



PR 2005/92 - Income tax: Film Investment - McLeod's Daughters Investment 2005

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 This document has changed over time. This is a consolidated version of the ruling which was published on *8 June 2005*



Product Ruling

Income tax: Film Investment – McLeod’s Daughters Investment 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 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 referred to as 'the Investment', 'the Program', 'the Project' or 'the arrangement'.

Tax law(s)

2. The tax laws dealt with in this Ruling are:

- section 8-1 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- Division 27 of the ITAA 1997;
- Division 40 of the ITAA 1997;
- section 995-1 of the ITAA 1997;
- section 79D of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 82KL of the ITAA 1936;
- Division 5 of Part III of the ITAA 1936;
- Division 10B of Part III of the ITAA 1936; and
- Part IVA of the ITAA 1936.

Unless otherwise stated, all legislative references that follow are in relation to the ITAA 1936.

Goods and Services Tax

3. In this Ruling, where applicable, all fees and expenditure referred to include Goods and Services Tax (GST) set out in the *A New Tax System (Goods and Services Tax) Act 1999* (GST ACT). An entity is entitled to claim input tax credits for the GST included in its expenditure provided that the acquisition is a creditable acquisition under Division 11 of the GST Act.

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 produced films 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 those persons 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 agreement until their term expires), and deriving assessable income from this involvement as set out in the description of the arrangement. In this Ruling, each of these persons, referred to as 'Investors', will be wholesale clients for the purpose of the *Corporations Act 2001* (refer to paragraphs 69 to 73).

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, who otherwise do not intend to derive assessable income from it or are non-residents of Australia for the purposes of the ITAA 1936 or ITAA 1997.

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. This work 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 8 June 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 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 2006. 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 persons' involvement in the arrangement.

Arrangement

14. The arrangement is the McLeod's Daughters Investment 2005 and is described below. This arrangement incorporates the following documents:

- Application for a Product Ruling dated 1 March 2005 as constituted by documents provided on 2, 11, 14, 15 March 2005, 13, 18 April 2005, 3, 9, 10, 13 and 18 May 2005 and additional correspondence from the Applicant (or Applicant's representative) dated 4, 14, 15 March 2005, 11, 13, 14, 18 April 2005, 2, 6, 10, 12, 13, 18, 24 and 30 May 2005;
- Correspondence from the Tax Office to the Applicant (or Applicant's representative) dated 3, 7 March 2005, 5, 14, 15 April 2005, 16 and 27 May 2005;

- Draft Information Memorandum for the McLeod's Daughters 2005 Investment to be issued by sixteenby9 Film & Television Pty Ltd (the 'Applicant' and 'Issuer'), received by the Tax Office on 13 May 2005;
- Draft **Investor Agent Agreement**, each of which is between Christopher Coote & Co Pty Ltd (the 'Agent') and an Investor, received by the Tax Office on 3 May 2005;
- Letter from the Agent to the Issuer, accepting appointment to act as Agent for Investors, dated 1 March 2005 and received by the Tax Office on 13 May 2005;
- Draft **Investor Acquisition Agreement** between Millennium Pictures Pty Ltd ('Producer'), the Agent, and each Investor, received by the Tax Office on 13 May 2005;
- Draft **FTA Licence Agreement** between Nine Network Australia Pty Ltd (the 'FTA Licensee'), the Producer, the Agent, and each Investor, received by the Tax Office on 13 May 2005;
- Draft **Investor Distribution Agreement** between Nine Films & Television Pty Ltd (the 'Distributor' or 'NFT'), Nine Network Australia Pty Ltd ('NNA'), the Agent, and each Investor, received by the Tax Office on 13 May 2005;
- Draft NFT Acquisition Agreement between the Producer and NFT, received by the Tax Office on 18 May 2005;
- Draft Producer Distribution Agreement between the Producer and NFT, received by the Tax Office on 18 May 2005;
- Draft NTF Licence Agreement between NFT as the Licensor and NNA as Licensee, received by the Tax Office on 13 May 2005;
- Draft Sub-Distribution Agreement between NFT, the Producer, the Sub-Distributor ('Sub-Distributor') and others, received by the Tax Office on 2 March 2005;
- Draft Pay Television Licence, between the Sub-Distributor and the Pay Television Licensee ('PTL'), received by the Tax Office on 13 May 2005;
- Draft Pre-committed Third Party Production & Investment Agreement between the Producer and the Pre-committed Third Party ('PCTP'), received by the Tax Office on 9 May 2005;
- Draft Pre-committed Third Party Distribution Agreement between the Distributor and the PCTP, received by the Tax Office on 9 May 2005; and

- Certificates under subsection 124K(1) of the ITAA 1936, received by the Tax Office on 11 March 2005.

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

15. In accordance with the above documents, an Investor who participates in the arrangement must be a wholesale client as defined in section 761G of the *Corporations Act 2001*. A wholesale client is explained in paragraphs 69 to 73 in the Explanation area of this Product Ruling.

16. The documents highlighted are those that the Investors enter into. There are no other agreements, whether formal or informal, and whether or not legally enforceable, which an Investor, or an associate of the Investor will be a party to that are part of the arrangement to which this Ruling applies. The effect of the agreements is summarised as follows.

