



PR 2006/147 - Income tax: Cool Climate Apricot Project - 2007 Growers (from 16 November 2006 to 31 May 2007)

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 This document has changed over time. This is a consolidated version of the ruling which was published on *14 March 2007*



Product Ruling

Income tax: Cool Climate Apricot Project – 2007 Growers (from 16 November 2006 to 31 May 2007)

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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.

Relevant provision(s)

2. The relevant provision(s) dealt with in this Ruling are:
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
 - section 8-1 of the ITAA 1997;
 - section 17-5 of the ITAA 1997;
 - section 25-25 of the ITAA 1997;
 - Division 27 of the ITAA 1997;
 - Division 35 of the ITAA 1997;
 - Division 40 of the ITAA 1997;
 - Subdivision 61-J of the ITAA 1997;
 - Division 328 of the ITAA 1997;
 - 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; 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 participants in projects such as this. In keeping with that intention the Tax Office suggests that promoters and advisers ensure that participants are fully informed of any legislative changes after the Ruling is issued.

Class of entities

7. The class of each entity to which this Ruling applies is the entity more specifically identified in the Ruling part of this Product Ruling and who enters into the scheme specified below on or after the date this Ruling is made. The entity 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, the entity is referred to as 'Growers'.

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

- an entity who intends to terminate their involvement in the scheme prior to its completion, or who otherwise do not intend to derive assessable income from it;
- an entity who participates in the Cool Climate Apricot Project (the Project) through offers made other than through the Product Disclosure Statement;
- an entity who is accepted to participate in the Project before 16 November 2006 and after 31 May 2007;
- an entity who elects to market and sell the apricots from their 'Apricot Lot' in accordance with clause 9 of the Management Agreement;
- an entity who finances their participation in the Project with loans other than from Momentum Funding Pty Ltd,

or other than as described at paragraphs 57 to 63 of this Ruling; and

- Cool Climate Investments Pty Ltd or its associates.

Qualifications

9. The class of entity 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 63 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 11 October 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 2009. The Ruling continues to apply, in respect of the tax law(s) 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 entity's involvement in the scheme.

Scheme

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

- Application for Product Ruling constituted by documents provided on 8 November 2005, 20, 25 January 2006, 2, 9, 11, 12, 14, 17, 20 February 2006, 2, 6, 23, 24, 27, 29, 30 March 2006, 6, 19, 24 April 2006, 21, 28 July 2007, 14 August 2006, 4, 6, 25 September 2006 and 5 October 2006 and additional correspondence dated 23 January 2006, 9, 11, 17 February 2006, 2, 23, 24, 29 March 2006, 6, 19 April 2006, 21, 26, 27, 28 July 2006, 14, 28, 30, 31 August 2006, and 4, 5, 6, 25 September 2006;
- Draft Product Disclosure Statement for Cool Climate Apricot Project, received 5 October 2006 (**PDS**);
- Draft Power of Attorney to be entered into by each Grower in favour of Primary Securities Ltd (as 'Responsible Entity'), received 28 July 2006 (**Power of Attorney**);
- Draft Consolidated Constitution for Cool Climate Apricot Project, received 5 October 2006 (**Constitution**);

- Draft Rules for Cool Climate Apricot Project, received 21 July 2006 (Rules);
- Draft Consolidated Management Agreement between Primary Securities Ltd (as 'Responsible Entity') and a Grower for Cool Climate Apricot Project, received 5 October 2006 (**Management Agreement**);
- Draft Compliance Plan for Cool Climate Apricot Project made by Primary Securities Ltd (as 'Responsible Entity'), received 21 July 2006 (Compliance Plan);
- Draft Consolidated Sub-Management Agreement between Primary Securities Ltd (as 'Responsible Entity') and Cool Climate Investments Pty Ltd (as 'Manager') for Cool Climate Apricot Project, received 25 September 2006;
- Draft Consolidated Orchard Management Agreement between Primary Securities Ltd (as 'Responsible Entity'), Cool Climate Investments Pty Ltd (as 'Manager') and Tian-An Pty Ltd (as 'Orchard Manager') for Cool Climate Apricot Project, received 25 September 2006;
- Draft Responsible Entity Services Agreement between Primary Securities Ltd (as 'Responsible Entity') and Cool Climate Investments Pty Ltd (as 'Manager'), received 21 July 2006;
- Draft Consolidated Tree Right between Primary Securities Ltd (as 'Responsible Entity') and a Grower for Cool Climate Apricot Project, received 25 September 2006 (**Tree Right**);
- Draft Custodian Agreement between Primary Securities Ltd (as 'Responsible Entity') and Robert Garton Smith (as 'Custodian'), received 21 July 2006 (Custodian Agreement);
- Draft Consolidated Infrastructure and Planting Agreement between Cool Climate Investments Pty Ltd (as 'Manager') and Tian-An Pty Ltd (as 'Orchard Manager') for Cool Climate Apricot Project, received 25 September 2006;
- Lease Agreement between Tian-An Pty Ltd (as 'Lessor') and the 'Facilitators' (as 'Lessees') in relation to land described in the agreement as Register Volume 109388, Folio 3, received 14 August 2006 (Facilitating Lease);
- Sub-lease Agreement between the 'Facilitators' (as 'Lessors') and Cool Climate Investments Pty Ltd (as 'Lessee') in relation to part of the land described in the

