



PR 2006/121 - Income tax: Great Southern Plantations 2006 Project - (Post 30 June Growers - New Species)

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Product Ruling

Income tax: Great Southern Plantations 2006 Project – (Post 30 June Growers – New Species)

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① This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

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 scheme is carried out in accordance with the information we have been given, and have described below in the **Scheme** part of this document.

If the scheme 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 scheme 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 scheme has been implemented as described below and to ensure that the participants in the scheme 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 entity(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 Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates. In this Ruling, the scheme is sometimes referred to as the 'Great Southern Plantations 2006 Project', or just simply as 'the Project'.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
 - section 8-1 of the ITAA 1997;
 - section 17-5 of the ITAA 1997;
 - section 25-25 of the ITAA 1997;
 - Division 27 of the ITAA 1997;
 - Division 35 of the ITAA 1997;
 - Subdivision 61-J of the ITAA 1997;
 - Division 328 of the ITAA 1997;
 - Division 328 of the *Income Tax (Transitional Provisions) Act 1997*;
 - section 82KL of the *Income Tax Assessment Act 1936* (ITAA 1936);
 - section 82KZME and 82KZMF of the ITAA 1936;
 - section 82KZMG of the ITAA 1936; and
 - Part IVA of the ITAA 1936.

Note: All legislative references in this Ruling are to the ITAA 1997 unless otherwise indicated.

Goods and Services Tax

3. All fees and expenditure referred to in this Ruling include the goods and services tax ('GST') where applicable. In order for an entity (referred to in this Ruling as a 'Grower') to be entitled to claim input tax credits for the GST included in its expenditure, it must be registered or required to be registered for GST and hold a valid tax invoice.

Changes in the Law

4. Although this Ruling deals with the laws enacted at the time it was issued, later amendments may impact on this Ruling. Any such changes will take precedence over the application of this Ruling and, to that extent, this Ruling will be superseded.

5. Entities 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 entities in projects such as this. In keeping with that intention, the ATO suggests that promoters and advisers ensure that entities are fully informed of any legislative changes after the Ruling is issued.

Class of entities

7. The class of entities to whom this Ruling applies are the entities more specifically identified in the Ruling part of this Product Ruling and who enter into the scheme described below on or after the date this Ruling is made. They will have a purpose of staying in the scheme 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 scheme. In this Ruling, these entities are referred to as 'Growers'.

8. The class of entities to whom this Ruling applies does not include Growers who:

- intend to terminate their involvement in the scheme prior to its completion, or who otherwise do not intend to derive assessable income from it;
- elect to market their own produce;
- enter the Project before 1 July 2006 or after 31 March 2007;
- enter into finance arrangements with Great Southern Finance Pty Ltd, or with any associate of Great Southern Finance Pty Ltd that do not comply with the written undertakings given to the Tax Office by Great Southern Finance Pty Ltd dated 14 March 2006 and 11 May 2006 (the word 'associate' has the meaning given in section 318 of the ITAA 1936); or

- enter into finance arrangements with Great Southern Finance Pty Ltd, the Preferred Financier or entities associated with this Project other than those specified in paragraph 50(i) of this Ruling (the word 'associate' has the same meaning given in section 318 of the ITAA 1936).

Qualifications

9. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 18 to 54 of this Ruling.

10. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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Date of effect

12. This Ruling applies prospectively from 2 August 2006, 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. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

13. If this Product Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

14. If this Product Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Product Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

15. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Withdrawal

16. This Product Ruling is withdrawn and ceases to have effect after 30 June 2008. The Ruling continues to apply, in respect of the relevant provisions ruled upon, to all entities within the specified class who enter into the scheme specified below. Thus, the Ruling continues to apply to those entities, even following its withdrawal, who entered into the specified scheme prior to withdrawal of the Ruling. This is subject to there being no change in the scheme or in the entities involvement in the scheme.