The Participants

17. The parties involved in the arrangement are:

- **Investor:** A person, being a wholesale client, who incurs capital expenditure in acquiring an interest in the Program Copyright. An investor will licence their interest in the Program Copyright to NNA and NFT for a period of 7 years in return for the payment of licence fees.
- **Applicant and Issuer:** sixteenby9 Film & Television Pty Ltd ('sixteenby9') is the Applicant who applied for the Product Ruling. sixteenby9 is the Issuer of the Information Memorandum to the Investors.
- **Agent:** Christopher Coote & Co Pty Ltd, under the Investor Agent Agreement will be appointed by each of the Investors as their attorney to execute the Investor Acquisition Agreement and the Investor Distribution Agreement.
- **Producer:** Millennium Pictures Pty Ltd has the obligation to produce the Program under the Investor Acquisition Agreement.
- **Distributor or NFT:** Nine Films & Television Pty Limited ('NFT') will receive a licence from the Investors under the Investor Distribution Agreement to distribute the Program worldwide (excluding the rights granted under the FTA Licence Agreement). NFT will provide a distribution guarantee of 49.5% (inclusive of GST) of the Investment to Investors. NFT will licence its Free Television Rights in the Australian Territory to NNA under the NFT Licence Agreement and NFT will licence certain worldwide rights to the Sub-Distributor.

- **NNA:** Nine Network Australia Pty Ltd will guarantee the performance of the Distributor's payment obligations under the Investor Distribution Agreement. NNA receives a licence from the Investors for the Australian Territory Free Television Rights in the Program in return for licence fees. NNA also receives a licence from the Distributor for the Australian Territory Free Television Rights.
- **Pre-committed Third Party ('PCTP'):** Will contribute a set amount towards each of the 38 Episodes in McLeod's Daughters – Series 5 for the purchase of an interest in the Program Copyright. PCTP will licence their interest in the Program Copyright to the Distributor in return for a share of the Gross Receipts.
- **Sub-Distributor:** The Sub-Distributor will receive certain rights from the Distributor to distribute the Program worldwide. The Sub-Distributor will enter into the Pay Television licence with PTL.
- **PTL:** The PTL will receive a licence for certain pay television rights from the Sub-Distributor under the Pay Television Licence.

Defined terms

18. Terms which have been defined within the relevant documents to the arrangement include the following:

- **Application** means an application by a wholesale client (as defined under the Corporation Act) for an Investment.
- **Application Fee** means an amount equal to 0.11% of each Investor's Investment Amount payable by each Investor towards the Agent's fees.
- **Australian Territory** means Australia and Papua New Guinea.
- **Available Copyright Interest** means 93% of the Copyright Interest.
- **Budget** means the budget for the production of the Program (including all above-the-line and below-the-line items) approved by the Producer, NFT and the PCTP.
- **Budgeted Cost** means the amount agreed by the Producer, NFT and the PCTP as the amount budgeted for the production of the Program, being \$545,655 per Episode.

- **Copyright** means:
 - (a) copyright arising under the *Copyright Act 1968* (Cth);
 - (b) copyright under the law of a country other than Australia; and
 - (c) rights in the nature of or analogous to the rights described in paragraphs (a) and (b) according to the law of any country.
- **Copyright Interest** means all existing and future copyright subsisting in the cinematographic film in the Program, strictly limited to the Copyright Term.
- **Copyright Term** for Investors means the 7 year period commencing 30 June 2005 and ending on 30 June 2012.
- **Episode** means each commercial hour episode of the Program.
- **Equity Participant** means each person (excluding each Investor as defined under and for the purposes of the Investor Acquisition Agreement) who pays a contribution to the Producer in respect of the Budgeted Cost (including the PCTP and NFT).
- **Excluded Rights** means the following exclusive rights:
 - (a) all rights in the Program Copyright, the Title, the script and the original music and any other works created for the production of the Program, to make any remake, sequel or spin-off and to authorise others to exercise these rights in relation to any remake, sequel or spin-off;
 - (b) the right to make cinematograph films about the production of the Program; and
 - (c) all rights in the Program assets.
- **FTA Licence Fee** means the amount payable by NNA under the FTA Licence Agreement in respect of the exploitation of the Free Television Rights in the Program in the Australian Territory, being an amount of \$346,500 per Episode.
- **Foreign Gross Receipts** means all non-returnable amounts which are received by NFT from the distribution of the Program in the Territory (excluding the Australian Territory) less any withholding tax.

- **Free Television Rights** means each of the following rights:
 - (a) the right to broadcast on the terrestrial spectrum by any manner of audiovisual transmission whether now known or hereafter devised and (including without limitation, all forms and means of broadcast, narrowcast, multipoint, point to point and on-line service audiovisual transmission);
 - (b) the right to contemporaneously retransmit without alteration a broadcast made in the manner described in paragraph (a) by cable, MDS, satellite or any other system or technology; and
 - (c) the right to sub-licence any of the rights described in paragraphs (a) and (b) above,and the promotional rights for each such right.
- **Gross Receipts** means:
 - (a) all non-returnable amounts which are received by NFT from the distribution of the Program in the Territory (excluding the FTA Licence Fee and, for the avoidance of doubt, the Excluded Rights receipts) less any withholding tax;
 - (b) advances, guarantees, security deposits, awards, subsidies, levies and other allowances received by any person relating to the Program or the distribution of the Program;
 - (c) amounts obtained from or in connection with any claim by any person relating to the Program Copyright, the underlying rights or the distribution of the Program;
 - (d) amounts received from exploitation of marketing materials by any person relating to the Program Copyright, the underlying rights or the distribution of the Program;
 - (e) amounts obtained from export marketing and export expansion grants and schemes from any person relating to sales expenses and marketing expenses; and
 - (f) amounts received by any person from the exploitation of the collection societies rights,but excluding for the avoidance of doubt, any amounts received from the distribution of Gross Receipts (including, without limitation any amounts received from NNA in respect of the exploitation of the Free Television Rights in Australia and Papua New Guinea) made to or retained by NFT or the Producer (in their

capacity as an Equity Participant) if either or both of them are an Equity Participant;