- agreement as Register Volume 109388, Folio 3, received 14 August 2006 (Qew Lease);
- Lease Agreement between the landowner (as 'Lessor') and Cool Climate Investments Pty Ltd (as 'Lessee') in relation to land described in the Sub-lease to RE as the 'New Property' and further described in that agreement as Register Volume 144678, Folio 1, received 14 August 2006 (Head Lease);
 - Sub-lease Agreement between Cool Climate Investments Pty Ltd (as 'Sub-Lessor') and Primary Securities Ltd (as 'Responsible Entity') in relation to part of the land described in the agreement as Register Volume 109388, Folio 3 and land described in the agreement as Register Volume 144678, Folio 1, received 14 August 2006 (Sub-lease to RE);
 - Draft Apricot Offtake Agreement between Primary Securities Ltd (as 'Responsible Entity'), Cool Climate Investments Pty Ltd (as 'Manager') and Tian-An Pty Ltd (as 'Orchard Manager'), received 25 September 2006;
 - Deed of Subordination between Cool Climate Investments Pty Ltd (as 'Borrower'), the Lender and Primary Securities Ltd (as 'Responsible Entity'), received 4 September 2006;
 - Letter dated 4 September 2006 from an entity related to Allco Managed Investments Ltd as trustee for the Gateway Momentum Funding Trust No. 1 ('Momentum Funding') advising details of loan terms to be offered by Momentum Funding to Growers, received 4 September 2006;
 - Draft Indicative Term Sheet, received 4 September 2006;
 - Draft Finance Application Form and Finance Agreement for the Cool Climate Apricot Project between Momentum Funding and a Grower, received 6 September 2006 (**Finance Application**); and
 - Draft Terms Agreement for the Cool Climate Apricot Project 2007 between Primary Securities Ltd (as 'Responsible Entity') and a Grower, received 5 October 2006 (**Terms Agreement**).

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 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

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

Location – ‘Qew Property’	Fingerpost Road, Campania, Southern Tasmania.
Location – ‘New Property’	Fingerpost Road, Campania, Southern Tasmania.
Type of business to be carried on by each participant	Cultivating apricot trees for the purpose of harvesting and selling the produce.
Number of hectares offered for cultivation	47.2 hectares and oversubscription will not be accepted.
Size of each interest	0.10 hectare (‘Apricot Lot’), of which approximately 0.0025 hectare will be on ‘Qew Property’ and 0.0975 hectare will be on ‘New Property’.
Minimum allocation	No minimum subscription.
Number of trees per hectare	Approximately 1,380 trees per hectare.
Term of the Project	18 years.
Initial cost	\$8,316 per ‘Apricot Lot’.
Initial cost per hectare	\$83,160.
Ongoing costs	<ul style="list-style-type: none"> • ‘Orchard Maintenance Fee’; • ‘Tree Right Fee’; • ‘Processing Costs’; • ‘Marketing Fee’; • ‘Variable Management Fee’; • Deferred Management Fee of 2% of ‘Net Proceeds to Growers’ from Year 7 for 10 years for services provided in Year 1; • Deferred Management Fee of 2% of ‘Net Proceeds to Growers’ from Year 7 for 10 years for services

	provided in Year 2; and • 'Performance Incentives'.
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21. The Project is registered as a managed investment scheme under the *Corporations Act 2001*. Primary Securities Ltd 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 472 'Apricot Lots' which comprises a total of 47.2 hectares. Entities will be invited to subscribe in the Project on or after 16 November 2006 and on or before 31 May 2007. Each entity will become a Grower of apricots by acquiring a 'Tree Right' over a 0.10 hectare 'Apricot Lot', of which 0.0025 hectare will be on 'Qew Property' and 0.0975 hectare will be on 'New Property'.

23. To participate in the Project participants must complete the 'Application Form' in the PDS and pay the 'Application Fee' in accordance with the payment schedule outlined in the PDS. The 'Application Fee' will be banked into the Custodian's trust account. These monies will be released to the Responsible Entity.

24. A Grower accepted on or after 16 November 2006 and on or before 31 May 2007, will commence participation as a '2007 Grower'. **This Ruling only applies in respect of a '2007 Grower' who is accepted into the Project on or after 16 November 2006 and on or before 31 May 2007. Note that a separate Product Ruling, PR 2006/140, has issued for Growers accepted into the Project from 27 September 2006 to 15 November 2006.**

25. Each Grower will enter into a Tree Right with the Responsible Entity. The Tree Right will comprise contractual rights in relation a parcel of land of 0.10 hectare called an 'Apricot Lot'.