Previous Ruling

17. This Ruling replaces Product Ruling PR 2004/117 which is withdrawn on and from 2 August 2006.

Scheme

18. The scheme that is the subject of this Ruling is described below. This scheme incorporates the following documents:

- Application for Product Ruling, dated 28 September 2004;
- Draft Product Disclosure Statement for the Great Southern Plantations 2006 Project, to be issued by Great Southern Managers Australia Ltd (GSMAL), received 1 October 2004 and 9 February 2006;
- Supplementary Product Disclosure Statement for the Great Southern Plantations 2006 Project to be issued by Great Southern Managers Australia Ltd (GSMAL), received 28 April 2006;

- Draft **Constitution** of the Great Southern Plantations 2006 Scheme, dated 20 September 2004, updated and received 1 February 2006 and 9 February 2006;
- Draft **Land and Management Agreement** between GSMAL (as both the 'Landholder' and 'Responsible Entity') and the Grower, dated 11 September 2004, updated and received and 1 February 2006;
- Draft **Lease or Forest Right Agreement or Forest Right Lease Agreement** between GSMAL (as both the 'Landholder' and 'Responsible Entity') and the Grower, dated 11 September 2004, updated and received 1 February 2006, 9 February 2006 and 28 April 2006;
- Draft Compliance Plan for Great Southern Plantations 2006 Project dated 21 September 2004, updated and received 1 February 2006 and 9 February 2006;
- Plantation Management Agreement between GSMAL and Great Southern Plantations Ltd (GSPL), dated 8 February 2001;
- Variation to Plantation Management Agreement between GSMAL and Great Southern Plantations Ltd (GSPL), undated;
- **Loan Deed** between Great Southern Finance Pty Ltd (as the 'Lender') and the Borrower, received 16 September 2005;
- Loan Deed between Great Southern Finance Pty Ltd (as 'Lender') and the Preferred Financier, received 16 September 2005;
- Proforma Lease between GSMAL and Great Southern Property Managers Ltd (as the 'Landholder'), received 1 February 2006 and 9 February 2006; and
- Additional correspondence between the Tax Office and the Applicant, dated 22 October 2004, 25 October 2004, 2 November 2004, 9 December 2004, 1 February 2005, 9 February 2006 28 April 2006 and 27 June 2006.

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

19. The documents highlighted (in **bold**) are those that Growers may enter into. For the purposes of describing the scheme to which this Ruling applies, there are no other schemes, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate of a Grower, will be a party to, which are a part of the scheme to which this Ruling applies.

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

Overview

21. The salient features of the Great Southern Plantations 2006 Project are as follows:

Location	Western Australia, Victoria, South Australia, Queensland, New South Wales, Tasmania, the Northern Territory or such other areas of Australia deemed suitable for the commercial growing of Hardwoods.
Type of business each participant is carrying on	Commercial growing of Hardwood species for the production of short fibre hardwood woodchips for use in the paper industry.
Number of hectares offered for cultivation	This PDS provides for 5,000 hectares to be planted, however, oversubscriptions may be accepted.
Size of each Woodlot	0.5 hectares on the Tiwi Islands in the Northern Territory and 0.33 hectares in all other areas.
Number of trees per hectare	Average of 1,000 per hectare
Term of the Project	Approximately 11 years
Initial cost	\$2,970 to \$3,300
Initial cost per hectare	\$5,940 or \$6,600 on the Tiwi Islands in the Northern Territory and \$9,000 to \$10,000 in all other areas.
Ongoing costs	Growers are required to pay 3.3% of net harvest proceeds as management fees and 2.75% of net harvest proceeds as rent/lease fees.
Other costs	Growers will be charged for the cost of all insurance except Public Liability Insurance.

22. Under this PDS, Great Southern Managers Australia Ltd (GSMAL) proposes to offer 15,000 interests called 'Woodlots' of 0.5 hectares on the Tiwi Islands in the Northern Territory and 0.33 hectares in all other areas. The Project is registered as a Managed Investment Scheme under the Corporations Act. The Responsible Entity for the Project is Great Southern Managers Australia Ltd.

23. Growers who have their 'Applications' accepted during the period 1 July 2006 to 31 March 2007 will enter into the Project as Post 30 June Growers. **This Ruling only applies in respect of these Post 30 June Growers. Note that Product Ruling PR 2004/116 may apply to Growers who enter into the Project on or before 30 June 2006.**

24. There is no minimum amount that must be raised under the PDS for this Project. The majority of the land for the Project has been, or will be, purchased by Great Southern Property Managers Ltd (GSPML), a wholly owned subsidiary of GSMAL. GSPML (or any other entity related to GSMAL's parent company, Great Southern Plantations Limited, ('Related Entity')) may lease, or may be granted other similar interests in land under relevant State or Territory laws, from third parties, which are sufficient for the purpose of carrying on the Project. GSMAL will lease the land, or be granted other similar interests in land under relevant State or Territory laws which are sufficient for the purpose of carrying on the Project, from GSPML or the other Related Entity. GSMAL has the right to accept oversubscriptions.