- **Investment** means the amount that an Investor pays as a non-refundable contribution to the Producer in respect of the Budgeted Cost (which is an amount exclusive of GST) as set out in Column 2 of Schedule 1 of the Investor Acquisition Agreement.
- **Investment Amount** means the amount paid by an Investor for the acquisition of its proportionate share of the Available Copyright Interest.
- **Investor's Share** means the amount expressed as a percentage, calculated using the following formula:

$$\frac{\text{Investment}}{\text{Total Investment}} \times 93$$

- **Licence Agreement** means any agreement between NFT and any third party sub-distributor, agent, sub-agent or licensee appointed or licensed by NFT for the distribution of the Program.
 - **Licensee** means any third party sub-distributor, agent, sub-agent or licensee appointed by NFT to distribute the Program.
 - **Master Production Account** means the bank account referred to in clause 13.1(a) of the Investor Acquisition Agreement.
 - **NFT** means Nine Films & Television Pty Limited ABN 51 066 040 024.
 - **NFT Investment** means the amount which NFT pays as a non-refundable contribution to the Producer in respect of the Budgeted Cost (which is an amount exclusive of GST).
 - **NFT Share** means the amount expressed as a percentage, calculated using the following formula:
- $$\frac{\text{NFT Investment}}{\text{Total Investment}} \times 93$$
- **NNA** means Nine Network Australia Pty Limited ABN 88 008 685 407.
 - **PCTP** means the Pre-committed Third Party or any other person approved by the Producer and NFT.
 - **PCTP Investment** means the amount the PCTP pays as a non-refundable contribution to the Producer in respect of the Budgeted Cost.

- **Program** means:
 - (a) a number of episodes (being a number of episodes determined by NFT that is no greater than 30 and if less than 30 as identified by NFT) of that part of the fifth series of an adult television program known by the Title, comprising certain episodes that are delivered to NFT as cinematographic films on or before 30 June 2005; and
 - (b) all copies and versions of the episodes referred to in paragraph (a), whether identical or differentiated by re-editing, cutting, dubbing, sub-titling or otherwise.
- **Program Copyright** of Investors means all existing and future Copyright subsisting in the Program, strictly limited to the period of the Term (excluding, for the avoidance of doubt, the Excluded Rights and including, for the avoidance of doubt, the Copyright subsisting in the Program as a cinematograph film or films pursuant to section 86 of the *Copyright Act 1968* (Cth) and the right to do or authorise the doing of all or any of the acts specified in section 86 of the *Copyright Act 1968* (Cth)).
- **Represented Investor** means each person who:
 - (a) pays a contribution to the Producer in respect of the Budgeted Cost; and
 - (b) appoints the Agent as its agent on the same terms as the Investor Agent Agreement,including, for the avoidance of doubt, the Investor.
- **Runs** means any of the following on one occasion:
 - (a) an analogue broadcast of the Program;
 - (b) a digital broadcast of the Program; or
 - (c) a contemporaneous broadcast of the Program by means of analogue and one or more methods of digital transmissions.
- **Security Interest** means any bill of sale (as defined in any statute), mortgage, charge, lien, encumbrance, pledge, hypothecation, title retention arrangement, trust or power, as or in effect as security for the payment of a monetary obligation or the observance of any other obligation or any rights of third parties.
- **Term** means for each Investor, the period commencing on 30 June 2005 and ending on 30 June 2012.
- **Territory** means worldwide.
- **Title** means McLeod's Daughters.

- **Total Investment** means \$518,655 per Episode (being the Budgeted Cost per Episode minus the PCTP Investment per Episode) multiplied by the number of Episodes comprised in the Program.

Overview of the Investment

19. The Issuer will make an invitation to wholesale clients to invest in the Program. The invitation will close, Interests in the Program Copyright will be allocated and documents will be executed on or before 30 June 2005. The Investment will involve an Investor paying an amount ('Investment'), together with an Application Fee equal to 0.11% of the Investment amount or such other amount as agreed between the Investors and the Agent (as a contribution towards the Agent's costs).

20. The Agent, acting on behalf of the Investors, will apply 100% of each Investment to investment in the Program by entering into the Investor Acquisition Agreement with the Producer.

21. The maximum investment is to be \$17,115,615 (inclusive of GST) and there is no minimum subscription. Depending on the level of funds raised, a reduced level of Copyright Interests in the Program may be acquired and/or the number of Episodes comprising the Program acquired may be scaled back in accordance with the documentation. In such case, the Agent and the Distributor have the final choice of which Episodes of the Program are selected for investment and which Episodes of the Program are excluded from the investment.

22. There are 38 Episodes commissioned for the 5th series of McLeod's Daughters (Episodes 101 to 138), 30 of which are planned for completion and delivery by 30 June 2005 (Episodes 101 to 130). Investors will be assigned an interest in the Program Copyright of a number of completed Episodes.