26. Each 'Apricot Lot' will comprise of 0.0025 hectare of fully established trees situated within the 'Qew Property' and 0.0975 hectare which will be situated within the 'New Property', of which 20 of the trees will be planted before 30 June 2007 and the remainder will be planted by 30 September 2007.

27. Each Grower will also enter into a Management Agreement to contract with the Responsible Entity to provide the 'Initial Services' and undertake services related to 'Apricot Farming' and 'Processing'. The Responsible Entity will also arrange to market and sell the apricots.

28. The Responsible Entity will appoint the Manager to perform the 'Apricot Farming', 'Processing' and marketing and selling of the apricots. The Manager will, in turn, sub-contract the Orchard Manager to perform most of these responsibilities.

29. There is no minimum subscription but the Responsible Entity will not accept oversubscriptions.

Constitution

30. The Constitution for the Project sets out the general functions, powers and duties under which the Responsible Entity agrees to act for the Growers and to manage the Project. The Tree Right and the Management Agreement are Schedules to the Constitution. These Agreements will be executed by each Grower who has signed the 'Application Form' attached to the PDS and who is accepted into the Project on or before 30 June 2007. Note that this Ruling only applies to an entity which is accepted to participate in the Project on or after 16 November 2006 and on or before 31 May 2007. After acceptance and execution of the agreements, Growers are bound by the Constitution by virtue of their participation in the Project.

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

32. The Responsible Entity is deemed to have received the 'Application Fee' as fees on acceptance of an 'Application' according to clause 3.5 and may invest all or part of the 'Application' money and 'Receipts' according to clause 6.

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

- general functions, powers and duties, clauses 6 to 9;
- deal with Receipts and other money in the Trust Account of the Grower, clause 11;
- complaints, clause 12;
- withdrawal from the Project, and buy-back or re-purchase of any Tree Right, clause 13;
- termination, clause 14;
- payments to Growers, clause 19; and
- compliance with rules laid down by the Responsible Entity, clause 22.

Custodian Agreement

34. The Custodian is to hold the 'Application Fee' and 'Project Property' as agent for the Responsible Entity in its capacity as a trustee for Applicants or Growers. Further, it will observe all of the usual duties and obligations of an agent acting in the best interest of its principal and in a professional and business like manner, according to clause 6.

Compliance Plan

35. As required by the *Corporations Act 2001*, the Responsible Entity 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.

36. The Responsible Entity must ensure, among other things, that it shall:

- send to each Grower financial information and other information, clauses 2.6 and 21.5;
- keep adequate records and copies of all contracts entered into on behalf of Growers, clause 6.1;
- appoints a 'Complaints Officer', clause 9.1; and
- requires the Manager to hold any Apricots forming part of the Project Property separate from other property, clause 12.4.

Sub-lease to RE

37. The Manager will lease both the 'New Property' and the 'Qew Property' under the Head Lease and Qew Lease for terms longer than the duration of the Project. Under the Sub-lease to RE, the Manager has entered into a sub-lease with the Responsible Entity granting various exclusive and non-exclusive rights over the land as set out in clause 2.

38. All leases will be registered against the relevant titles.

39. The Sub-Lessor has carried out all works and install all infrastructure necessary for the establishment of the Project on the 'New Property', clause 5.4. The Sub-Lessor will plant trees on the 'New Property' to a density of 138 trees per 'Apricot Lot', being 3 trees already existing on the 'Qew Property', 20 trees to be planted on the 'New Property' after 'Allotment' and prior to 26 June 2007 and the balance to be planted on the 'New Property' by 30 June 2008, clause 5.5.

Tree Right

40. Growers participating in the Project will enter into a 'Tree Right' with the Responsible Entity for the 'Term' of the Project. The Responsible Entity will grant to each Grower 'Tree Rights' over the 'Apricot Lot' which include the following under clause 2:

- access to the 'Apricot Lot';
- an exclusive right to access, use and enjoy the benefit of the trees;
- an exclusive right to harvest the apricots;
- an exclusive right to take all right, title and interest in the apricots; and
- access to and use of the 'Orchard' infrastructure, plant and equipment.

41. Other rights and obligations of the Grower and of the Responsible Entity are set out in clauses 2 to 6.

42. Under clause 4.1, the Responsible Entity is entitled to the 'Tree Right Fee' as described in clause 1.1 and Part 5 of the Schedule. In respect of the period from the 'Allotment' to 30 June 2007 the 'Tree Right Fee' will be included in the 'Application Fee'. In respect of the years ended 30 June 2008 and following, the 'Tree Right Fee' will be invoiced annually by 31 October.

43. After 30 June 2010, the 'Tree Right Fee' may be bought into line with the tree right fee for growers in the previous year's project.

44. If trees are destroyed or materially damaged, or a mineral or petroleum lease is established over the 'Apricot Lots', or the Grower and responsible Entity agree that it is no longer viable to carry out 'Apricot Farming' then the parties may terminate the obligations created by the Tree Right, clause 10.

Management Agreement

45. A Management Agreement is entered into between the Responsible Entity and each Grower, under which the Responsible Entity agrees to cause to be carried out during the 'Term', apricot farming on the 'Apricot Lots', processing and sale of the apricots.

