


***PR 2007/13 - Income tax: Limestone Coast Vignettes Project - 2007 Development Vignette Owners (to 30 June 2007)***

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## Product Ruling

### Income tax: Limestone Coast Vignettes Project – 2007 Development Vignette Owners (to 30 June 2007)

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#### **ⓘ 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. 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.

#### **Terms of use of this Product Ruling**

This Product Ruling has been given on the basis that the entity(s) who applied for the Product 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 Product Ruling.

## What this Ruling is about

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1. This Product Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified in the Ruling section (below) apply to the defined class of entities, who take part in the scheme to which this Ruling relates. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated. In this Product Ruling this scheme is referred to as the 'Limestone Coast Vignettes Project' or simply as the 'Project'.

### Class of entities

2. This part of the Product Ruling specifies which entities can rely on the tax benefits set out in the Ruling section of this Product Ruling and which entities cannot rely on those tax benefits.

3. The class of entities who can rely on those tax benefits are referred to as Owners. Owners will be those entities that are accepted to participate in the scheme specified below on or after the date this Product Ruling is made and who have executed the relevant Project Agreements set out in paragraph 41 of this Ruling on or before 30 June 2007. They must 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.

4. The class of entities who can rely on the tax benefits set out in the Ruling section of this Product Ruling 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;
- are accepted into this Project before the date of this Ruling or after 30 June 2007;
- participate in the scheme through offers made other than through the Product Disclosure Statement;
- enter into finance arrangements with entities associated with the Project;
- have not paid the Application Money by 30 June 2007, where they have not entered into a finance arrangement; or
- have their application conditionally accepted by Ironstone RE Limited subject to finance for the payment of the application fee, where finance has not been approved by the lender or finance has been approved and the funds have not been made available to Ironstone RE Limited by 30 June 2007.

**Qualifications**

5. The class of entities defined in this Product Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 41 to 90 of this Ruling.

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

- this Product 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 Product Ruling may be withdrawn or modified.

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**Date of effect**

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8. This Product Ruling applies prospectively from 28 February 2007, the date this Product Ruling is made. It therefore applies to the specified class of entities that enter into the scheme from 28 February 2007 until 30 June 2007, being the closing date for entry into the scheme. This Product Ruling provides advice on the availability of tax benefits to the specified class of entities up to 30 June 2009.

9. However the Product Ruling only applies to the extent that:

- there is no change in the scheme or in the entity's involvement in the scheme;
- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

10. 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)).

11. 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.

12. 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).

## **Changes in the Law**

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

14. Entities who are considering participating in the scheme 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**

15. Product Rulings were introduced for the purpose of providing certainty about tax consequences for entities in schemes 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 Product Ruling is issued.

## **Goods and Services Tax**

16. All fees and expenditure referred to in this Product Ruling include the Goods and Services Tax (GST) where applicable. In order for an entity (referred to in this Ruling as a Owner) 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.

# **Ruling**

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## **Application of this Ruling**

17. Subject to the stated qualifications, this part of the Product Ruling sets out in detail the taxation obligations and benefits for an Owner in the defined class of entities who enters into the scheme described at paragraphs 41 to 90 of this Ruling.

18. The Owner's participation in the Project must constitute the carrying on a business of primary production. Provided the Project is carried out as described below, the Owner's business of primary production will commence at the time that:

- minimum subscription is reached during the period from the date of this Ruling to 30 June 2007;
- the Owner's application has been accepted; and
- the Project Agreements have been executed.

### **Minimum subscription**

19. An Owner is not eligible to claim any tax deductions until the Owner's application to enter the Project is accepted and the Project has commenced. Under the terms of the PDS, an Owner's application will not be accepted until the minimum subscription of 1,000 Vignettes is reached.

### **The Simplified Tax System (STS)**

#### ***Division 328***

20. To be an 'STS taxpayer', an Owner must be eligible to be an 'STS taxpayer' and must have elected to an 'STS taxpayer' (Division 328 of the ITAA 1997). For an Owner participating in the Project, the recognition of income and the timing of tax deductions is different depending on whether the Owner who was an 'STS taxpayer' prior to 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*.

21. For such Owners, 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***

22. For the first income year starting on or after 1 July 2005, Subdivision 61-J provides a 25% tax offset 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**

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

24. The Owner recognises ordinary income from carrying on the business of viticulture at the time that income is derived.

**Deductions for land purchase and development costs and Vineyard Operating Costs****Section 8-1**

25. An Owner may claim tax deductions for the following fees and expenses on a **per 'Vignette' basis**, as set out in the Table below.

Fee Type	Year ending 30 June 2007	Year ending 30 June 2008	Year ending 30 June 2009
<b>Land Purchase and development costs</b>	Nil See Note (ii)		
<b>Vineyard Operating costs</b>	Nil See Notes (i), (iii), (iv) & (v)	\$422 See Notes (i), (iii), (iv) & (v)	\$724 See Notes (i), (iii), (iv) & (v)

**Notes:**

- (i) If the Owner is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (ii) The amount of \$4,455 paid on application for the purchase and development of the land is capital in nature and not deductible under section 8-1 (see paragraph 32 of this Ruling).
- (iii) The Vineyard Operating Costs of \$1,870 paid on application for the period from 1 December 2007 to 30 June 2010, are prepaid and are not deductible in full in the year incurred. Deductions for these amounts must be determined using the formula in subsection 82KZMF(1) of the *Income Tax Assessment Act 1936* (ITAA 1936). Section 82KZMF operates to apportion expenditure over the eligible service period.  
  