23. Each of the Investors will enter into an Investor Distribution Agreement (with the Agent contracting on behalf of each of the Investors severally). It will cover the Program and will provide for licence fees to be paid semi-annually during the first 2 years and annually thereafter based on the performance of the Program. In addition, the Distributor will enter into the Producer Distribution Agreement in respect of the Program with the Producer and a similar agreement with any other party having rights in respect of the Program. The Distributor will provide a distribution guarantee which will guarantee that Investors will receive by 30 June 2010 (on a cumulative basis) from all territories under the Investor Distribution Agreement an amount equal to 49.5% (inclusive of GST) of the amount of the Investment (see paragraph 38). Performance of these payment obligations will be guaranteed by NNA.

24. It is intended that if less than the full amount is invested, in accordance with the documentation the arrangement will be scaled back by either reducing the number of Episodes comprising the Program or by reducing the total Program Copyright available to the Investors with a consequential scaling back of the remainder of the obligations and benefits under the transaction documents.

25. It is intended that there will be either one or two closings under the arrangement. If there are two closings, then the first closing will operate to crystallise the actual investment package in which the Investors invest and the Investors in the second closing will invest on exactly the same basis as the investors investing under the first closing. There will be mirror documentation for each closing that will be executed on or before 30 June 2005.

Information Memorandum

26. The minimum application amount per Investor is \$100,000 (exclusive of GST) and then multiples of \$10,000 (exclusive of GST) thereafter. In addition an Investor will be required to pay an Application Fee equal to 0.11% of the Investment Amount to the Issuer.

27. To invest in the Program an Investor will complete the Application Form attached to the Information Memorandum. The Investor will be required to sign the Application Form and forward to the Issuer the Application Form, a bank cheque for the application amount together with certificates, acknowledgements or other evidence the Issuer needs to ensure the Investor is a wholesale client for the purposes of the Corporations Act.

Investor Agent Agreement

28. Under clause 2.1, each of the Investors irrevocably and by way of security appoints the Agent as their attorney to execute on their behalf the Investor Acquisition Agreement and the Investor Distribution Agreement. The Agent will not enter into this agreement or execute other documents on an Investor's behalf unless the Agent has received payment of the Application Fee. Under clause 2.2, each of the Investors appoints the Producer as their agent to execute on their behalf the FTA Licence Agreement and to grant to NNA a licence for the Free Television Rights.

29. The Agent will, by the receipt of the first Proceeds from the Program, open the Proceeds Account in the name of the Agent. The Agent will operate the Proceeds Account until 30 June 2014 and will pay into it any monies received by it on behalf of the Investors from licensing agreements entered into on or before 30 June 2012 (clause 11).

Investor Acquisition Agreement

30. This Agreement sets out the terms and conditions under which the Investors agree to invest in the Program.

31. Under clause 2 the Producer must produce the Program at its own cost and expense. At clause 3.1 the Producer will assign to each Investor that Investor's Copyright Interest in respect of the Program Copyright covered by the Investor Acquisition Agreement in consideration of the non-refundable payment of the Investment by each Investor to the Producer. The Investors will each hold their respective interests in the Program Copyright as tenants in common with each other, the Producer, the Equity Participants and NFT (clause 3.2).

32. At clause 5 each of the Investors and the Producer agree that Gross Receipts must be applied in accordance with the Application Schedule (refer paragraph 42). Investors will only be entitled to Gross Receipts received by NFT up to 30 June 2013 resulting from licensing agreements entered into on or before 30 June 2012.

FTA Licence Agreement

33. This agreement is between the Producer, the Producer as agent for the Investors (as per clause 2.2 of the Investor Agent Agreement), the Agent and NNA. Under clause 2, the Investors as Licensor grant NNA as Licensee the Free Television Rights in the Program for 4 Runs in Australia and Papua New Guinea for the period commencing 30 June 2005 and ending on 30 June 2012.

34. At clause 3 in conjunction with clause 10, in consideration for the grant of the Free Television Rights, NNA must pay the Investors the Investors' Share of the FTA Licence Fee in accordance with Schedule 2 as follows:

30 September 2011	Investors' Share of \$28,526.30 (inclusive of GST) per Episode
30 September 2012	Investors' Share of \$317,973.70 (inclusive of GST) per Episode
Total	Investors' Share of \$346,500 (inclusive of GST) per Episode

Note: 1/11th of the above amounts will be payable by the tax law partnership of the Investors to the Tax Office in respect of GST.

35. The balance of the FTA Licence Fee not payable to Investors under the agreement will be payable to NFT in its capacity as an Equity Participant under the NFT Licence Agreement.

Investor Distribution Agreement

36. The agreement is between NFT, the Investors, the Agent and NNA. Under clause 2(a) each of the Investors licences to NFT the rights to distribute the Program (excluding the rights granted under the FTA Licence Agreement) worldwide for the period commencing 30 June 2005 and ending on 30 June 2012. At clause 2(b) NFT acknowledges Investors are not the sole owners of the Program Copyright and do not own the underlying rights, therefore NFT will need to separately obtain licences of the rights to distribute the Program from all the other owners.

37. At clause 4.1 and 4.2 NFT will be entitled to a commission of 25% for the distribution of the Program as well as reimbursement of sales expenses and marketing expenses from Gross Receipts. Under clause 4.3 NFT must distribute Gross Receipts in accordance with the Application Schedule (refer paragraph 42). Investors are only entitled to Gross Receipts received by NFT up to 30 June 2013 and where received after 30 June 2012 must be receipts resulting from licensing agreements entered into on or before 30 June 2012. Investors will be entitled to receive Gross Receipts and an accounting statement twice per year for the first two years of the arrangement and thereafter on an annual basis (clause 4.3(d) and clause 6.1).

