the year in which it is incurred.

However, if a Vigneron who is an **'STS taxpayer' using the cash accounting method** chooses to pay the Initial Vineyard Management Fee of \$4661 over four payments, then the amount described above may not be fully paid in the year in which it is incurred. For STS taxpayers using the cash accounting method, the Management Fee is only deductible to the extent to which it has been paid, or has been paid for the Vigneron. Any amount, or part of an amount, which is not paid in the year in which it is incurred will be deductible in the year in which it is actually paid (paragraph 328-105(1)(b)).

- (iv) For the 2006-07 income year and later years, where a Vigneron pays the Management Fees and Rent in the relevant income years shown in the Vineyard Management and Lease Agreement, those fees are deductible in full in the year that they are incurred where the Vigneron is **not an STS taxpayer or is an STS taxpayer using the accruals accounting method** or in the year that they are paid where the Vigneron is **an STS taxpayer or is an STS taxpayer using the cash accounting method**.
- (v) If a Vigneron **chooses** to prepay fees for the doing of a thing (for example the provision of management services or the leasing of land) that will not be wholly done in the income year the fees are incurred, the prepayment rules of the ITAA may apply to apportion those fees (see paragraphs 96 to 103). In such cases, the tax deduction for the prepaid fee must be determined using the formula shown in paragraph 102, unless the expenditure is 'excluded expenditure'. 'Excluded expenditure' is an 'exception' to the prepayment rules, and is deductible in full in the year in which it is incurred. For the purpose of this Ruling 'excluded expenditure' refers to an amount of expenditure of less than \$1,000.

Deductions for capital expenditure***Non-STs taxpayers******Division 40***

67. A Vigneron who is not an 'STs taxpayer' will be entitled to tax deductions relating to trellising, irrigation and the establishment and decline in value of the grapevines and capital works. All deductions shown in the following Table are determined under Divisions 40 and 43.

Fee Type	ITAA 1997 Section	Year 1 Year ending 30 June 2006	Year 2 Year ending 30 June 2007	Year 3 Year ending 30 June 2008
Trellising	40-25	Nil See Notes (vi) & (vii)	Must be calculated See Notes (vi) & (vii)	Must be calculated See Notes (vi) & (vii)
Irrigation	40-515	\$298 See Notes (vi) & (viii)	\$298 See Notes (vi) & (viii)	\$297 See Notes (vi) & (viii)
Establishment of Grapevines	40-515	Nil	Nil	Must be calculated See Notes (vi) & (ix)
Roads & Buildings	43-10	Nil	Must be calculated See Notes (vi) & (x)	Must be calculated See Notes (vi) & (x)

Notes:

- (vi) If the Vigneron 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 at paragraph 124).
- (vii) Trellising meets the definition of a 'depreciating asset' in section 40-30 and therefore each Vigneron's interest in the trellising is a 'depreciating asset'. The 'cost' of the asset is the amount paid by the Vigneron. The decline in value of the asset is calculated using the formula in either subsection 40-70(1) ('diminishing value method') or subsection 40-75(1) ('prime cost method'). Both formulas rely on the 'effective life' of the trellising.

Vignerons can either self-assess the 'effective life' (section 40-105) or use the Commissioner's determination of 'effective life' (section 40-100). The Commissioner has determined that trellising has an 'effective life' of 20 years. For Vignerons who enter the Project during the period 1 October 2005 to 15 June 2006, the trellising will be installed and first used during the year ended 30 June 2007.

For a Vigneron who purchases the minimum allocation of one Vineyard Lot in this Project, their interest in the trellising will be a 'low cost asset' that is, an asset costing less than \$1,000. A 'low-cost asset' can be allocated to a 'low-value pool'. Once any 'low-cost asset' of a Vigneron is allocated to a 'low-value pool', all other 'low-cost assets' the Vigneron starts to 'hold' in that year or a later year must be allocated to that pool. If the Vigneron has already allocated an asset to a 'low-value pool', the trellising would also have to be allocated to that pool. Otherwise, the Vigneron must decide whether to create a 'low-value pool'.