46. The parties also agree that the Responsible Entity will provide the 'Initial Services' in respect of each Grower's 'Apricot Lot'. These services include:

- installation of drainage;
- inspection of the above ground components of the 'Irrigation System';
- checking that the training wire or mesh or other suitable support structure between the strainer posts is suitable for 'Apricot Farming'; and
- inspection and supervision of 'Initial Services' that are carried out by subcontractors.

47. The Responsible Entity must provide the 'Initial Services' during the period from 'Allotment' to 30 June 2007. Payment of the 'Application Fee' constitutes full payment for the services to be carried out by 30 June 2007.

48. The responsible Entity will perform the 'Initial Services' and 'Apricot Farming' in accordance with good horticultural and agricultural practices and in accordance with the requirements of clause 5.6.

49. The Responsible Entity will provide a written report to each Grower confirming that their 'Apricot Lots' have been established or substantially established in accordance with the Management Agreement, and a report concerning the potential market for the apricots by 30 June 2007. The Responsible Entity will also provide a written report to each Grower by 30 September each year in relation to the state of the Orchard and the report from the Horticultural Expert, clause 12.

50. The Responsible Entity is entitled to an annual 'Management Fee' as set out in Part 2 of the Schedule in consideration for the performance of its obligations.

51. The Grower appoints the Responsible Entity to sell (and to appoint the Orchard Manager to sell) apricots harvested from the Grower's trees, for the highest price practicable having regard to circumstances at the time, clause 8.

52. The Responsible Entity will be responsible for insuring the Orchard against public risk. The Responsible Entity is also required to keep insurance on behalf of the Growers insuring the 'Apricot Lots' against damage or theft of the apricots, damage to picked apricots resulting from cool-store breakdown or other plant breakdown, loss due to fortuitous circumstances, product liability and other such risks in respect of the 'Apricot Lots' and apricots in a manner consistent with the prevailing usual industry practice, clause 7.

Pooling of apricots and distribution of Proceeds

53. The Management Agreement sets out provisions relating to the pooling of Growers' apricots and the distribution of proceeds from that sale. This Product Ruling only applies where the following principles apply to those pooling and distribution arrangements:

- only Growers who have contributed apricots from a 'Harvest' to the pool are entitled to benefit from distributions from the proceeds of sale; and
- apricots can only be pooled with the apricots of Growers accepted to participate in the Project on or after 16 November 2006 and on or before 31 May 2007.

Project Fees

54. The Grower must pay an Application Fee of \$8,316 per 'Apricot Lot' payable on Application which will be applied towards the following:

- \$6,359 'Initial Services Fee' for services to be provided from the 'Commencement Date' to 30 June 2007;
- \$32 'Tree Right Fee' for the period from Allotment to 30 June 2007;

- \$825 'Irrigation Systems Fee'; and
- \$1,100 prepaid 'Orchard Maintenance Fee' for services to be provided in the period 1 July 2007 to 30 June 2009.

55. Under clause 4 and Part 2 of the Schedule to the Management Agreement and clause 4 and Part 5 of the Schedule to the Tree Right each Grower will make the following other payments per 'Apricot Lot':

For the year ending 30 June 2008:

- \$2,235 'Orchard Maintenance Fee' plus that sum which equals the 'Grower's Proportion' of the 'Net Proceeds to Growers' payable out of 'Net Proceeds to Growers';
- \$388 (indexed) 'Tree Right Fee';
- 'Grower's Proportion' of 'Processing Costs' (to the extent not already deducted from 'Gross Sale Proceeds'); and
- 'Marketing Fee' capped at \$152.90 (indexed). For the Financial Year up to and including Year 6, the fee is that proportion of the 'Marketing Fee' as the actual or anticipated harvest yield for the 'Financial Year' bears to peak forecast yield.

'Processing Costs' (to the extent not already deducted from 'Gross Sale Proceeds') and the 'Marketing Fee' are payable out of the balance of the 'Gross Sale Proceeds'.

For the year ending 30 June 2009:

- \$2,671 'Orchard Maintenance Fee';
- \$388 (indexed) 'Tree Right Fee';
- 'Grower's Proportion' of 'Processing Costs' (to the extent not already deducted from 'Gross Sale Proceeds');
- 'Marketing Fee' capped at \$152.90 (indexed). For the Financial Year up to and including Year 6, the fee is that proportion of the 'Marketing Fee' as the actual or anticipated harvest yield for the 'Financial Year' bears to peak forecast yield; and
- 'Variable Management Fee' being the 'Grower's Proportion' of that sum that equals 28% of the 'Net Proceeds to Growers', less a Base Management Fee and an amount equal to the 'Tree Right Fee' payable out of 'Gross Sale Proceeds'.

'Processing Costs' (to the extent not already deducted from 'Gross Sale Proceeds') and the 'Marketing Fee' are payable out of the balance of the 'Gross Sale Proceeds'.