38. Under clause 5.1 NFT commits to a series of progressive cumulative distribution guarantee(s) payable within 3 months of 30 June 2006, 2007, 2008, 2009 and 2010 and in total equal to a maximum of 49.5% (inclusive of GST) of the amount of the Investor's Investment. NFT will only be required to pay the distribution guarantee if NFT has not paid sufficient Gross Receipts to Investors by each guarantee date. The maximum distribution guarantee amounts are set out in the Table below.

Distribution guarantee amount	Guarantee date
5.5% (inclusive of GST) of the Investor's Investment	30 June 2006
11% (inclusive of GST) of the Investor's Investment	30 June 2007
27.5% (inclusive of GST) of the Investor's Investment	30 June 2008
44% (inclusive of GST) of the Investor's Investment	30 June 2009
49.5% (inclusive of GST) of the Investor's Investment	30 June 2010

Note: 1/11th of the above amounts will be payable by the tax law partnership of the Investors to the Tax Office in respect of GST.

39. If NFT is required to make any payments as outlined in the Table above NFT will be entitled to recover such amounts from Gross Receipts (clause 5.2). The distribution guarantee is additional to, and separate from, the Investors entitlement to the FTA Licence Fees.

40. Under clause 16 NNA guarantees to each of the Investors the performance of NFT's payment obligations of any distribution guarantee amounts.

41. The funding of the progressive cumulative distribution guarantee(s) is not attributable in any way or form whether directly or indirectly to any money raised or expended in relation to the acquisition by the Investors of their respective interest in the Program Copyright. This includes the fees payable to the Producer, director and any other person who receives payment out of any moneys contributed to the cost of producing the Program.

Distribution of Gross Receipts – Application Schedule

42. Under Schedule 2 of the Investor Acquisition Agreement and Investor Distribution Agreement Gross Receipts must be applied as follows:

- (a) first, to the Distributor, the Distributor's distribution commissions;
- (b) second, to the Distributor, the reimbursement of the Distributor's sales expenses and marketing expenses;
- (c) third, by way of licence fees, to the Investors and the Equity Participants (excluding the PCTP), an amount equal to the sum of the Sub-Distributor distribution guarantee and the PTL presale, *pari passu* and to each of them in the proportion that their respective investments in the Program bears to the total of their Investments;
- (d) fourth, to a government film body, 1% of Foreign Gross Receipts;
- (e) fifth, by way of licence fees, to the Investors, the Producer, the PCTP and the Equity Participants (excluding the PCTP):
 - (a) to the Producer, 15%;
 - (b) to the PCTP, 14%; and
 - (c) to the Investors and the Equity Participants (excluding the PCTP) 71%, *pari passu* and to each of them in the proportion that their respective investments in the Program bears to the total of their Investments,

- until the Investors and the Equity Participants (excluding the PCTP) have received an amount (under this paragraph (e), paragraph (c) and from any other source – that is, under the FTA Licence Agreement) equal to their respective investments in the Program;
- (f) sixth, to the Producer, with the consent of the Agent, NFT and the PCTP, the amount of any overage paid by the Producer; and
 - (g) thereafter, by way of licence fees, in the following proportions *pari passu*:
 - (A) to the Producer, 52%;
 - (B) to the Investors and the Equity Participants (excluding the PCTP), 43%, *pari passu* and to each of them in the proportion that their respective Investments in the Program bears to the total of their Investments; and
 - (C) to the PCTP, 5%.

NFT Acquisition Agreement

43. The agreement is between the Producer and NFT. Under clause 2 the Producer must produce the Program at its own cost and expense. At clause 3.1 the Producer will assign to NFT the NFT Share of the Program Copyright in consideration of the non-refundable payment of the NFT Investment by NFT to the Producer. NFT will hold its interests in the Program Copyright as tenants in common with the Producer, the Equity Participants and the Investors (clause 3.2).

44. On execution of this agreement NFT must pay the NFT Investment to the Producer into the Master Production Account (clause 4.2(a)). At clause 5 NFT and the Producer agree that Gross Receipts must be applied in accordance with the Application Schedule (refer paragraph 42). NFT will only be entitled to Gross Receipts received by NFT up to 30 June 2013 resulting from licensing agreements entered into on or before 30 June 2012.

Producer Distribution Agreement

45. The agreement is between NFT and the Producer under which the Producer licences to NFT the rights to distribute the Program, from the creation of the copyright in each Episode of the Program, throughout the world in perpetuity (clause 2(a)). At clause 2(b) NFT acknowledges the Producer is not the sole owner of the Program Copyright and the underlying rights, therefore NFT will need to separately obtain licences of the rights to distribute the Program from all the other owners.

46. At clause 4.1 and 4.2 NFT will be entitled to a commission of 25% for the distribution of the Program as well as reimbursement of sales expenses and marketing expenses from Gross Receipts. Under clause 4.3(a) NFT must distribute Gross Receipts in accordance with the Application Schedule (refer paragraph 42). The Producer will be entitled to receive Gross Receipts and an accounting statement every three months (clause 4.3(d) and clause 5.1).

47. Clause 28 will apply where the total of Investments by Investors is less than \$570,520.50 (inclusive of GST) per Episode. Should this occur, subject to any other agreement between the Producer and NFT, NFT agrees to invest an amount equal to the difference between:

- (a) the amount equal to \$570,520.50 (inclusive of GST) per Episode multiplied by the number of Episodes included within the Program; and
- (b) the total of the Investments by Investors,

on substantially the same terms and conditions as set out in the NFT Acquisition Agreement.

