



PR 2006/137 - Income tax: Australian Cricket Bat Willow Project - Product Disclosure Statement 2006 (2007 Growers)

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Product Ruling

Income tax: Australian Cricket Bat Willow Project – Product Disclosure Statement 2006 (2007 Growers)

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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 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, commencing at paragraph 17, 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 at paragraph 2 apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

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;
- 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 82KZL of the ITAA 1936;
- sections 82KZME and 82KZMF of the ITAA 1936;
- section 82KZMG of the ITAA 1936; and
- Part IVA of the ITAA 1936.

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. 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 entities in projects such as this. In keeping with that intention the Tax Office 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 consists of the entities more specifically identified in the Ruling part of this Product Ruling who enter into the scheme specified, commencing at paragraph 17, 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. In this Ruling, these entities are referred to as 'Growers'.

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

- entities 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;
- entities who participate in the Australian Cricket Bat Willow Project – Product Disclosure Statement 2006 (2007 Growers) (the Project) through offers made other than through the Product Disclosure Statement;
- entities who are accepted to participate in the Project after 30 June 2007; and
- Australian Cricket Bat Willow Plantation Management Services Limited or its associates.

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 17 to 57 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 27 September 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 two conditions in paragraph 14 of this Ruling 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 2009. 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, commencing at paragraph 17. 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 entity's involvement in the scheme.

Scheme

17. The scheme that is the subject of this Ruling is specified in paragraphs 17 to 57. This scheme incorporates the following documents:

- Application for Product Ruling constituted by documents provided on 28, 31 March 2006, 27, 28 April 2006, 8, 9, 16 June 2006 and 23, 28 August 2006, and additional correspondence dated 31 March 2006, 27 April 2006, 8, 9, 16, 19, 20, 21, 22, 30 June 2006, 21 July 2006, and 14, 23, 28, 29 August 2006;
- Draft **Product Disclosure Statement 2006** ('PDS') for Australian Cricket Bat Willow Project, received 28 August 2006, and additional correspondence dated 14 September 2006;
- Draft **Constitution** for Australian Cricket Bat Willow Project, received 28 March 2006;
- Draft **Plantation Management Agreement** (2006) between Australian Cricket Bat Willow Plantation Management Services Limited ('ACBW', as 'Manager') and a Grower for Australian Cricket Bat Willow Project, received 16 June 2006;
- Draft Compliance Plan for Australian Cricket Bat Willow Project, received 8 June 2006;
- Draft **Plantation Lease** (2006) between Australian Cricket Bat Willow Plantation Management Services Limited (as 'Landholder') and a Grower, received 28 August 2006;
- Lease between the 'Lessor' and Australian Cricket Bat Willow Plantation Management Services Limited (as 'Lessee') (Head Lease), received 28 August 2006;

- Custody Agreement between Australian Cricket Bat Willow Plantation Management Services Limited and Sandhurst Trustees Limited (as 'Custodian') dated 7 March 2000, received 28 March 2006;
- Forestry Adviser's Agreement between Australian Cricket Bat Willow Plantation Management Services Limited and the 'Forestry Adviser' dated 4 February 2000, received 28 March 2006;
- Draft Plantation Services Agreement (Stage 5) between Australian Cricket Bat Willow Plantation Management Services Limited (as 'Project Manager') and Murray Valley Nurseries Pty Ltd (as 'Contractor'), received 28 March 2006;
- Administrative Service Agreement between Australian Cricket Bat Willow Plantation Management Services Limited and Calculum Pty Ltd dated 31 January 2000, received 28 March 2006;
- Supply of Rootstock Agreement between Australian Cricket Bat Willow Plantation Management Services Limited and Australian Cricket Willow Pty Ltd dated 29 March 2006, received 27 April 2006; and
- Deed of Trust and Supplemental Deed between Australian Cricket Bat Willow Plantation Management Services Limited and Sandhurst Trustees Ltd, received 8 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.

18. The documents highlighted are those that a Grower may enter into. For the purposes of describing the scheme to which this Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Grower, or any associate of a Grower, will be a party to, which are a part of the scheme. The effect of these agreements is summarised as follows.