25. The Growers will enter into a contract with GSMAL to have suitable Hardwood seedlings planted on their Woodlot for the purpose of eventual felling and sale in approximately eleven years. GSMAL will establish and cultivate the trees and be responsible for harvesting, processing and selling the timber. Unless the Grower elects to take possession of their timber, GSMAL will arrange the marketing and sale of the forest produce.

26. Upon application, Growers will execute a Power of Attorney enabling GSMAL to act on their behalf as required. Each Grower is provided with an ownership certificate and a copy of the plantation grid map from which their land and trees can be identified.

27. Growers in this Project who initially invested in the Great Southern Plantations 1994 or 1995 Projects and whose names are shown on the Register of Growers upon harvest of those Projects will be entitled to a discount of 10% on the cost of their application fees for Establishment Services for this Project.

Constitution

28. The Constitution establishes the Project and operates as a deed binding on all of the Project's Growers and the Responsible Entity. The Constitution sets out the terms and conditions under which GSMAL agrees to act as Responsible Entity and thereby manage the Project. Growers are bound by the Constitution by virtue of their participation in the Project. Pursuant to clause 29 of the Constitution, the Responsible Entity will keep a register of Growers.

29. Under the terms of the Constitution, all moneys received from applications shall be paid to the Responsible Entity. The Responsible Entity shall deposit those moneys into an Application Fund in the name of the Responsible Entity. The application moneys will be released by the Responsible Entity when it is reasonably satisfied that certain specified criteria in the Constitution have been met (clauses 7 and 8 of the Constitution).

Compliance Plan

30. As required by the *Corporations Act 2001*, a Compliance Plan has been prepared by GSMAL for the Project. The purpose of the Compliance Plan is to ensure that GSMAL manages the Project in accordance with its obligations and responsibilities contained in the Constitution and that the interests of Growers are protected.

Land and Management Agreement

31. Growers participating in the scheme will enter into a Land and Management Agreement (LMA) between GSMAL and the Grower.

32. Under the Land and Management Agreement, each Grower appoints GSMAL to perform services under the agreement from the Commencement Date, being the date of execution of the agreement. GSMAL will supervise and manage all silvicultural activities on behalf of the Grower. The services to be performed are specified in the clause 1 definitions of 'Establishment Services', 'Planting Services' and 'Services'.

33. The Establishment Services to be performed during the Establishment Period, being a period of 12 months from the Commencement Date are as follows:

- (a) ripping and mounding the Woodlot as necessary from the Commencement Date;
- (b) otherwise preparing the Woodlot for planting as necessary from the Commencement Date;
- (c) procurement of sufficient Hardwood seedlings or trees of appropriate size as is reasonably required to complete the Planting Services;
- (d) fertilising the Woodlot as necessary from the Commencement Date;
- (e) spraying the Woodlot as necessary from the Commencement Date;
- (f) maintaining the Woodlot according to good silvicultural and forestry practices; and
- (g) the Planting Services.

Land Interest

34. Growers participating in the Project will, pursuant to the terms of the Land and Management Agreement, be granted an interest in land by GSMAL in the form of a lease, forest right or similar interest in land to use their Woodlot for the purpose of conducting their afforestation business.

35. Growers with Woodlots in Western Australia, Victoria or South Australia will be granted a lease whereas Growers in Queensland will be granted a forest right. Growers who are allotted Woodlot(s) in Tasmania will enter into a Forestry Right Lease Agreement with the Responsible Entity. Growers with Woodlots in any other State or Territory will be granted a similar interest in land in accordance with the relevant State/Territory laws. Where this Ruling uses the terms 'Lease' and 'Lessor' it is intended to also include the respective terms 'Forest Right' and 'Grantor' or similar terms used in a document granting any similar interest in land.

36. The Land Interest gives the Grower a lease over an identifiable area of land for approximately 11 years when the final distribution of the sale proceeds is made to the Grower or until the Project is terminated.

37. Each Grower must pay Rent to the Lessor in an amount specified in clause 3 of the Land Interest Agreement. Payment of Rent is deferred until the year the harvest proceeds are received.

38. Some of the conditions of the lease are that the Grower:

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

Fees

39. The fees payable under the Land and Management Agreement on a per Woodlot basis are as follows:

- \$3,300 payable on Application for Establishment Services, or for Growers in this Project who initially invested in the Great Southern Plantations 1994 or 1995 Projects and whose names are shown on the Register of Growers upon harvest of those Projects, \$2,970 is payable on Application for Establishment Services;

- at harvest, GSMAL is entitled to 3.3% of the Net Proceeds of Sale of harvest in consideration for meeting the ongoing management and maintenance expenses from completion of the Establishment Services until harvest; and
- at harvest, GSMAL is entitled to 2.75% of the Net Proceeds of Sale of harvest for Rent during the term of the agreement.