NFT Licence Agreement

48. Under clause 2(a) NFT licences to NNA the Free Television Rights in the Program for 4 Runs in Australia and Papua New Guinea for the period commencing 30 June 2005 and ending on 30 June 2012.

49. To the extent that the whole of the FTA Licence Fee is not payable by NNA to the Investors, or to the Agent on behalf of the Investors, under the FTA Licence Agreement, NNA must pay the remainder of the FTA Licence Fee to the Equity Participants (other than the PCTP and the Investors), in accordance with Schedule 1 of the NFT Licence Agreement (clause 6).

Pre-committed Third Party Production & Investment Agreement

50. The agreement is between the Producer and the PCTP. Under clause 2 the Producer must produce the Program at its own cost and expense. At clause 3.1 the Producer will assign to the PCTP 5% of the Program Copyright in perpetuity, in consideration of the non-refundable payment of the PCTP Investment by the PCTP to the Producer. The PCTP will hold its interests in the Program Copyright as tenants in common with the Producer, the Investors, NFT and the Equity Participants (clause 3.3).

51. Within 5 business days after the execution of this agreement the PCTP must pay its investment to the Producer into the Master Production Account (clause 4(a)). At clause 5(a) the PCTP and the Producer agree that Gross Receipts must be applied in accordance with the Application Schedule (refer paragraph 42). At clause 5(d) receipts from the Excluded Rights must be distributed in the following proportions *pari passu*:

- (a) to the Producer 52%;
- (b) to NFT 43%; and
- (c) to the PCTP 5%.

Pre-committed Third Party Distribution Agreement

52. The agreement is between NFT and the PCTP. Under clause 2(a) the PCTP licences to NFT the rights to distribute the Program worldwide in perpetuity. At clause 2(b) NFT acknowledges the PCTP is not the sole owner of the Program Copyright and the underlying rights, therefore NFT will need to separately obtain licences of the rights to distribute the Program from all the other owners.

53. At clause 4.1 and 4.2 NFT will be entitled to a commission of 25% for the distribution of the Program as well as reimbursement of sales expenses and marketing expenses from Gross Receipts. Under clause 4.3 NFT must distribute Gross Receipts in accordance with the Application Schedule (refer paragraph 42).

Sub-Distribution Agreement

54. Under the terms of the agreement NFT will grant all rights throughout the world, excluding certain rights, to the Sub-Distributor for a period of 10 years from the delivery of McLeod's Daughters 5th series. McLeod's Daughters 5th series will consist of 38 Episodes with a delivery date of 1 October 2005, or such later date as is reasonably agreed by the parties.

55. The Sub-Distributor will be entitled to a 25% commission as well as reimbursement of sales expenses and marketing expenses from Gross Receipts. Under clause 4 the Sub-Distributor will provide NFT with a distribution guarantee. The guarantee will only be payable where the cumulative Gross Receipts received by NFT is less than the guaranteed amounts. The amount of the guarantee will be the difference between the Gross Receipts actually paid and the guarantee that is due. The Sub-Distributor is entitled to be repaid any guarantee paid from future Gross Receipts.

Pay Television Licence

56. Under this licence the Sub-Distributor will grant non-standard television rights in various countries to the PTL in return for presales payable by the PTL to the Sub-Distributor.

Finance

57. There is no finance facility offered by the Agent, the Issuer or any other party involved in the arrangement. Investors can fund their investment in the Program themselves, or borrow from an independent lender.

58. This Ruling does not apply if a finance arrangement entered into by an Investor to fund the Investor's Investment in the arrangement 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;
- the funding arrangements transform the Project into a 'scheme' to which Part IVA may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project are involved or become involved, in the provision of finance to Investors for the Project.

Ruling

Division 10B

59. Provided the Investor Agent Agreement, Investor Acquisition Agreement, FTA Licence Agreement and Investor Distribution Agreement are all executed and commence on or before 30 June 2005, an Investor will become an owner of the Copyright in the Program for the purposes of subsection 124K(1).

60. A deduction is available to an Investor in the Project under Division 10B as follows:

- (a) 50% of the Investment is allowable in the year ending 30 June 2005, the year of income in which the Program is first used by the Investors to produce assessable income; and
- (b) the remaining 50% is allowable in the year ending 30 June 2006.

61. The Application Fee of 0.11% of the Investor's Investment, or such other amount as agreed between an Investor and the Agent are capital in nature and non deductible under Division 10B or section 8-1 of the ITAA 1997.

Partnership

62. For the year ending 30 June 2005 and subsequent years of income, Investors who acquire an interest in the Copyright of the Program from the Producer will be in a tax law partnership for the purposes of Division 5 of Part III of the ITAA 1936 (see definition of 'partnership' in section 995-1 of the ITAA 1997). The partners will receive income jointly from the commercial exploitation of the Copyright in the Program. Section 90 of ITAA 1936 provides that the net income of a partnership is calculated as if the partnership were a resident taxpayer, and is the assessable income less all allowable deductions. The partnership will be required to lodge a partnership return for each year of income, as required by section 91 of the ITAA 1936.

63. Each partner will be a partner in a partnership and, in accordance with section 92 of the ITAA 1936, where the partner is a resident, will be required to include his or her individual interest in the net income of the partnership in his or her assessable income.