If the asset is allocated to a 'low-value pool', the capital expenditure on the trellising will be deducted under the diminishing value methodology of the pool based on a rate of 18.75% in the year the trellising is first used and a rate of 37.5% in subsequent years (section 40-440). If the trellising is not allocated to a 'low-value pool', it can be written off based on the 'effective life' of the asset.

- (viii) 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 for water facilities is available under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one third of the capital expenditure of \$893 incurred by each Vigneron 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).
- (ix) Grapevines are a 'horticultural plant' as defined in subsection 40-520(2). As Vignerons hold the land under a lease, 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 Grapevines is determined using the formula in section 40-545 and is based on the capital expenditure incurred by the Vigneron that is attributable to their establishment. If the Grapevines 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% per annum. The deduction is allowable when the Grapevines enter their first commercial season (section 40-530, item 2). The Responsible Entity will inform Vignerons of when the Grapevines enter their first commercial season.

- (x) A deduction is available for expenditure incurred on the construction of buildings and roads for use in the vineyard business. Where the expenditure is incurred in relation to a construction expenditure area (section 43-10), it may be written off at 2.5% per annum from the date the relevant construction is completed. The Responsible Entity will inform Vignerons of when the construction has been completed.

STS taxpayers*Division 328 and Subdivision 40-F*

68. A Vigneron who is an 'STS taxpayer' will also be entitled to tax deductions relating to trellising, irrigation, the establishment and decline in value of the grapevines and capital works.

69. Trellising meets the definition of a 'depreciating asset' and deductions relating to the 'cost' of trellising must be determined under Division 328. 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 Vigneron 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.

70. An 'STS taxpayer' may claim deductions in relation to irrigation under Subdivision 40-F because irrigation meets the definition of a 'water facility'. As expenditure on irrigation would also meet the definition of a 'depreciating asset', an 'STS taxpayer' may choose to claim deductions under Division 328.

71. Deductions for the Grapevines must be determined under Subdivision 40-F.

72. Deductions for capital write-off for buildings and roads must be determined under Division 43.

73. The deductions shown in the following Table assume, for representative purposes only, the Vigneron has one interest in the Project and has chosen to claim deductions for expenditure on irrigation under Division 328 and not under Subdivision 40F. If the expenditure is claimed under Division 328, the deduction is determined as discussed in Note (xii) below.

Fee Type	ITAA 1997 Section	Year 1 Year ending 30 June 2006	Year 2 Year ending 30 June 2007	Year 3 Year ending 30 June 2008
Trellising	Subdivision 328-D	Nil See Notes (vi) & (xi)	\$822 See Notes (vi) & (xi)	Nil See Notes (vi) & (xi)
Irrigation	Subdivision 328-D	\$893 See Notes (vi) & (xii)	Nil See Notes (vi) & (xii)	Nil See Notes (vi) & (xii)
Establishment of Grapevines	40-515	Nil See Notes (vi) & (ix)	Nil See Notes (vi) & (ix)	Must be calculated See Notes (vi) & (ix)
Roads and Buildings	43-10	Nil	Must be calculated See Notes (vi) & (x)	Must be calculated See Notes (vi) & (x)

Notes:

- (xi) Trellising is a 'depreciating asset'. Each Vigneron's interest in the trellising is a 'depreciating asset' under section 40-30. Where a Vigneron acquires only one Vigneron Lot, the Vigneron's interest in the trellising is a 'low-cost asset' as defined in subsection 40-525(2). 'Low cost assets' cannot be allocated to a 'general STS pool' (section 328-180). A deduction equal to the amount of the Vigneron's expenditure for the trellising is available in the income year in which it is first used or 'installed ready for use'. This is so provided the Vigneron 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.

Where a Vigneron acquires **two or more Interests**, the Vigneron's interest in the trellising will not be a 'low cost asset' as the cost will be \$1,000 or greater. For these Vignerons, their interest in the trellising is a 'depreciating asset' that can be allocated to a 'general STS pool'. The 'cost' of the asset is the amount paid by each Vigneron.