40. GSMAL will use reasonable endeavours to arrange insurance of the Woodlot on behalf of the Grower to cover against fire and other usual risks.

Planting

41. GSMAL will be responsible for planting Hardwood seedlings on the Woodlots. The species to be planted will generally be *Eucalyptus globulus* for Woodlots located in Western Australia, South Australia and Victoria, *Eucalyptus dunnii*, *Eucalyptus grandis* or selected hybrids of *Eucalyptus camaldulensis* × *E. grandis* hybrids for Woodlots located in Queensland and northern NSW, *Eucalyptus globulus* or *Eucalyptus nitens* in Tasmania and *Acacia mangium* for Woodlots located on the Tiwi Islands in the Northern Territory.

42. Other appropriate hardwood species may also be established in locations where it is considered they will achieve the necessary yields and quality required for this Project as well as meeting other appropriate silviculture and economic parameters. Therefore these species will have similar characteristics in regard to growth, colour and fibre pulp yield per Woodlot to the eucalyptus species referred to above and will be preferred species for pulp and paper manufacture. A sufficient number of trees will be planted which would reasonably be expected to meet the projected timber production.

43. GSMAL must complete all Establishment Services, including the Planting Services, within 12 months of the Grower's Commencement Date. GSMAL will then maintain the trees in accordance with good silvicultural practice and will furnish reports to the Grower regarding the progress of the trees.

Harvesting and sale

44. Growers may elect, within 6 years of the Commencement Date, to become an 'Electing Grower' (clause 8.1 of the LMA) and take their own Collectable Produce by giving written notice to GSMAL. This Ruling does not apply to Electing Growers.

45. GSMAL will sell the forest produce on behalf of the 'Non-Electing Growers' for the maximum practicable price (clause 9.1 of the LMA). At all times the Grower has full right, title and interest in the Forest Produce and the right to have the Forest Produce sold for their benefit (clause 11.3 of the LFR).

46. Harvesting is to take place within 12 months of the forest produce reaching harvest maturity (as reasonably determined by the Responsible Entity and, in any event, not later than 11 years from the Commencement Date) unless GSMAL believes that it would be in the best interest of the Growers for harvesting to be deferred and the Growers resolve to do so by ordinary resolution (clause 7 of the LMA).

47. Growers will share the Gross Proceeds of Sale on a proportionate basis following the payment of felling costs, costs of sale, costs of chipping (if applicable), and any amounts due and payable by the relevant Grower (clause 11 of the LMA).

48. GSMAL will ensure that the Gross Proceeds of Sale are paid into the Proceeds Fund trust bank account. The Growers' proportional share of the costs of felling and costs of sale, and, if applicable, the costs of chipping, will be paid from the Gross Proceeds of Sale to GSMAL, or the relevant contractor. GSMAL will receive from the Proceeds Funds an amount equal to 2.75% of the Net Proceeds of Sale, as rent, and another amount equal to 3.3%, as remuneration for the services provided following completion of the Establishment Services. The balance of the Net Proceeds of Sale will be distributed to the Non-Electing Growers on a proportionate basis. The terms 'Proceeds Fund' and 'Grower's Proportional Share' are defined in clause 1 of the LMA.

Finance

49. Growers can fund their participation in the Project themselves, borrow from Great Southern Finance Pty Ltd (a lender associated with GSMAL), borrow from the Preferred Financier, or borrow from an independent lender.

50. Details of the loans that will be offered to Growers by Great Southern Finance Pty Ltd and the Preferred Financier are set out in the Application for Term Finance form and the Terms of Loan Deed. Normal debt recovery procedures, including legal action, will be taken in the case of defaulting borrowers. These options are summarised as follows:

(i) *Great Southern Finance Pty Ltd*

Option A – 12 months terms payments:

- equal monthly principal instalments are payable over a period of 12 months;
- instalments are paid by direct debit commencing 15 July 2007;
- the GST component is not financed and is invoiced on execution of the Land and Management Agreement; and
- no interest is applicable.