Division 40 of the ITAA 1997

64. Division 40 of the ITAA 1997 does not apply to the Investors interest in the Copyright.

Section 79D

65. Section 79D does not apply to deny or defer the deductions otherwise allowable.

Section 82KL

66. Section 82KL will not be applied to deny deductions otherwise allowable.

Part IVA

67. Part IVA will not apply to deny deductibility or to accelerate assessability of the above amounts.

Assumptions

68. This Ruling is made subject to the following assumptions in respect of the Program acquired by the Investors:

- (a) an Investor will incur capital expenditure on the purchase of Copyright (paragraph 124L(1)(b));
- (b) the Investor Agent Agreement, Investor Acquisition Agreement, FTA Licence Agreement and Investor Distribution Agreement are all executed and commence on or before 30 June 2005;
- (c) the Program will be produced and the Investors tax law partnership will use the Copyright for the purpose of producing assessable income on or before 30 June 2005 (subsection 124L(1));
- (d) a certificate, issued by the Department of Communication, Information Technology and the Arts, will be in existence in relation to the Program (subsection 124K(1));
- (e) the Investors will not exercise the discretion contained in subsection 124UA(2);
- (f) the effective life of the Copyright in the Program is deemed to be two years (subsection 124UA(1));
- (g) no pre-sale arrangements, distribution rights agreements, distribution guarantee agreements, or other like agreements, have been, or will be, entered into in circumstances where such agreements would put funds into the hands of the Investors, by loan or otherwise, to enable them to expend capital moneys by way of contribution to the cost of acquiring Copyright interests in the Program ('Australian films');
- (h) the dominant purpose of the Investors is to make a commercial return from their investment in the Program and the arrangement will be executed in the manner described in this Ruling; and
- (i) Copyright interests are acquired at an arm's length value from the Producer.

Explanation

Corporations Act 2001

69. For this Ruling to apply, an offer for an interest in the Program must have been made to, and accepted by an Investor, who qualifies as a wholesale client as defined in section 761G of the *Corporations Act 2001*.

70. An Investor in the Program may be a person who is a wholesale client within the definition in section 761G. A person will be a wholesale client where the person satisfies one of the following tests:

- the 'product value test' (paragraph 761G(7)(a));
- the 'individual wealth test' (paragraph 761G(7)(c)); or
- the 'professional investor test' (paragraph 761G(7)(d)).

71. A participant in a managed investment scheme, referred to below as 'the person' or 'the person to whom the offer is made', will satisfy the 'product value test' where:

- the minimum amount payable for the interests in the Program on acceptance of the offer by the person to whom the offer is made is at least \$500,000; or
- the amount payable for the interests in the Program on acceptance by the person to whom the offer is made and the amounts previously paid by the person for interests in the Program of the same class that are held by the person add up to at least \$500,000.

72. A participant in a managed investment scheme, referred to below as 'the person' or 'the person to whom the offer is made', will satisfy the 'individual wealth test' where, it appears from a certificate given by a qualified accountant no more than 6 months before the offer is made, that the person to whom the offer is made:

- has net assets of at least \$2.5 million; or
- has a gross income for each of the last 2 financial years of at least \$250,000 a year.

73. A participant in a managed investment scheme, referred to below as 'the person' or 'the person to whom the offer is made', will satisfy the 'professional investor test' where:

- the person is a financial services licensee; or
- the person controls at least \$10 million for the purposes of investment in securities.

Division 10B

The Cost of a Unit of Industrial Property

74. The cost of an Australian film for the purposes of Division 10B is determined under section 124R.

75. In our view, based on the information provided, the Investors and the Producer are dealing at arm's length. The Investors will pay the Investment to the Producer under the terms of the Investor Acquisition Agreement. In return for the Investment the Producer will assign each of the Investors an interest in the Program Copyright of the Program for the period commencing 30 June 2005 and ending 30 June 2012.

76. The 0.11% Application Fee the Investors pay to the Agent is not a cost of acquiring a unit of industrial property (the Program Copyright). The Application Fee is capital in nature and is not deductible under either Division 10BA of Part III of the ITAA 1936 or section 8-1 of the ITAA 1997.

Used for the purpose of producing assessable income

77. For Division 10B to apply, section 124L requires the owner of a unit of industrial property to have used it in the year of income concerned or in a previous year of income for the purpose of producing assessable income.

78. The Investors, through the Agent and the Producer, will licence their interest in the Program Copyright to the Distributor and NNA. The Distributor will market the Program worldwide, excluding the Free Television Rights in Australia and Papua New Guinea. NNA will receive the Free Television Rights in Australia and New Guinea in return for the FTA Licence Fee. The Investors tax law partnership is to receive income generated from the commercial exploitation of the Program in accordance with Investor Distribution Agreement and the FTA Licence Agreement. It is our view that the Program Copyright in the Program will be used for the purpose of producing assessable income. A deduction will be available to the Investors in the year ending 30 June 2005, provided the Investors purchase their Program Copyright interest in the Program and the relevant transaction documents are executed and commence on or before 30 June 2005.

Entitlement to annual deductions

79. The amount of the annual deduction allowable to the owner of a unit of industrial property to whom Division 10B applies is determined in accordance with section 124M.

80. The amount of the annual deduction is calculated by dividing the residual value of the unit at the end of the income year by the number of whole years in the effective life of the unit as at the beginning of the year. The residual value of a unit is determined in accordance with section 124S and the effective life of a unit, being a copyright subsisting in an Australian film, is determined in accordance with section 124UA.

Residual value

81. Residual value is determined under section 124S. Generally speaking, the residual value, as per subsection 124S(1), is the cost of the unit to the owner less the sum of:

- (a) the deductions (if any) allowed or allowable to that person in respect of the unit in previous years; and
- (b) any consideration receivable by the owner in respect of any earlier part disposal of the unit.