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

Overview

20. The main features of the Project are as follows:

Location	Heathcote, Victoria. Comprising part of the land described in Certificate of Title Volume 10726 Folio 537.
Type of business to be carried on by each entity	Cultivating <i>Salix alba var. caerulea</i> ('Willow Trees') for the purpose of harvesting and selling timber.
Number of hectares offered for cultivation	22.5 hectares
Size of each interest	150m ² ('Unit')
Minimum allocation	One 'Unit'
Number of trees per hectare	Approximately 1,333 'Willow Trees' per planted hectare
Term of the Project	10-12 years
Initial cost	\$5,500 per 'Unit'
Initial cost per planted hectare	\$366,666
Ongoing costs	<ul style="list-style-type: none"> • annual management fee; • annual 'Rent'; • 'Harvest' costs and expenses; and • 'product marketing fee'.

21. The Project is registered as a managed investment scheme under the *Corporations Act 2001*. Australian Cricket Bat Willow Plantation Management Services Limited has been issued with an Australian Financial Service Licence and will be the Responsible Entity for the Project.

22. An offer to participate in the Project will be made through a PDS for 1,500 'Plantation Allotments' which comprises a total of 22.5 hectares. Entities will be invited to subscribe in the Project on or after the date of this Ruling and on or before 30 June 2007. These entities will be known as '2007 Growers'.

23. To participate in the Project entities must complete the 'Application Form' and Power of Attorney in the PDS and pay the 'Initial Plantation Management Fees'.

24. Each entity will enter into a Plantation Lease after the execution of the Head Lease and on or before 30 June 2007 with the 'Landholder'. The Plantation Lease will comprise contractual rights in relation to a parcel of land of 150m² called a 'Unit' that will be planted with 20 'Willow Trees'.

25. Each Grower will also enter into a Plantation Management Agreement to contract with the Manager to provide the 'Initial Maintenance Services' and 'Plantation Establishment Services', and undertake services related to 'Plantation Services' and 'Processing'. The Manager may enter into 'Timber Sale Agreements' on behalf of Growers.

26. The 'Plantation Services' include planting the 'Willow Trees' and establishing the 'Plantation Allotment'. These services will be provided during the optimal planting season but no later than 12 months after the acceptance of the 'Application'.

27. The Project will conclude upon 'Harvest' of the 'Plantation' when the Growers' 'Timber' will be jointly harvested and sold. The 'Harvest Income' less any deductions will be distributed to the Growers on a pro rata basis.

28. The Responsible Entity will not accept oversubscriptions.

Constitution

29. The Constitution establishes the Project and operates as a deed binding all of the Growers and ACBW. The Constitution sets out the terms and conditions under which ACBW agrees to act as Responsible Entity. Growers are bound by the Constitution by virtue of their participation in the Project.

30. Under the terms of the Constitution, all moneys received from 'Applications' shall be paid to ACBW. ACBW shall, within a reasonable time or at a time of the receipt of the 'Grower's Contributions', forward the payment to the Custodian. In accordance with section 1017E of the *Corporations Act 2001* ACBW must ensure that the Custodian deposits 'Grower's Contributions' into the designated 'Project Trust Account'. On the first 30 June after the date of the PDS, the 'Growers Contributions' will be released by the Custodian to the 'Lessor' for the 'Lease Rental' and the balance will be released to the Responsible Entity (clause 5.2).

31. Upon acceptance an 'Applicant' becomes a Grower and the Responsible Entity will enter into the 'Register' all relevant details of the Grower and their 'Plantation Allotment' (clause 10).

32. Clause 8.1 provides that the balance of the 'Harvest Income' shall be distributed to the Growers in respect of whose 'Plantations' the 'Harvest Income' was derived in the same proportion that each Grower's 'Plantation Allotment' bears to the total of all 'Plantation Allotments' leased to all relevant Growers. 'Plantation Allotment' means the specified portion of the 'Land' on which a Grower carries on or will carry on their afforestation business.