Option B – Principal and Interest Finance:

- principal and interest loans with a repayment term of two years up to a term of no more than 9 years;
- equal monthly principal and interest repayments over the term of the loan, commencing from 31 July 2007; and
- interest rates will be fixed for the period of the loan and are set on an arms length basis with reference to a commercial margin over the inter bank SWAP rate for that term.

For loans under Option B, the following will apply:

- the GST component is not financed and is invoiced on execution of the Land and Management Agreement;
- a Loan Establishment Fee, comprising an application fee of up to 1.1% of the loan advance and a fee to cover legal costs and expenses of up to \$275 (GST inclusive) may be charged; and
- the security for the loan is taken over the Grower's interest under the Land and Management Agreement and subsequent Land Interest issued.

*(ii) Preferred Financier***Option A – 12 months terms payments:**

- equal monthly principal instalments over a period of 12 months;
- instalments paid by direct debit commencing from 15 July 2007;
- the GST component is not financed and is invoiced on execution of the Land and Management Agreement; and
- no interest is applicable.

Option B – Principal and Interest Finance:

- principal and interest loans from 2 years up to no more than 9 years; or
- loans with interest only payments for up to 2 years followed by principal and interest repayments for the remainder of the term; provided that the loan term cannot be less than 5 years or greater than 9 years;
- where an interest only period is applicable, equal monthly interest payments followed by equal monthly principal and interest repayments for the term of the loan commencing from 31 July 2007; or

- where there is no interest only period, equal monthly principal and interest repayments over the term of the loan commencing from 31 July 2007; and
- interest rates will be fixed for the period of the loan and are set on an arms length basis with reference to a commercial margin over the inter bank SWAP rate for that term.

For loans under Option B, the following will apply:

- the GST component is not financed and is invoiced on execution of the Land and Management Agreement;
- a Loan Establishment Fee, comprising an application fee of up to 1.1% of the loan advance and a fee to cover legal costs and expenses of up to \$275 may be charged; and
- the security for the loan is taken over the Grower's interest under the Land and Management Agreement and subsequent Land interest issued.

51. This Ruling will not apply to Growers who enter into any other finance arrangement offered to Growers by Great Southern Finance Pty Ltd, or by an 'associate' of the Responsible Entity (the word 'associate' has the meaning given in section 318 of the ITAA 1936).

52. This Ruling will not apply to Growers who enter into finance arrangements with Great Southern Finance Pty Ltd, or with any associate of Great Southern Finance Pty Ltd, that do not comply with the written undertakings given to the Tax Office by Great Southern Finance Pty Ltd dated 27 June 2006.

53. Growers cannot rely on any part of this Ruling if the 'Application Fee' is not paid in full to the Responsible Entity on or before 15 June 2007 whether by the Grower or on the Growers behalf by a lending institution. Where an application is accepted by the Responsible Entity, and that application is subject to finance approval by any lending institution, Growers cannot rely on this Ruling if written evidence of that approval has not been given to the Responsible Entity by the relevant lending institution on or before 15 June 2007.

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

- entities associated with the Project, other than Great Southern Finance Pty Ltd, are involved in the provision of finance for the Project;
- 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 of the ITAA 1936, or the funding arrangements transform the Project into a 'scheme' to which Part IVA of the ITAA 1936 may apply;
- the loan terms or rate of interest 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, other than Great Southern Finance Pty Ltd or the Preferred Financier are involved or become involved in the provision of finance to Growers for the Project.

Ruling

Application of this Ruling

55. Subject to paragraph 8 and the specific exclusions set out in paragraphs 51, 52, 53 and 54 this Ruling applies only to Growers who:

- are accepted to participate in the Project during the period from the date of this Ruling until 31 March 2007 (Post 30 June Growers);
- have executed a Land and Management Agreement between the date of this Ruling and 30 April 2007 (inclusive); and where
- the Establishment Services will be completed within 12 months of the Commencement Date.

56. The Grower's participation in the Project must constitute the carrying on of a business of primary production. A Grower is not eligible to claim any tax deductions until the Grower's application to enter the Project is accepted and the Project has commenced. This Ruling does not apply to Growers who elect to market timber produce from their Woodlots (Electing Growers).

The Simplified Tax System (STS)

Division 328

57. To be an 'STS taxpayer' a Grower must be eligible to be an 'STS taxpayer' and must have elected to be an 'STS taxpayer' (Division 328 of the ITAA 1997). For a Grower participating in the Project, the recognition of income and the timing of tax deductions is different under the STS where a Grower who was an 'STS taxpayer' prior to the 1 July 2005 continues to use the cash accounting method (called the 'STS accounting method') – see sections 328-120 and 328-125 of the *Income Tax (Transitional Provisions) Act 1997*.