For the year ending 30 June 2010 and following the same costs (indexed where applicable), except for:

- 'Orchard Maintenance Fee' is equal to the 'Grower's Proportion' of the cost or anticipated costs of 'Apricot Farming'; and
- for the years ending 30 June 2013 and following, a Deferred Management Fee for Year 1 being the 'Grower's Proportion' of that sum which equals 2% of 'Net Proceeds to Growers' for 10 'Financial Years' and a further Deferred Management Fee for Year 2 being the 'Grower's Proportion' of that sum which equals 2% of 'Net Proceeds to Growers' for 10 'Financial Years'.

56. Project agreements indicate, and the Manager has confirmed, that where 'Gross Sale Proceeds' are insufficient, Growers will be invoiced for the shortfall.

Finance

57. Each Grower can fund their involvement in the Project as follows:

- from their own financial resources;
- under a Terms Agreement with Primary Securities Ltd;
- by borrowing from Momentum Funding; or
- by borrowing from an independent lender.

58. Growers cannot rely on this Product Ruling if they enter into a finance package with Momentum Funding that materially differs from those provided to the Tax Office by the Manager as part of the application for this Product Ruling. This finance package is summarised below.

Terms Agreement

59. If Primary Securities Ltd accepts that the application fee can be paid under a Terms Arrangement the Grower must complete a terms application and Direct Debit Authority. The Grower will be required to pay their application fee as follows:

- An additional fee of \$824 for processing the Terms Payment Option;
- Growers must pay a deposit of \$1,100 on application;
- The balance of the Application Fee and the Processing Fee of \$8,040 by 12 monthly payments of \$670;
- Primary Security Ltd will take security over the Grower's Apricot lot(s); and

- There will be no interest levied to the Grower, unless instalments are not paid on time, then Primary Securities Ltd may charge a reasonable amount of interest, calculated on a daily basis from the due date until payment is received.

Finance by Momentum Funding

60. Momentum Funding may offer loans to Growers for the 'Application Fee' and also the 'Management Fee' for the years ended 30 June 2008, 2009 and 2010 (the 'additional advances'). The loan available to Growers is for 3 years interest only followed by 9 years principal & interest repayments.

61. The features of the loan include:

- the maximum interest only period will be 36 months from the initial loan draw down. For avoidance of doubt, principal repayments on the initial advance and any additional advance will commence at the latest on the 37th month following the initial advance;
- a loan establishment fee being 1% of the Loan amount required will be added to the loan to become the Initial Loan Amount;
- Momentum Funding will take security over the Growers 'Apricot Lot';
- the indicative interest rate is 11.25% per annum, that Momentum Funding may amend from time to time;
- an additional 3% interest per annum applies to overdue amounts due and payable;
- in the event of early repayment of a loan product or where a Grower elects for Momentum Funding to finance the 'additional advances' and subsequently finances these fees by other means, Growers will be liable for an administration fee not exceeding \$250 and break fees; and
- Growers who enter into these finance arrangements will be required to make equal monthly repayments of the outstanding balance, commencing at the end of the interest only period.

62. A Grower cannot rely on any part of this Product Ruling if the 'Application Fee', including amounts subject to a finance arrangement is not paid in full by 31 May 2007. Note that the Responsible Entity cannot accept an 'Application' that is subject to finance where finance is not approved, payment is not received and the funds are not cleared by the Custodian by 31 May 2007.

63. 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, other than Momentum Funding, are involved or become involved in the provision of finance to any Grower in the Project.

Ruling

Application of this Ruling

64. Subject to paragraph 8 and the specific exclusions set out in paragraphs 30, 58, 62, 63 of this Ruling, this Ruling will only apply to a Grower who is accepted to participate in the Project and who has executed a Management Agreement and a Tree Right on or after 16 November 2006 and on or before 31 May 2007.

65. 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

66. 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*.

67. 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

68. 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

69. 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 the 'Finance Application Fee' payable to Momentum Funding

Section 25-25

70. The 'Finance Application Fee' payable to Momentum Funding is a borrowing expense and is deductible under section 25-25. It is incurred for borrowing moneys that are used, or are to be used during that income year solely for income producing purposes. Borrowing expenses of \$100 or less are deductible in the year in which they are incurred (subsection 25-25(6)). Where the borrowing expense exceeds \$100 the deduction is spread over the period of the loan or 5 years, whichever is the shorter. The deductibility or otherwise of borrowing costs arising from loan agreements entered into other than those described in paragraphs 60 to 63 of this Ruling is outside the scope of this Ruling.

Deductions for the 'Initial Services Fee', the 'Tree Right Fee', the 'Orchard Maintenance Fee', 'Processing Costs', the 'Marketing Fee', the 'Variable Management Fee' and 'Interest'

Section 8-1

71. A Grower who is accepted to participate in the Project on or before 31 May 2007 may claim tax deductions under section 8-1 of the ITAA 1997, on a per 'Apricot Lot' basis, for the following expenditure.