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

- the irrevocable appointment of ACBW as the Grower's Representative (clause 2);
- remuneration of the Responsible Entity (clause 9);
- the assignment of the Grower's interest in the Project (clause 11);
- ACBW's powers and duties (clauses 12, 13, 16 and 17);
- meetings of Growers (clause 21);
- termination of the Project (clause 22) and winding up of the Project (clause 23); and
- resolution of complaints made by a Grower in relation to the Responsible Entity's management of the Project (clause 25).

Custody Agreement

34. The Responsible Entity has entered into a Custody Agreement with the Custodian. A condition of the Responsible Entity's Australian Financial Services Licence is that the Responsible Entity engages an agent to act as Custodian of 'Scheme Property'. The Custodian has agreed to accept the appointment on the terms set out in the Custody Agreement.

Compliance Plan

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

Head Lease

36. ACBW has entered into a lease with the Lessor in respect of the 'Leased Property' for the duration of the Project. The 'Leased Property' comprises part of the land described in Certificate of Title Volume 10726 Folio 537.

37. ACBW may sub-lease the 'Leased Property' or any part of the 'Leased Property' for a term equivalent to the term of the Plantation Lease made to Growers in the Project.

38. ACBW will install or cause to be installed a trickle irrigation system. The Lessor will make available for use by ACBW an irrigation water supply of up to 12 megalitres per planted hectare per year, as required.

Plantation Lease

39. The parties to the Plantation Lease are ACBW (the Landholder) and the Grower. Under the terms of the Lease, the Grower is granted an interest over identifiable interest of land called the 'Plantation Allotment' consisting of at least 150m².

40. The Grower will sublease their 'Plantation Allotment' from the Landholder for a Term of 11 years. However, as the 'Willow Trees' may take longer to attain a suitable size and density for the production of clefts, the Grower will be granted an option to extend the term of their Plantation Lease for an additional 4 years or until the earlier harvesting of the 'Willow Trees'.

41. Pursuant to the Plantation Lease, the Grower is required to pay 'Rent' for their 'Plantation Allotment' and 'Rent' is inclusive of water consumption and the cost of leasing irrigation equipment. Clauses 6.13 and 6.14 provide for the Landholder to install and maintain a trickle irrigation system to water the 'Plantation Allotments' contained within the area of the Head Lease of up to 12 megalitres of water per planted hectare per annum.

42. If a substantial part of the Plantation is damaged or determined to be no longer commercially viable, clause 8 provides Growers with a capacity to terminate the Plantation Lease or reduce the 'Leased Area'. Where a Grower exercises this option the area of the 'Plantation Allotment' will be reduced commensurately.

43. Among other things, the Plantation Lease sets out:

- the purpose for which the Grower may use the land (clause 5.2);
- the Grower's covenants (clause 5);
- the Landholder's covenants (clause 6); and
- mutual covenants (clause 7).

Plantation Management Agreement

44. Growers enter into a Plantation Management Agreement with the Manager on or before 30 June 2007. Growers engage the Manager as an independent contractor to perform the 'Plantation Services' during the 'Term' of the Project (clause 2.1). Other than termination for default (clause 11), the 'Term' of the Plantation Management Agreement will continue until the 'Plantation' has been 'Harvested' and the 'Timber' sold (clause 2.2).

45. The Manager will establish and maintain a 'Plantation' of 'Willow Trees' on the Growers 'Plantation Allotment' in accordance with the 'Management Plan' and 'Best Silvicultural Practice' (clause 3.1). The services related to establishment and planting of the 'Plantation', the 'Plantation Establishment Services', shall be completed no later than the 'Plantation Establishment Date' being within 12 months after the 'Commencement Date'.

46. The Manager will provide the 'Plantation Services' described in clause 3.2 of the agreement. These include:

- the establishment and management of the 'Willow Tree' 'Plantation';
- planting of the 'Plantation' of 'Willow Trees';
- tending, maintaining and monitoring of the 'Plantation';
- 'Harvesting' of the 'Plantation';
- provision of sufficient healthy 'Willow Tree' root stock;
- repair of all damage done to roads, tracks or fences; and
- prevention of land degradation.