58. For such Growers, a reference in this Ruling to an amount being deductible when 'incurred' will mean that amount is deductible when paid and a reference to an amount being included in assessable income when 'derived' will mean that amount is included in assessable income when received.

25% entrepreneurs tax offset

59. For the first income year starting on or after 1 July 2005, Subdivision 61-J 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

Section 6-5 and Division 328

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

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

Deductions for management fees and interest**Section 8-1**

62. A Grower may claim tax deductions under section 8-1 for the expenses in the following Table:

Fee Type	ITAA 1997 Section	Year Ending 30 June 2007	Year Ending 30 June 2008
Establishment Services Fee or Discounted Establishment Services Fee	8-1	\$3,300 or \$2,970 See Notes (i) & (ii)	
Interest	8-1	As incurred See Note (iii)	As incurred See Note (iii)
Loan Establishment Fee (for finance entered into with Great Southern Finance Pty Ltd or the Preferred Financier)	25-25	See Note (iv)	

Notes:

- (i) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (ii) Under section 82KZMG of the ITAA 1936 the fee for the Establishment Services is expenditure for 'seasonally dependant agronomic activities' (see paragraphs 90 to 94 of this Ruling) and is deductible in the income year in which it is incurred.
- (iii) The deductibility or otherwise of interest arising from agreements entered into with financiers other than Great Southern Finance Pty Ltd, the internal financier, or the Preferred Financier is outside the scope of this Ruling. However, all Growers including those who finance their participation in the Project other than with Great Southern Finance Pty Ltd or the Preferred Financier should read carefully the discussion of the prepayment rules in paragraphs 81 to 95 of this Ruling as those rules may be applicable if interest is prepaid. Subject to the 'excluded expenditure' exception, the prepayment rules apply whether the prepayment is

required under the relevant loan agreement or is at the Grower's choice.

- (iv) The Loan Establishment Fee payable to either Great Southern Finance Pty Ltd or to the Preferred Financier is a borrowing cost and is deductible under section 25-25. It is incurred for borrowing funds that are used or are to be used during the income year solely for income producing purposes. The deduction is spread on a straight line basis over the period of the loan or 5 years, whichever is the shorter. The deductibility or otherwise of borrowing costs arising from loan agreements entered into with financiers other than Great Southern Finance Pty Ltd or the Preferred Financier is outside the scope of this Ruling.

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

Section 35-55 – Commissioner's discretion

63. A Post 30 June Grower who is an individual accepted into the Project in the year ended 30 June 2007 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 Growers for the income years ending **30 June 2007 to 30 June 2017**. This conditional exercise of the discretion will allow those losses to be offset against the Grower's other assessable income in the income year in which the losses arise.

Section 82KL and Part IVA

64. For a Grower who commences participation in the 2006 Project and incurs expenditure as required by the Land and Management Agreement, the following provisions of the ITAA 1936 have application as indicated:

- section 82KL does not apply to deny the deductions otherwise allowable; and
- the relevant provisions in Part IVA will not be applied to cancel a tax benefit obtained under a tax provision dealt with in this Ruling.

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

Is the Grower carrying on a business?

65. For the amounts set out in the Tables above to constitute allowable deductions, the Grower's afforestation activities as a participant in the Great Southern Plantations 2006 Project must amount to the carrying on of a business of primary production.

66. Where there is a business, or a future business, the gross proceeds from the sale of the timber will constitute assessable income in their own right. The generation of 'business income' from such a business, or future business, provides the backdrop against which to judge whether the outgoings in question have the requisite connection with the operations that more directly gain or produce this income.

67. For schemes such as those of the Great Southern Plantations 2006 Project, Taxation Ruling TR 2000/8 sets out in paragraph 89 the circumstances in which the Grower's activities can constitute the carrying on of a business. As Taxation Ruling TR 2000/8 sets out, these circumstances have been established in court decisions such as *Commission of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

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

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

69. In this Project, each Grower enters into a Land Interest Agreement. Under the agreement each individual Grower will have rights over a specific and identifiable area of land. The agreement provides the Grower with an ongoing interest in the specific trees on the leased area for the term of the Project. Under the agreement, the Grower must use the land in question for the purpose of carrying out afforestation activities, and for no other purpose. The agreement allows Great Southern Managers Australia Ltd, the Landholder and the Responsible Entity, to come onto the land to carry out their obligations.