Fee Type	Year ended 30 June 2007	Year ended 30 June 2008	Year ended 30 June 2009
'Initial Services Fee'	\$5,940 See Notes (i) & (ii)	Nil	Nil
'Tree Right Fee'	\$32 See Note (i)	\$388 (indexed) See Notes (i) & (iv)	\$388 (indexed) See Notes (i) & (iv)
'Orchard Maintenance Fee'	Nil See Note (iii)	As incurred See Notes (i), (iii) & (iv)	\$3,222 See Notes (i), (iii), (iv)
'Processing Costs'	Nil	As incurred (to the extent not already deducted from 'Gross Sale Proceeds') See Notes (i) & (iv)	As incurred (to the extent not already deducted from 'Gross Sale Proceeds') See Notes (i) & (iv)
'Marketing Fee'	Nil	As incurred See Notes (i) & (iv)	As incurred See Note (i) & (iv)
'Variable Management Fee'	Nil	As incurred See Note (i)	As incurred See Note (i)
Interest	As incurred See Note (v)	As incurred See Note (v)	As incurred See Note (v)

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) For the year ended 30 June 2007, the 'Initial Services Fee' payable on application is deductible to the extent shown in the table above in the year that it is incurred. The 'Initial Services Fee' payable on application is not deductible in full under section 8-1 as it consists of an amount of \$419 relating to cost of horticultural plant, cost of landcare and 'brand rights', which are capital in nature (see paragraphs 72 and 75 of this Ruling).
- (iii) The 'Orchard Maintenance Fee' payable on application is a prepayment and **not** deductible in full in the year incurred. Deductions for these amounts **must** be determined using the formula in subsection 82KZMF(1) of the ITAA 1936 (see paragraphs 103 to 112 of this Ruling). This provision operates to apportion expenditure over the eligible service period. The eligible service period extends from 1 July 2006 to 30 June 2008. Therefore an amount of \$2,784 per 'Apricot Lot' plus that sum which equals the 'Grower's Proportion' of the 'Net Proceeds to Growers' is deductible for the 'Orchard Maintenance Fee' in the year ending 30 June 2007 and an amount of \$3,222 per 'Apricot Lot' is deductible for the 'Orchard Maintenance Fee' in the year ending 30 June 2008.
- (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 to 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.
- (v) The deductibility or otherwise of interest arising from loan agreements entered into with financiers other than Momentum Funding is outside the scope of this Ruling. However all Growers, including those who finance their participation in the Project other than with Momentum Funding, should read the discussion of the prepayment rules in paragraphs 103 to 112 of this Ruling as those rules may be applicable if interest is prepaid. A Grower who chooses, or who is required to prepay interest under a loan agreement is outside the scope of this Ruling and may request a private ruling on the taxation consequences of participation in the Project.

Deductions for capital expenditure (Non-‘STS taxpayers’)**Division 40**

72. A Grower who is not an ‘STS taxpayer’ will also be entitled to tax deductions relating to water facilities (for example irrigation), a ‘landcare operation’, trees and for the ‘Processing Fee’ if the Grower elected to pay the ‘Initial Services Fee’ under the ‘Terms Agreement Option’. All deductions shown in the following Table are determined under Division 40.

Fee Type	ITAA 1997 Section	Year ended 30 June 2007	Year ended 30 June 2008	Year ended 30 June 2009
Water facility (eg dam, irrigation)	40-515	\$275 See Notes (vi) & (vii)	\$275 See Notes (vi) & (vii)	\$275 See Notes (vi) & (vii)
Landcare Operation	40-630	\$63 See Notes (vi) & (viii)	Nil	Nil
Establishment of horticultural plants (trees)	40-515	Nil See Notes (vi) & (ix)	Nil See Notes (vi) & (ix)	Nil See Notes (vi) & (ix)
Terms Payment Option ‘Processing Fee’	40-880	Must be calculated See Notes (vi) & (x)	Must be calculated See Notes (vi) & (x)	Must be calculated See Notes (vi) & (x)

Notes:

- (vi) If the Grower is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted for GST (for example input tax credits): Division 27.
- (vii) Any irrigation system, dam or bore is a ‘water facility’ as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. A deduction is available under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one third of the capital expenditure of \$825 per ‘Apricot Lot’ incurred by each Grower on the installation of the ‘water facility’ in the year in which it is incurred and one third in each of the next 2 years of income (section 40-540).

- (viii) Any capital expenditure incurred for a 'landcare operation' (as defined in section 40-635) is fully deductible in the year it is incurred under Subdivision 40-G, section 40-630.
- (ix) trees are a 'horticultural plant' as defined in subsection 40-520(2). As Growers hold a 'Tree Right' over the land, one of the conditions in subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the trees is determined using the formula in section 40-545 and is based on the capital expenditure of \$2,251 per 'Apricot Lot' incurred by the Grower that is attributable to their establishment. If the trees have an 'effective life' of greater than 13 but fewer than 30 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 13%. The deduction is allowable when the trees enter their first commercial season (section 40-530, item 2). The Manager will inform Growers of when the trees enter their first commercial season.
- (x) Under section 40-880 the 'Processing Fee' for the Terms Payment Option is deductible on a straight line basis over five income years (see paragraphs 114 and 115 of this Ruling).