47. Further, Part 1 of the Schedule to the Plantation Management Agreement sets out the 'Management Plan' and provides that the Manager will ensure that, among other things:

- the 'Plantation Allotment' is cleared and prepared for planting with initial spraying of herbicides, deep ripping and ploughing;
- the 'Initial Maintenance Services' are performed;
- sufficient 'Willow Tree' root stock is provided to achieve a stocking rate of 20 trees per 'Unit';
- the 'Willow Trees' are planted in rows, equally spaced, at a stocking rate of 20 trees per 'Unit' on or before the 'Plantation Establishment Date';
- the 'Plantation' is tended, maintained and monitored including the use of, when appropriate, fertilisers and herbicides;
- measures are taken to prevent land degradation;
- the insurance policies for fire and public liability are maintained as agreed;
- the 'Plantation' is 'Harvested' at maturity and processed; and
- reports are issued to Growers regarding the 'Plantation Allotment'.

48. At maturity, the 'Willow Trees' will be 'Harvested' and the 'Timber' sold on behalf of the Grower (clause 8.1). Growers will pay or reimburse the Manager, on a pro rata basis for cost of harvesting the 'Willow Trees' (clause 8.3).

49. Part 4 of the Schedule to the Plantation Management Agreement provides for a management fee of \$110 per 'Unit'. This fee is in respect of initial plantation maintenance services required immediately after the 'Willow Trees' are planted.

Plantation Services Agreement (Stage 5)

50. The Responsible Entity, as 'Project Manager', has engaged Murray Valley Nurseries Pty Ltd as an independent contractor to carry out the 'Plantation Services' in relation to Stage 5 of the Project during the 'Term' in accordance with the 'Plantation Establishment and Maintenance Plan' (attached as a Schedule to the agreement).

Harvesting and sale of pooled 'Timber'

51. The Constitution sets out the principles applying to the pooling of Growers' 'Timber' and distribution of 'Harvest Income' from the 'Harvest Trust Account' (clause 8). Distributions from the 'Harvest Trust Account' will be on a pro rata basis according to the ratio that the Grower's 'Plantation Allotment' bears to all 'Plantation Allotments' leased to all Growers in the Project. This Product Ruling only applies where the following principles apply to those pooling and distribution arrangements:

- only Growers who have contributed 'Timber' to the pool, the proceeds of sale of which make up the 'Harvest Trust Account', are entitled to benefit from distributions from the 'Harvest Trust Account; and
- 'Timber' can only be pooled with the 'Timber' of Growers accepted to participate in the Project.

Project fees

52. Upon application, for each 150m² 'Unit' of the Grower's 'Plantation Allotment', the following fees (referred to in the PDS as the 'Initial Plantation Management Fee') are payable:

- \$5,335 for the 'Plantation Establishment Services';
- \$110 for initial plantation maintenance services; and
- \$55 for 'Rent' for the period from 1 July 2007 to 30 June 2008 (the initial 'Rent').

53. In each subsequent year, for each 150m² of the Grower's 'Plantation Allotment' the following fees are payable:

- \$220 (indexed), for annual management fees, first payable on 1 August 2008 for the period 1 July 2008 to 30 June 2009 and thereafter 1 August each following year during the 'Term' of the Project; and
- \$55 (indexed) for 'Rent' first payable on 1 August 2008 for the period 1 July 2008 to 30 June 2009 and thereafter 1 August each following year during the 'Term' of the Project (the annual 'Rent').

54. Other fees and costs are set out in the Table at paragraph 20 of this Ruling.

Finance

55. A Grower may finance their participation in the scheme from their own funds or borrow from an independent lender external to the Project. A Grower who enters into a finance arrangement with an independent lender may request a private ruling on the deductibility or otherwise of interest incurred under that finance arrangement as it is not covered by this Product Ruling.

56. Growers cannot rely on any part of this Ruling if the 'Initial Plantation Management Fee' is not paid in full on or before 30 June 2007 by the Grower or, on the Grower's behalf, by an independent lending institution. Where an application is accepted and that application is subject to finance approval by any independent lending institution, Growers cannot rely on this Ruling if written evidence of that approval has not been given to the Responsible Entity by the Grower or relevant lending institution on or before 30 June 2007.

57. This Ruling does not apply if the finance arrangement entered into by the Grower includes or has any of the following features:

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL 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 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 any Grower in the Project.