70. Each Grower also enters into a Land and Management Agreement. Under the agreement, the Responsible Entity is engaged by the Grower to establish and maintain a Woodlot on the Grower's identifiable area of land during the term of the Project. The Responsible Entity has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the Woodlot on the Grower's behalf.

71. The Responsible Entity is also engaged to harvest and sell, on the Grower's behalf, the wood produce grown on the Grower's Woodlot.

72. 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.

73. The activities that will be regularly carried out during the term of the Project demonstrate a significant commercial purpose. Based on reasonable projections, a Grower in the Project will derive assessable income from the sale of the wood produce that will return a before-tax profit, that is, a profit in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

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

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

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

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

The Simplified Tax System***Division 328***

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

79. Changes to the STS rules apply from 1 July 2005. The question of whether a Grower is eligible to be an 'STS taxpayer' is outside the scope of this Product Ruling. Therefore, any Grower who relies on those parts of this Ruling that refer to the STS will be assumed to have correctly determined whether or not they are eligible to be an 'STS taxpayer'.

Deductibility of management fees***Section 8-1***

80. Consideration of whether the initial management fees are deductible under section 8-1 begins with the first limb of the section. This view proceeds on the following basis:

- the outgoing in question must have a sufficient connection with the operations or activities that directly gain or produce the taxpayer's assessable income;
- the outgoings are not deductible under the second limb if they are incurred when the business has not commenced; and
- where all that happens in a year of income is that a taxpayer 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.

81. The fee for Establishment Services is associated with the afforestation activities that will relate to the gaining of income from the Grower's business of afforestation (see above), and hence has a sufficient connection to the operations by which income (from the harvesting and sale of wood produce) is to be gained from this business. It 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 scheme. There is no capital component of the management fee. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

Prepayment provisions***Sections 82KZL to 82KZMG***

82. 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.

83. For this Project, only section 82KZL of the ITAA 1936 (an interpretive provision) and sections 82KZME, 82KZMF and 82KZMG of the ITAA 1936 are relevant. Subject to section 82KZMG, if 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).

Sections 82KZME and 82KZMF

84. Other than expenditure deductible under section 82KZMG of the ITAA 1936, if the requirements of subsections 82KZME(2) and (3) of the ITAA 1936 are met, the formula in subsection 82KZMF(1) of the ITAA 1936 (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)).

85. The requirements of subsection 82KZME(3) of the ITAA 1936 will be met where the agreement (or scheme) has the following characteristics:

- the taxpayer's allowable deductions under the agreement for the 'expenditure year' exceed any assessable income attributable to the agreement for that year;
- the taxpayer does not have effective day to day control over the operation of the agreement. That is, the significant aspects of the scheme 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.

86. For the purpose of these provisions, the agreement includes all activities that relate to the agreement (subsection 82KZME(4) of the ITAA 1936). This has particular relevance for a Grower in this Project who, in order to participate in the Project may borrow funds from a financier other than Great Southern Finance Pty Ltd. Although undertaken with an unrelated party, that financing would be an element of the scheme. The funds borrowed and the interest deductions are directly related to the activities under the scheme. If a Grower prepays interest under such financing arrangements, the deductions allowable will be subject to apportionment under section 82KZMF of the ITAA 1936.

87. There are a number of exceptions to these rules, but for Growers participating in this Project, only the 'excluded expenditure' exception in subsection 82KZME(7) of the ITAA 1936 is relevant. 'Excluded expenditure' is defined in subsection 82KZL(1) of the ITAA 1936. However, for the purposes of Growers in this Project, 'excluded expenditure' is prepaid expenditure incurred under the scheme that is less than \$1,000. Such expenditure is immediately deductible.

88. Where the requirements of section 82KZME of the ITAA 1936 are met, section 82KZMF of the ITAA 1936 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.

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

89. In the formula 'eligible service period' (defined in subsection 82KZL(1) of the ITAA 1936) means, the period during which the thing under the agreement is to be done. The eligible service period begins on the day on which the thing under the agreement commences to be done or on the day on which the expenditure is incurred, whichever is the later, and ends on the last day on which the thing under the agreement ceases to be done, up to a maximum of 10 years.

Section 82KZMG

90. Under section 82KZMG(1) of the ITAA 1936, expenditure is excluded from the prepayment rules that would otherwise apply, to the extent that the prepaid amount satisfies the requirements of subsections 82KZMG(2) to (4).