For trellising allocated to a 'general STS pool' the tax deduction allowable is determined in the year ended 30 June 2007 by multiplying the 'cost' of the interest by half the 'general STS pool rate, that is, by 15%. Each Vigneron's interest in the trellising is allocated to their 'general STS pool' at the end of the financial year ended 30 June 2007 and that part of the 'cost' not deducted in the first year is added to the pool balance. In subsequent years, the full pool rate of 30% will apply.

- (xii) 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 Vigneron may choose to claim a deduction under either Division 328 or Subdivision 40-F.

For the purposes of Division 328, each Vigneron'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 \$1000, 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 Vigneron 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 2006 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 the Vigneron chooses to use Subdivision 40-F, the deductions are claimed under Subdivision 40-F, paragraph 40-515(1)(a). The deduction is equal to one third of the capital expenditure incurred by each Vigneron 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).

Tax outcomes that apply to all Vignerons

74. The deductibility or otherwise of interest incurred by Vignerons 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 Vignerons who borrow funds in order to participate in the Project should read the discussion of the prepayment rules in paragraphs 96 to 103 (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 Vigneron's choice.

Shares and Vineyard Estate Interest

75. The shares in Port Robe Estate Ltd and the interest in the vineyard land are CGT assets (section 108-5 of the ITAA 1997) and the amounts paid by a Vigneron to acquire the shares and the vineyard interest are an outgoing of capital and not allowable as a deduction.

76. The amounts paid for the vineyard estate interest and each share will represent the first element of the cost base of the share (subsection 110-25(2)). Any disposal of the shares or the interest in the vineyard land by a Vigneron will be a CGT event and may give rise to a capital gain or loss.

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

77. A Vigneron who is an individual and is accepted into the Project during the year ended 30 June 2006 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 Vignerons for the income years **30 June 2006 to 30 June 2010**. This conditional exercise of the discretion will allow those losses to be offset against the Vigneron's other assessable income in the income year in which the losses arise.

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

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

- expenditure by a Vigneron does not fall within the scope of sections 82KZME to 82KZMF (but see paragraphs 96 to 103);

- 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 Vigneron carrying on a business?

79. For the amounts set out in the Tables above to constitute allowable deductions, the Vigneron's viticulture activities as a participant in the Port Robe Estate Vineyard Project Stage 3 must amount to the carrying on of a business of primary production. These viticulture activities will fall within the definitions of 'viticulture' and 'commercial viticulture' in section 40-535 of the ITAA 1997.

80. For schemes such as that of the Port Robe Estate Vineyard Project Stage 3, Taxation Ruling TR 2000/8 sets out in paragraph 89 the circumstances in which the Vigneron'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* (1984) 6 FCR 202; 84 ATC 4929, (1984) 16 ATR 932.

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

- the Vigneron has an identifiable interest in the land (by lease) or holds rights over the land (under a licence) on which the Vigneron's grapevines are established;
- the Vigneron has a right to harvest and sell the grapes each year from those grapevines;
- the viticulture activities are carried out on the Vigneron's behalf;
- the viticulture activities of the Vigneron 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.

82. In this Project, each Vigneron enters into a Vineyard Management and Lease Agreement.

83. Under the Lease, each individual Vigneron will have rights over a specific and identifiable area of land (Vigneron's Lots). The Lease provides the Vigneron with an ongoing interest in the specific grapevines on the Vigneron Lots for the term of the Project. Under the Lease the Vigneron must use the Lots in question for the purpose of carrying out viticultural activities and for no other purpose. The Lease allows the Responsible Entity to come onto the land to carry out its obligations under the Vineyard Management and Lease Agreement.

84. Under the Vineyard Management and Lease Agreement the Responsible Entity is engaged by the Vigneron to maintain the grapevines on the Vigneron's Lots during the term of the Project. The Responsible Entity will subcontract the management services to the Project Manager under the Vineyard Management and Lease Agreement. The Project Manager has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to maintain the Lot on the Vigneron's behalf.

85. The Vigneron engages the Responsible Entity to maintain the grapevines on the Lots according to the principles of sound viticultural practice which includes irrigation, fertilisation, weed control and pruning. The Responsible Entity is also engaged to harvest and sell, on the Vigneron's behalf, the grapes grown on the Vigneron's Lot.