Ruling

Application of this Ruling

58. Subject to paragraph 8, this Ruling applies only to Growers who are accepted to participate in the Project on or after the date of this Product Ruling and on or before 30 June 2007 and who have executed a Plantation Lease and Plantation Management Agreement on or before that date.

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

The Simplified Tax System (STS)

Division 328

60. 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). 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*.

61. 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***Subdivision 61-J***

62. 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***

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

Deductions for fees payable for 'Plantation Establishment Services', initial plantation maintenance services, annual management services and 'Rent'***Section 8-1***

64. A Grower who is accepted to participate in the Project on or after the date of this Product Ruling and on or before 30 June 2007 may claim tax deductions under section 8-1, on a per 'Unit' basis, for the following expenditure.

Fee Type	Year ended 30 June 2007	Year ended 30 June 2008	Year ended 30 June 2009
'Plantation Establishment Services' fee	\$5,335 See Notes (i) & (ii)	Nil	Nil
Plantation maintenance services fee	Amount must be calculated See Notes (i) & (iii)	Nil	Nil
Annual management fee	Nil	Nil	\$220 (indexed) See Notes (i) & (iv)
Initial 'Rent'	Amount must be calculated See Notes (i) & (iii)	Nil	Nil
Annual 'Rent'	Nil	Nil	\$55 (indexed) See Notes (i) & (iv)

Notes:

- (i) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted for GST (for example, input tax credits): Division 27.
- (ii) The fee for 'Plantation Establishment Services' is expenditure for 'seasonally dependent agronomic activities' (see paragraphs 85 to 101 of this Ruling) and is deductible in the income year in which it is incurred.
- (iii) The fee for initial plantation maintenance services of \$110 per 'Unit' and the initial 'Rent' of \$55 per 'Unit' are subject to the prepayment rules in sections 82KZME and 82KZMF of the ITAA 1936. Although the Plantation Management Agreement and Plantation Lease require these fees to be prepaid, for a Grower who acquires the minimum allocation, the amount of the prepaid fees is less than \$1,000. For the purposes of this Project, an amount of less than \$1,000 is 'excluded expenditure'. 'Excluded expenditure' is an 'exception' to the prepayment rules and is deductible in full in the year in which it is incurred. However, where a Grower acquires more than the minimum allocation in the Project, the amount of the Grower's prepaid initial plantation maintenance services fee and prepaid initial 'Rent' may be \$1,000 or more. Such Growers **must** determine the deduction for the prepaid fees using the formula in subsection 82KZMF(1) (see paragraphs 85 to 100 of this Ruling).
- (iv) This Ruling does not apply to Growers who choose to prepay fees, other than those discussed at Note (iii). Amounts that are prepaid for a period that extends beyond the income year in which the expenditure is incurred may be subject to the prepayment provisions in sections 82KZME and 82KZMF of the ITAA 1936. Any Grower who prepays such amounts may request a private ruling on the taxation consequences of their participation in the Project.

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

65. A Grower who is an individual accepted into the Project on or before 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, the Commissioner will exercise the discretion in paragraph 35-55(1)(b) for each Grower for the income years ending **30 June 2007 to 30 June 2016** or the income year in which the 'Trees' are 'Harvested', whichever occurs earlier.

This conditional exercise of the discretion will allow those losses to be offset against the Growers other assessable income in the income year in which the losses arise.

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

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

- expenditure on the 'Plantation Establishment Services', annual management fee and annual 'Rent' does not fall within the scope of sections 82KZME and 82KZMF;
- expenditure on the initial plantation maintenance services and initial 'Rent' is within the scope of sections 82KZME and 82KZMF;
- section 82KL does not apply to deny the deductions otherwise allowable; and
- the relevant provisions in Part IVA will not be applied to cancel a tax benefit obtained under a tax law dealt with in this Ruling.

Commissioner of Taxation27 September 2006

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?

67. For the amounts set out in the Tables at paragraphs 20 and 64 of this Ruling to constitute allowable deductions the Grower's afforestation activities as a participant in the Australian Cricket Bat Willow Project – Product Disclosure Statement 2006 must amount to the carrying on of a business of primary production.