91. Subsection 82KZMG(2) of the ITAA 1936 requires that the expenditure is:

- incurred on or after 2 October 2001 and on or before 30 June 2008;
- the eligible service period must be 12 months or shorter and must end on or before the last day of the year of income after the expenditure year; and
- for the doing of a thing under the agreement that is not to be wholly done within the expenditure year.

92. To satisfy subsection 82KZMG(3) of the ITAA 1936 the agreement must satisfy the following requirements:

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

93. Under subsection 82KZMG(4) of the ITAA 1936 the expenditure incurred by the taxpayer must be paid for 'seasonally dependent agronomic activities' undertaken by the manager during the 'establishment period' for the relevant planting of trees for felling. The term 'seasonally dependent agronomic activities' is explained in Taxation Determination TD 2003/12.

94. Subsection 82KZMG(5) of the ITAA 1936 defines the 'establishment period to commence at the time that the first 'seasonally dependent agronomic activity' is performed in relation to a specific planting of trees and to conclude with the planting of trees. Where it is necessary to apply a fertiliser or herbicide to the trees at the same time as planting then those activities fall within the establishment period. Planting of trees refers to the main planting of the particular plantation and expressly excludes specific planting to replace existing seedlings that have not survived.

Application of the prepayment provisions to this Project

95. Under the Land and Management Agreement, a Grower incurs an Establishment Fee consisting of expenditure of \$2,970 or \$3,300 per Woodlot for 'seasonally dependent agronomic activities'.

96. As the requirements of section 82KZMG of the ITAA 1936 have been met, a deduction is allowable in the income year ended 30 June 2007 for the expenditure incurred under the Land and Management Agreement for 'seasonally dependent agronomic activities'.

Interest deductibility***(i) Growers who use Great Southern Finance Pty Ltd as the finance provider***

97. Some Growers may finance their participation in the Project through a loan facility with Great Southern Finance Pty Ltd or the Preferred Financier. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of lease and management fees.

98. The interest incurred by these Growers will be in respect of a loan to finance the Project business operations of growing trees and is therefore directly connected with the gaining of 'business income' from the Project. Such interest will, therefore, have a sufficient connection with the gaining of assessable income to be deductible under section 8-1.

(ii) Growers who DO NOT use Great Southern Finance Pty Ltd or the Preferred Financier as the finance provider

99. The deductibility of interest incurred by Growers who finance their participation in the Project through a loan facility with a bank or financier other than Great Southern Finance Pty Ltd or the Preferred Financier is outside the scope of this Ruling. Product Rulings only deal with schemes where all details and documentation have been provided to, and examined by, the Tax Office.

100. While the terms of any finance agreement entered into between relevant Growers and such financiers are subject to commercial negotiation, those agreements may require interest to be prepaid. Alternatively, a Grower may choose to prepay such interest. 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 82 to 94 of this Ruling).

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

Section 35-55 – exercise of Commissioner’s discretion

101. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for Growers for the income years **30 June 2007 to 30 June 2017**, 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 2007 up to and including 30 June 2017:

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

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

Section 82KL – recouped expenditure

103. The operation of section 82KL of the ITAA 1936 depends, among other things, on the identification of a certain quantum of ‘additional benefits(s)’. Insufficient ‘additional benefits’ will be provided to trigger the application of section 82KL. It will not apply to deny the deduction otherwise allowable under section 8-1 of the ITAA 1997.

Part IVA – general tax avoidance provisions

104. For Part IVA of the ITAA 1936 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).

105. The Project will be a 'scheme'. A Grower will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraph 62 of this Ruling 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.

106. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the wood produce. There are no facts that would suggest that Growers have the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There 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) of the ITAA 1936 it cannot be concluded, on the information available, that participants will enter into the scheme for the dominant purpose of obtaining a tax benefit.

Appendix 2 – Detailed contents list

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Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

IT 360; TD 2003/12; TR 97/11;
TR 98/22; TR 2000/8; TR 2001/14

Previous Rulings/Determinations:

PR 2004/117

Subject references:

- advance deductions and expenses for
certain forestry expenditure
- carrying on a business
- commencement of business
- fee expenses
- forestry agreement
- interest expenses
- management fees
- non-commercial losses
- producing assessable income
- product rulings
- public rulings
- seasonally dependent agronomic
activity
- tax avoidance
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schemes
- tax shelters
- tax shelters project
- taxation administration

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ATO references:

NO: 2004/15274

ISSN: 1441-1172

ATOlaw topic: Income Tax ~~ Product ~~ timber