Deductions for capital expenditure (STS taxpayers)***Subdivision 328-D and Subdivisions 40-F and 40-G***

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

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

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

Fee Type	ITAA 1997 Section	Year ended 30 June 2007	Year ended 30 June 2008	Year ended 30 June 2009
Water facility (eg dam, irrigation)	40-515	\$275 See Notes (xi) & (xii)	\$275 See Notes (xi) & (xii)	\$275 See Notes (xi) & (xii)
Landcare Operation	40-630	\$63 See Notes (xi) & (xiii)	Nil	Nil
Establishment of horticultural plants (trees)	40-515	Nil See Notes (ix) & (xi)	Nil See Notes (ix) & (xi)	Nil See Notes (ix) & (xi)

Notes:

- (xi) If the Grower is registered or required to be registered for GST, amounts of capital expenditure would need to be adjusted for GST (for example input tax credits): Division 27.
- (xii) Any irrigation system, dam or bore is a 'water facility' as defined in subsection 40-520(1), being used primarily and principally for the purpose of conserving or conveying water. If the expenditure is on a 'depreciating asset' (the underlying asset), the Grower may choose to claim a deduction under either Division 328 or Subdivision 40-F. For the purposes of Division 328, each Grower's interest in the underlying asset is deemed to be a 'depreciating asset'. The irrigation fee is \$825 per 'Apricot Lot'. If the 'cost' apportionable to that deemed 'depreciating asset' is less than \$1,000, the deemed asset is treated as a 'low-cost asset' and that amount is deductible in full when the underlying asset is first used or 'held' ready for use.

This is so provided the Grower is an 'STS taxpayer' for the income year in which it starts to 'hold' the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income. If the deemed asset is not treated as a 'low-cost asset', the tax deduction allowable in the year ended 30 June 2007 is determined by multiplying its 'cost' by half the relevant STS pool rate. At the end of the year, it is allocated to the relevant STS pool and in subsequent years the full pool rate will apply. If the expenditure is not on a 'depreciating asset', or if they choose to use Subdivision 40-F, Growers must claim deductions under Subdivision 40-F, paragraph 40-515(1)(a). This deduction is equal to one-third of the capital expenditure incurred by each Grower on the installation of the 'water facility' in the year in which it is incurred and one-third in each of the next 2 years of income (section 40-540).

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

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

76. A Grower who is an individual accepted into the Project by 31 May 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 each Grower for the income years ending **30 June 2007 to 30 June 2011**. 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.

Section 82KL and Part IVA

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

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

Commissioner of Taxation11 October 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?

78. For the amounts set out in the Tables above to constitute allowable deductions the Grower's horticulture activities as a participant in the Project must amount to the carrying on of a business of primary production.

79. Where there is a business, or a future business, the gross proceeds from the sale of the apricots 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.

80. For schemes such as that of the Project, Taxation Ruling TR 2000/8 sets out in paragraph 88 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.

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

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

82. In this Project, each Grower enters into a Tree Right and a Management Agreement.

83. Under the Tree Right each Grower will have rights over the land on which the trees will be planted. The Tree Right provides the Grower with an ongoing right to the trees for the term of the Project. Under the Tree Right the Grower must use the land in question for the purpose of carrying out horticultural activities and for no other purpose. The Tree Right allows the Responsible Entity to come onto the land to carry out its obligations under the Management Agreement.

84. Under the Management Agreement the Responsible Entity is engaged by the Grower to establish and maintain an 'Apricot Lot' during the term of the Project. The Responsible Entity (through engaging the services of the Manager and Orchard Manager) has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the 'Apricot Lot' on the Grower's behalf.

85. In establishing the 'Apricot Lot', the Grower engages the Responsible Entity to carry out 'landcare operations', install the above ground components of the irrigation system and to plant the trees on the Grower's 'Apricot Lot'. During the term of the Project, these assets will be used wholly to carry out the Grower's horticulture activities. The Responsible Entity is also engaged to harvest and sell, on the Grower's behalf, the apricots grown on the Growers' 'Apricot Lot'.

86. The general indicators of a business, as used by the Courts, are described in Taxation Ruling TR 97/11. Positive findings can be made from the Projects description for all the indicators.

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

88. The pooling of apricots grown on the Grower's 'Apricot Lot' with the apricots of other Growers is consistent with general horticulture practices. Each Grower's proportionate share of the sale proceeds of the pooled apricots will reflect the proportion of the 'Apricot' contributed from their 'Apricot Lot'.

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

90. The Grower's degree of control over the Responsible Entity as evidenced by the Management Agreement, and supplemented by the Corporations Act, is sufficient. During the term of the Project, the Responsible Entity will provide the Grower with regular progress reports on the Grower's 'Apricot Lot' 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.

91. The horticulture 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 Grower's horticulture activities in the Project will constitute the carrying on of a business.

The Simplified Tax System (STS)

Division 328

92. 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.