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

69. For schemes such as that of the Australian Cricket Bat Willow Project – Product Disclosure Statement 2006, 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 TR 2000/8 sets out, these circumstances have been established in court decisions such as *Commissioner of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

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

- the Grower has an identifiable interest (by lease or by licence) in the land on which the Grower's trees are established;
- the Grower has a right to harvest and sell the timber 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.

71. In this Project, each Grower enters into a Plantation Management Agreement and a Plantation Lease.

72. Under the Plantation Lease each individual Grower will have rights over a specific and identifiable area of 150m² of land. The Plantation Lease provides the Grower with an ongoing interest in the specific 'Willow Trees' on the leased area for the 'Term' of the Project. Under the Plantation Lease the Grower must use the land in question for the purpose of carrying out afforestation activities, and for no other purpose. The Plantation Lease allows the Manager to come onto the land to carry out its obligations under the Plantation Management Agreement.

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

74. The Manager is also engaged to harvest and sell, on the Grower's behalf, the 'Timber' grown on the Grower's 'Plantation Allotment'.

75. 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.

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

77. The pooling of 'Timber' grown on the Grower's 'Plantation Allotment' with the 'Timber' of other Growers in the Project is consistent with general afforestation practices. Each Grower's proportionate share of the sale proceeds of the pooled 'Timber' will reflect the proportion of the 'Willow Trees' contributed from their 'Plantation Allotment'.

78. The Manager's services are also consistent with general silvicultural practices. They are of the type ordinarily found in afforestation ventures that would commonly be said to be businesses. While the size of a 'Plantation Allotment' is relatively small, it is of a size and scale to allow it to be commercially viable.

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

80. 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 Australian Cricket Bat Willow Project – Product Disclosure Statement 2006 will constitute the carrying on of a business.

The Simplified Tax System

Division 328

81. 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.

82. 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 (but refer to Taxation Ruling TR 2002/6 and Taxation Ruling TR 2002/11). Therefore, any Grower who relies on those parts of this Ruling that refer to the STS will be assumed to have correctly determined whether or not they are eligible to be an 'STS taxpayer'.

Deductions for fees payable for 'Plantation Establishment Services', initial plantation maintenance services, annual management services and 'Rent'

Section 8-1

83. Consideration of whether the fees payable for 'Plantation Establishment Services', initial plantation maintenance services, annual management services and 'Rent' are deductible under section 8-1 begins with the first limb of the section. This view proceeds on the following basis:

- (i) the outgoing in question must have a sufficient connection with the operations or activities that directly gain or produce the taxpayer's assessable income;
- (ii) the outgoings are not deductible under the second limb if they are incurred when the business has not commenced; and
- (iii) 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.

84. The fees payable for 'Plantation Establishment Services', initial plantation maintenance services, annual management services and 'Rent' associated with the afforestation activities will relate to the gaining of income from the Grower's business of afforestation, and hence have a sufficient connection to the operations by which income (from the harvesting and sale of 'Timber') is to be gained from this business. They will thus be deductible under the first limb of section 8-1. Further, no 'non-income producing' purpose in incurring the fee is identifiable from the scheme. The fee appears to be reasonable. There is no capital component of the management fees. 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

85. 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.

86. 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). These provisions also apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes them from the operation of section 82KZMF.

Sections 82KZME and 82KZMF

87. 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 paragraph 91 of this Ruling) will apply to apportion expenditure that is otherwise deductible under section 8-1. The requirements of subsection 82KZME(2) of the ITAA 1936 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) of the ITAA 1936).

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

- (i) the taxpayer's allowable deductions under the agreement for the 'expenditure year' exceed any assessable income attributable to the agreement for that year;
- (ii) 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
- (iii) either:
 - a) there is more than one participant in the agreement in the same capacity as the taxpayer; or
 - b) the entity who promotes, arranges or manages the agreement (or an associate of that entity) promotes similar agreements for other taxpayers.

89. 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. Although undertaken with an independent external party, that financing would be an element of the scheme. The funds borrowed and the interest deduction 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.