86. 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.

87. The activities that will be regularly carried out during the term of the Project demonstrate a significant commercial purpose. Based on reasonable forecasts, a Vigneron in the Project may derive assessable income from the sale of its grapes that may 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.

88. The pooling of grapes grown on the Vigneron's Lot with the grapes of other Vignerons is consistent with general viticulture practices. Each Vigneron's proportionate share of the sale proceeds of the pooled grapes will reflect the proportion of the grapes contributed from their Lot.

89. The Responsible Entity's services are consistent with general viticulture practices. While the size of a Lot is relatively small, it is of a size and scale to allow it to be commercially viable.

90. The Vigneron's degree of control over the Responsible Entity as evidenced by the Management Agreement, and supplemented by the *Corporations Act 2001*, is sufficient. During the term of the Project, the Responsible Entity will provide the Vigneron with regular progress reports on the Vigneron's Grove and the activities carried out on the Vigneron's behalf. Vignerons are able to terminate arrangements with the Responsible Entity in certain instances, such as cases of default or neglect.

91. 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 Vignerons' viticulture activities in the Port Robe Estate Vineyard Project Stage 3 will constitute the carrying on of a business.

The Simplified Tax System

Division 328

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

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

Deductibility of Management Fees and Rent

Section 8-1

94. Consideration of whether the initial Management Fees, other than the amounts for capital expenditure, and Rent are deductible under section 8-1 begins with the first limb of the section. This view proceeds on the following basis:

- the outgoing in question must have a sufficient connection with the operations or activities that directly gain or produce the taxpayer's assessable income;
- the outgoings are not deductible under the second limb if they are incurred when the business has not commenced; and
- where all that happens in a year of income is that a taxpayer is contractually committed to a venture that may not turn out to be a business, there can be doubt about whether the relevant business has commenced, and hence, whether the second limb applies. However, that does not preclude the application of the first limb in determining whether the outgoing in question has a sufficient connection with activities to produce assessable income.

95. The Management Fees and Rent associated with the viticulture activities will relate to the gaining of income from the Vigneron's business of viticulture, and hence have a sufficient connection to the operations by which income (from the regular sale of fruit) 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. 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

96. 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.

97. 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 STS taxpayers from the operation of section 82KZMF.

Sections 82KZME and 82KZMF

98. 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)).

99. 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;

PR 2005/81

- 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.

100. 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 Vigneron in this Project who, in order to participate in the Project may borrow funds from a financier that is not associated with the Project. Although undertaken with an unrelated party, that financing would be an element of the arrangement. The funds borrowed and any interest incurred is directly related to the activities under the arrangement. If a Vigneron prepays interest under such financing arrangements, any interest deductions allowable will be subject to apportionment under section 82KZMF.

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

102. 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.

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

103. 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

104. In this Project, an initial Management Fee of \$4,661 per Lot will be incurred on the execution of the Vineyard Management and Lease Agreement. The Management Fee is charged for providing management services to a Vigneron by 30 June of the year of execution of the Agreement. Under the Agreement further annual expenditure is required each year during the term of the Project for the provision of management services until 30 June in those years.

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

106. There is also no evidence that might suggest the management services covered by the fee could not be provided within the relevant expenditure year. Thus, for the purposes of this Ruling, it can be accepted that no part of the initial management fee, and the fees for subsequent years, is for the Responsible Entity doing 'things' that are not to be wholly done within the expenditure year. Under the Lease, Rent is payable annually for the lease of the land during the expenditure year.

107. On this basis, provided a Vigneron incurs expenditure as required under the Project agreements, as set out in paragraphs 47 to 52, then the basic precondition in subsection 82KZME(2) is not satisfied and, in these circumstances, section 82KZMF will have no application.

108. A Vigneron who is an 'STS taxpayer' and uses the cash accounting method can, therefore, claim an immediate deduction for each of the relevant fees in the income year in which the fee is paid. A Vigneron who is not an 'STS taxpayer' using the cash accounting method can claim an immediate deduction for each of the relevant fees in the income year in which the fee is incurred.