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

Deductions for the 'Initial Services Fee' and the 'Tree Right Fee'

Section 8-1

94. Consideration of whether the 'Initial Services Fee' and the 'Tree Right Fee' 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.

95. The 'Initial Services Fee' and 'Tree Right Fee' associated with the horticulture activities will relate to the gaining of income from the Grower's business of horticulture (see above), and hence have a sufficient connection to the operations by which income (from the regular sale of apricots) 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. Other than expenditure on 'landcare operations', horticultural plant and 'brand rights', there is no capital component found in the 'Initial Services Fee' and 'Tree Right Fee'. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

Interest deductibility**Section 8-1***(i) A Grower who uses Momentum Funding as the finance provider*

96. A Grower may finance their participation in the Project through a loan facility with Momentum Funding. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of the 'Orchard Maintenance Fees' and 'Tree Right Fees'.

97. The interest incurred for the year ended 30 June 2007 and in subsequent years of income will be in respect of a loan to finance the Grower's business operations – growing of apricots and the lease (or licence) of the land on which the trees will have been planted – that will continue to be directly connected with the gaining of 'business income' from the Project. Such interest will, therefore, have a sufficient connection with the gaining of assessable income to be deductible under section 8-1.

98. As with the 'Orchard Maintenance Fee', 'Processing Costs', the 'Marketing Fee', the 'Variable Management and 'Tree Right Fees', in the absence of any application of the prepayment provisions (see paragraphs 103 to 112 of this Ruling), the timing of deductions for interest will be different where a Grower is an 'STS taxpayer' who continues to use the 'STS accounting method'.

99. If the Grower is not an 'STS taxpayer' using the 'STS accounting method', interest is deductible in the year in which it is incurred.

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

(ii) A Grower who prepays interest or DOES NOT use Momentum Funding as the finance provider

101. The deductibility of interest incurred by a Grower who finances their participation in the Project through a loan facility with a bank or financier other than Momentum Funding 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.

102. While the terms of any finance agreement entered into between a Grower and financiers other than Momentum Funding are subject to commercial negotiation, those agreements may require interest to be prepaid. Alternatively, a Grower may choose to prepay such interest. Those Growers who choose, or who are required to prepay interest under a loan agreement are outside the scope of this Ruling and may request a private ruling on the taxation consequences of their participation in the Project (see paragraphs 103 to 112 of this Ruling).

Prepayment provisions***Sections 82KZL to 82KZMF***

103. 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.

104. For this Project, only section 82KZL of the ITAA 1936 (an interpretive provision) and sections 82KZME and 82KZMF of the ITAA 1936 are relevant. Where the requirements of sections 82KZME and 82KZMF are met, taxpayers determine deductions for prepaid expenditure under section 82KZMF using the formula in subsection 82KZMF(1). These provisions also apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes them from the operation of section 82KZMF.

Sections 82KZME and 82KZMF

105. Where 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. 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)).

106. 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.

107. 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 Momentum Funding. Although undertaken with an unrelated 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.

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

109. 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:

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

110. 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.

Application of the prepayment provisions to this Project

111. The expenditure incurred by a Grower in the Project for the 'Orchard Maintenance Fee' paid on application meets the requirements of subsections 82KZME(1) and (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.

112. The prepaid 'Orchard Maintenance Fee' incurred by each Grower does not fall within any of the five exceptions to section 82KZME of the ITAA 1936. Therefore, the deduction for each year is determined using the formula in subsection 82KZMF(1) of the ITAA 1936. Section 82KZMF apportions the deduction for prepaid 'Orchard Maintenance Fee' over the period that the services for which the prepayment is made are provided.

Expenditure of a capital nature

Division 40

113. Any part of the expenditure of a Grower that is attributable to acquiring an asset or advantage of an enduring kind is generally capital or capital in nature and will not be an allowable deduction under section 8-1. In this Project, expenditure attributable to water facilities, a 'landcare operation', the establishment of the trees and 'brand rights' is of a capital nature. All, excepting the latter expenditure, fall for consideration under Division 40.

Terms Payment Option Processing Fee

Section 40-880

114. Growers who elect to pay the 'Initial Services Fee' under the Terms Agreement option must pay a 'Processing Fee' of \$824. This expenditure does not constitute a borrowing expense and is therefore not deductible under section 25-25. As it is capital in nature it is also not deductible under section 8-1.

115. However, section 40-880 will allow the Processing Fee to be deducted on a straight line basis over five income years.

Section 40-880 applies to capital expenditure that is incurred in relation to a business and which is not taken into account elsewhere or denied deductibility under another provision of income tax law.

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

116. 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 2011** 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 2011:

- (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.

117. 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

118. 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.

Part IVA – general tax avoidance provisions

119. 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).

120. The 'Cool Climate Apricot 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 paragraphs 70 to 77 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.

121. 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 apricots. 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 participants 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; IT 360*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

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- ITAA 1997 Div 27
- ITAA 1997 Div 35
- ITAA 1997 35-10
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- ITAA 1997 35-55
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