90. There are a number of exceptions to these rules, but for Growers participating in this Project, only the 'excluded expenditure' exception in subsection 82KZME(7) is relevant. 'Excluded expenditure' is defined in subsection 82KZL(1) 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.

91. 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 herein, to apportion prepaid expenditure and allow a deduction over the period that the benefits are provided:

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

92. 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

93. 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).

94. 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.

95. 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.

96. 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.

97. 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

Sections 82KZME and 82KZMF

98. The expenditure incurred by a Grower in the Project for the initial plantation maintenance services fee and the initial 'Rent' paid on application meets the requirements of subsections 82KZME(1) and 82KZME(2) of the ITAA 1936 and is incurred under an 'agreement' as described in subsection 82KZME(3). Therefore, unless one of the exceptions to section 82KZME applies, the amount and timing of tax deductions for those fees are determined under section 82KZMF of the ITAA 1936.

99. The prepaid initial plantation maintenance services fee and the initial 'Rent', being amounts of less than \$1,000 in each expenditure year, constitute 'excluded expenditure' as defined in subsection 82KZL(1) of the ITAA 1936. Under Exception 3 (subsection 82KZME(7) of the ITAA 1936) 'excluded expenditure' is specifically excluded from the operation of section 82KZMF of the ITAA 1936. A Grower can, therefore, claim an immediate deduction for the initial plantation maintenance services fee and the initial 'Rent' in the income year in which it is paid.

100. However, where a Grower acquires more than the minimum allocation of one 'Plantation Allotment' in the Project and the quantum of the prepaid initial plantation maintenance services fee and the initial 'Rent' is \$1,000 or more, the deduction allowable for those amounts will also be subject to apportionment according to the formula in subsection 82KZMF(1) of the ITAA 1936.

Section 82KZMG

101. Under the Plantation Management Agreement, a Grower incurs a fee for the 'Plantation Establishment Services' of \$5,335 per 'Plantation Allotment' for 'seasonally dependent agronomic activities'.

102. 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 Plantation Management Agreement for 'seasonally dependent agronomic activities'.

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

103. Although not required under either the Plantation Management Agreement or the Plantation Lease, a Grower participating in the Project may **choose** to prepay fees for a period beyond the 'expenditure year'. Where this occurs, contrary to the conclusion reached in paragraph 64 of this Ruling, section 82KZMF of the ITAA 1936 will apply to apportion the expenditure and allow a deduction over the period in which the prepaid benefits are provided.

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

105. However, as noted at paragraph 99 of this Ruling, prepaid fees of less than \$1,000 incurred in an 'expenditure year' will be 'excluded expenditure' and will be not subject to apportionment under section 82KZMF of the ITAA 1936.

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

106. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income years **30 June 2007 to 30 June 2016** 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 2016:

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

107. 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

108. 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 of the ITAA 1936. It will not apply to deny the deduction otherwise allowable under section 8-1.

Part IVA – general tax avoidance provisions

109. 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).

110. The Australian Cricket Bat Willow Project – Product Disclosure Statement 2006 will be a 'scheme'. A Grower will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 64 to 66 of this Ruling that would not have been obtained but for the scheme. However, it is not possible to conclude the scheme will be entered into or carried out with the dominant purpose of obtaining this tax benefit.

111. Each Grower to whom this Ruling applies intends to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the 'Timber'. There are no facts that would suggest that a Grower has the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There is no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing at arm's length or, if any parties are not dealing at arm's length, that any adverse tax consequences result. Further, having regard to the factors to be considered under paragraph 177D(b) of the ITAA 1936 it cannot be concluded, on the information available, that entities will enter into the scheme for the dominant purpose of obtaining a tax benefit.

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 97/11; TR 98/22; TR 2000/8,
TR 2001/14; TR 2002/6;
TR 2002/11; TD 2003/12

Subject references:

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

Legislative references:

- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
- ITAA 1936 82KZMD
- ITAA 1936 82KZME
- ITAA 1936 82KZME(1)
- ITAA 1936 82KZME(2)
- ITAA 1936 82KZME(3)
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- ITAA 1936 Pt IVA
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- ITAA 1997 Div 35
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