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

109. Although not required under the Vineyard Management and Lease Agreement, a Vigneron participating in the Project may **choose** to prepay fees for a period beyond the 'expenditure year'. Similarly, Vignerons who use financiers may either choose, or be required to prepay interest. Where this occurs, contrary to the conclusion reached in paragraph 107, section 82KZMF will apply to apportion the expenditure and allow a deduction over the period in which the prepaid benefits are provided.

110. For these Vignerons, the amount and timing of deductions for any relevant prepaid management fees, prepaid rent, or prepaid interest will depend upon when the respective amounts are incurred and what the 'eligible service period' is in relation to these amounts.

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

Expenditure of a capital nature

112. Any part of the expenditure of a Vigneron 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 water facilities, trellising, roads and buildings and the establishment of the grapevines is of a capital nature. This expenditure falls for consideration under Division 40, Division 43 or Division 328 of the ITAA 1997.

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

114. The tax treatment of capital expenditure has been dealt with in a representative way in paragraphs 67 and 73 (above) in the Tables and accompanying notes.

Interest deductibility

115. The deductibility of interest incurred by Vignerons who finance their participation in the Project through a loan facility with a bank or financier is outside the scope of this Ruling. Product Rulings only deal with arrangements where all details and documentation have been provided to, and examined by, the Tax Office.

116. While the terms of any finance agreement entered into between relevant Vignerons and such financiers are subject to commercial negotiation, those agreements may require interest to be prepaid. Alternatively, a Vigneron may choose to prepay such interest. Unless such prepaid interest is 'excluded expenditure', any tax deduction that is allowable will be subject to the relevant prepayments provisions of the ITAA 1936 (see paragraphs 96 to 103).

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

Section 35-55 – exercise of Commissioner's discretion

117. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income years **30 June 2006 to 30 June 2010** 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 2006 up to and including 30 June 2010:

- it is because of its nature the business activity of a Vigneron that will not satisfy one of the four tests in Division 35; and
- there is an objective expectation that within a period that is commercially viable for the horticultural industry, a Vigneron's business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

118. Therefore, a Vigneron 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.

119. 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 Vigneron will need to apply for a private ruling on the application of section 35-55 to those changed circumstances.

Section 82KL – recouped expenditure

120. The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefit(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

121. 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).

122. The Port Robe Estate Vineyard Project Stage 3 will be a 'scheme' commencing with the issue of the combined Product Disclosure Statement and Prospectus. A Vigneron will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 66, 67 and 73 that would not have been obtained but for the scheme. However, it is not possible to conclude that the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

123. Vignerons 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 their grapes. There are no facts that would suggest that Vignerons have the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There are no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing with each other at arm's length, or, if any parties are not at arm's length, that any adverse tax consequences result. Further, having regard to the factors to be considered under paragraph 177D(b) it cannot be concluded, on the information available, that participants will enter into the scheme for the dominant purpose of obtaining a tax benefit.

Example

Entitlement to GST input tax credits

124. 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 2003, 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 1/1/2004 to 30/6/2004	\$4,400*
Carrying out of upgrade of power for your vineyard as quoted	<u>\$2,200*</u>
Total due and payable by 1 January 2004 (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 2004, 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).

Detailed contents list

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

	Paragraph
What this Product Ruling is about	1
Tax law(s)	2
Goods and Services Tax	3
Changes in the Law	4
Note to promoters and advisers	6
Class of persons	7
Qualifications	9
Date of effect	11
Withdrawal	13
Arrangement	14
Overview	16
Constitution	26
Compliance Plan	29
Declaration of Trust	30
Vineyard Management and Lease Agreement	31
Harvesting and Sale	37
Grape Sale Agreement	41
Exclusive Licence of Plant Breeders Rights	44
Port Robe Agreement	45
Vineyard Management Agreement	46
Fees	47
Shares	53
Finance	54
Ruling	56
Application of this Ruling	56