Effective life of a unit

82. The effective life of a unit to which section 124UA applies, that is a copyright subsisting in an Australian film, will commence at the commencement of the year of income during which it is first used by the owner for the purpose of producing assessable income and shall end at the conclusion of the next succeeding year of income, or, where the unit was acquired for a specified period, the end of the year of income in which that specified period ends, whichever first occurs. Effectively this means that the cost of the unit is written off over two years except in circumstances where the unit is acquired for a specified period which expires within the same year of income in which the unit was acquired, in which case the capital cost of the unit will be fully deductible in that year.

83. Subsection 124UA(2) gives an owner of a unit of industrial property that relates to a copyright in an Australian film the right to elect to have the effective life of the unit determined under section 124U. If the owner makes such an election, the deductions allowable in respect of the cost to the owner will be determined under the general basis provided for in Division 10B, that is by way of annual deductions over 25 years or any shorter effective life as determined in accordance with section 124U.

84. The Producer will assign up to 93% of the Program Copyright in the Program to the Investors. The residual value for an Investor will be the capital expenditure incurred by that Investor to acquire their Program Copyright interest in the Program on or before 30 June 2005.

85. On the assumption that no election in terms of subsection 124UA(2) will be made, the effective life of the Program Copyright in the Program is two years. Consequently, the deduction available to an Investor in the year in which the Program Copyright is first used by the investors to produce assessable income is 50% of the capital expenditure incurred by that Investor to acquire his or her interest in the Program Copyright.

86. The deduction available in the following year will be the residual value of the Program Copyright in the Program at that time, being the cost of the unit to the owner less the deductions allowed in previous years (assuming that no consideration was received by the investors tax law partnership or the Investors when the Agent or the Producer, on behalf of the Investors, enters into the Investor Distribution Agreement and FTA Licence Agreement). The deduction available is therefore the remaining 50% being, the capital expenditure incurred (cost of unit) less the 50% deduction allowed in the previous year.

Interest deductibility

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

88. This Product Ruling will have no application to Investors who obtain finance that has any of the features listed at paragraph 58.

Partnership for income tax purposes

89. The Investors who acquire up to 93% of the Program Copyright in the Program will comprise a partnership for income tax purposes as they are in receipt of ordinary income or statutory income jointly (see the definition of 'partnership' in section 995-1 of the ITAA 1997). Division 5 of Part III applies so that the assessable income of a partner includes so much of the individual interest of the partner in the net income of the partnership or, in the case of a partnership loss, a partner is entitled to a deduction for so much of his or her individual interest in any loss of the partnership. It should be noted that the partnerships are not common law partnerships and consist only of the persons who receive income jointly from the exploitation of the Program Copyright in the Program.

90. The tax law partnership will receive passive income from the exploitation of the Program Copyright in the Program.

91. As the Investors between them hold up to 93% of the Program Copyright in the Program, the Investors' tax law partnership is entitled to the Investors share of income under the Investor Distribution Agreement and the FTA Licence Agreement.

92. A partnership return will be required to be furnished for each year of income as required by section 91. The Investors will be required to disclose their share of the partnership net income in their returns of income as required by section 92.

Division 40 of the ITAA 1997

93. Division 40 of the ITAA 1997 does not apply to the Program Copyright as it is excluded by the operation of subsection 40-45(5) of the ITAA 1997 where the relevant depreciating asset is a copyright in an Australian film and the Investor is entitled to a deduction under Division 10B.

Section 79D

94. Section 79D does not apply where there are no 'foreign income deductions' (as defined in subsection 160AFD(9)).

95. The transactions covered by the arrangement do not give rise to 'foreign income deductions' because the deductions under Division 10B do not relate to any 'assessable foreign income' (as defined in subsection 160AFD(9)). The income derived by the Investors under the Investor Distribution Agreement and FTA Licence Agreement will have an Australian source and will not be 'assessable foreign income'.

Section 82KL – recouped expenditure

96. The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefits'. Insufficient 'additional benefits' will be provided in respect of this project, to trigger the application of section 82KL. It will not apply to deny the deductions otherwise allowable under section 124M.

Part IVA

97. 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). The arrangement subject to this Ruling will be a 'scheme'. The Investors will obtain, for example, a 'tax benefit' from entering into the scheme, in the form of a deduction allowable under the provisions in Division 10B, that would not have been obtained but for the scheme. However, it is not possible to conclude, from the arrangement outlined in this Ruling, that the scheme will be entered into or carried out with the dominant purpose of obtaining a tax benefit.

98. An Investor to whom this Ruling applies intends to stay in the scheme for its full term and derive assessable income from the exploitation of the Program Copyright in the Program. Further, there are no features of the Project, as described in the said arrangement, that suggest that the Project is so 'tax driven' and 'so designed to produce a tax deduction of a certain magnitude', that the operation of Part IVA is attracted.

Detailed contents list

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PR 2005/92

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

PR 1999/95; TR 92/1; TR 92/20;
TR 97/16; TR 98/22; TD 93/34

Subject references:

- Australian films
- film income
- film industry
- product rulings
- schemes and shams
- tax administration
- tax avoidance

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- ITAA 1936 124S
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- ITAA 1936 124U
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- ITAA 1936 Pt III Div 10BA
- ITAA 1936 160AFD(9)
- ITAA 1936 Pt IVA
- ITAA 1936 177A
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- ITAA 1997 8-1
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- Corporations Act 2001 761G(7)(a)
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Legislative references:

- ITAA 1936 79D
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 - ITAA 1936 90
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