The Simplified Tax System ('STS')	59
<i>Division 328</i>	59
25% Entrepreneurs Tax Offset	61
<i>Subdivision 61-J</i>	61
Assessable income	62
<i>Sections 6-5, 328-105 and 44</i>	62
Deductions for Management Fees and Rent	66
<i>Sections 8-1 and 328-105</i>	66
Deductions for capital expenditure	67
<i>Non-STS taxpayers</i>	67
<i>Division 40</i>	67
<i>STS taxpayers</i>	68
<i>Division 328 and Subdivision 40-F</i>	68
Tax outcomes that apply to all Vignerons	74
Shares and Vineyard Estate Interest	75
Division 35 – deferral of losses from non-commercial business activities	77
<i>Section 35-55 – exercise of Commissioner's discretion</i>	77
<i>Sections 82KZME, 82KZMF and 82KL and Part IVA</i>	78
Explanation	79
Is the Vigneron carrying on a business?	79
The Simplified Tax System	92
<i>Division 328</i>	92
Deductibility of Management Fees and Rent	94
<i>Section 8-1</i>	94
Prepayments provisions	96
<i>Sections 82KZL to 82KZMF</i>	96
<i>Sections 82KME and 82KZMF</i>	98
<i>Application of the prepayment provisions to this Project</i>	104
<i>Vignerons who <u>choose</u> to pay fees for a period in excess of that required by the Project's agreements</i>	109
Expenditure of a capital nature	112
Interest deductibility	115
Division 35 – deferral of losses from non-commercial business activities	117
<i>Section 35-55 – exercise of Commissioner's discretion</i>	117

Section 82KL – recouped expenditure	121
Part IVA	121
Example	124
Entitlement to GST input tax credits	124
Detailed contents list	125

Commissioner of Taxation

25 May 2005

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

PR 1999/95; TR 92/1; TR 92/20;
 TR 97/11; TR 97/16; TR 98/22;
 TR 2000/8; TR 2001/14;
 TD 93/34

Subject references:

- carrying on a business
- commencement of business
- management fee expenses
- non-commercial loss
- primary production
- primary production expenses
- producing assessable income
- product rulings
- public rulings
- schemes and shams
- taxation administration
- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters

Legislative references:

- ITAA 1936 44
- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
- ITAA 1936 82KZMD
- ITAA 1936 82KZME
- ITAA 1936 82KZME(1)
- ITAA 1936 82KZME(2)
- ITAA 1936 82KZME(3)

- ITAA 1936 82KZME(4)
- ITAA 1936 82KZME(7)
- ITAA 1936 82KZMF
- ITAA 1936 82KZMF(1)
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)
- 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 35-55
- ITAA 1997 35-55(1)(b)
- ITAA 1997 Div 40
- ITAA 1997 40-25
- ITAA 1997 40-30
- ITAA 1997 40-70(1)
- ITAA 1997 40-75(1)
- ITAA 1997 40-100
- ITAA 1997 40-105
- ITAA 1997 40-440
- ITAA 1997 Subdiv 40-F
- ITAA 1997 40-515
- ITAA 1997 40-515(1)(a)
- ITAA 1997 40-515(1)(b)
- ITAA 1997 40-520(1)
- ITAA 1997 40-520(2)
- ITAA 1997 40-525(2)
- ITAA 1997 40-530
- ITAA 1997 40-535
- ITAA 1997 40-540
- ITAA 1997 40-545
- ITAA 1997 Div 43
- ITAA 1997 43-10
- ITAA 1997 Subdiv 61-J
- ITAA 1997 Div 108
- ITAA 1997 108-5
- ITAA 1997 Div 110

PR 2005/81

- ITAA 1997 110-25(2)
 - ITAA 1997 Div 328
 - ITAA 1997 328-105
 - ITAA 1997 328-105(1)(b)
 - ITAA 1997 Subdiv 328-D
 - ITAA 1997 328-180
 - ITAA 1997 Subdiv 328-F
 - ITAA 1997 Subdiv 328-G
 - TAA 1953 Pt IVAAA
-

- Copyright Act 1968
- Corporations Act 2001

Case references:

- FCT v. Lau (1984) 6 FCR 202;
84 ATC 4929; (1984) 16 ATR 932

ATO references:

NO: 2005/7463

ISSN: 1441-1172

ATOlaw topic: Income Tax ~~ Product Ruling ~~ vineyards & wineries