The eligible service period for the Vineyard Operating Costs commences on 1 December 2007 and ends on 30 June 2010. Accordingly for each Vignette an amount of \$422 is deductible in the 2008 income year and an amount of \$724 is deductible in each of the 2009 and 2010 income years.

- (iv) The Vineyard Operating Costs notified to the Owner by the Responsible Entity for the 2011 income year and subsequent years are deductible in full in the year they are incurred.
- (v) This Ruling does not apply to Owners who choose to prepay the Vineyard Operating Costs (referred to in Note (iv)) or any other expenses not mentioned above. Subject to certain exclusions, 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 Owner who prepays such amounts may request a private ruling on the taxation consequences of their participation in the Project.

**Interest**

26. The deductibility or otherwise of interest incurred by Owners who finance their participation in the Project through a loan facility with an independent lender external to the Project is outside the scope of this Ruling. Such Owners may request a private ruling on the deductibility or otherwise of interest under finance arrangements not covered by this Product Ruling.

**Deductions for capital expenditure*****Division 40 and Division 328***

27. An Owner will be entitled to tax deductions relating to the trellising, irrigation system and the establishment of the grapevines. Deductions shown in the following Table are determined under Division 40.

<b>Fee type</b>	<b>ITAA 1997 section</b>	<b>Year ended 30 June 2007</b>	<b>Year ended 30 June 2008</b>	<b>Year ended 30 June 2009</b>
<b>Trellising</b>	40-25		Amount must be calculated See Notes (i) and (vi)	Amount must be calculated See Notes (i) and (vi)
<b>Irrigation</b>	40-515	\$323 See Notes (i) and (vii)	\$323 See Notes (i) and (vii)	\$323 See Notes (i) and (vii)
<b>Establishment of horticultural plants (grapevines)</b>	40-515	Nil See Notes ((i) and (viii))	Nil See Notes ((i) and (viii))	Nil See Notes ((i) and (viii))

**Notes:**

- (iv) The trellising is a depreciating asset as defined in section 40-30. The deduction, which is, the 'decline in value' of the asset is calculated using the formula in either subsection 40-70(1) (diminishing value method) or subsection 40-75(1) (prime cost method). Both formulas rely on the 'cost' and 'effective life' of the trellising.

The cost of the trellising is the amount of \$1,480 per Vignette paid by each Owner. Owners can either self-assess the effective life (section 40-105) or use the Commissioner's determination of effective life (section 40-100). The Commissioner has determined that trellising has an effective life of 20 years. The trellising will be installed and first used during the 2008 income year. The Responsible Entity will advise Owners when this occurs to enable Owners to calculate the deduction for the decline in value.

**STS taxpayers** will calculate the deduction for trellising under Division 328. For Division 328 to apply the Owner must be an 'STS taxpayer' for the income year in which it holds the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income. The tax deduction allowable in the 2008 income year is determined by multiplying the cost of the trellising by half the general STS pool rate. At the end of the year, the cost is allocated to the general STS pool and in subsequent years the full pool rate will apply (section 328-190).

- (v) The irrigation system meets the definition of 'depreciating asset' in section 40-30 and 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) for the capital expenditure incurred by each Owner on the installation of the irrigation system. This deduction is equal to one third of the capital expenditure in the year in which it is incurred and one third in each of the next two years of income (section 40-540).

**STS taxpayers** may choose to calculate their deduction under Division 40 (as discussed above) or under Division 328. For Division 328 to apply, the Owner must be an 'STS taxpayer' for the income year in which it holds the asset and the income year in which it first uses the asset or has it 'installed ready for use' to produce assessable income. The tax deduction allowable in the 2007 income year 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 (section 328-190).

- (vi) A 'horticultural plant' is a 'depreciating asset' as defined in section 40-30 and grapevines are 'horticultural plants' as defined in subsection 40-520(2). As Owners hold the land under a licence, one of the conditions in subsection 40-525(2) is met and a deduction for 'horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the grapevines is determined using the formula in section 40-545 and is based on the capital expenditure incurred that is attributable to their establishment. If the grapevines have an 'effective life' of greater than 13 but fewer than 30 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 13%. The deduction is allowable when the grapevines enter their first commercial season (section 40-530, item 2). The Responsible Entity will inform Owners of when the grapevines enter their first commercial season.

### **Trading stock**

#### **Section 70-35**

28. An Owner who is not an STS taxpayer will, in some years, hold grapes (or bulk wine) that will constitute trading stock on hand. Where, in an income year, the value of trading stock on hand at the end of an income year exceeds the value of trading stock on hand at the start of an income year an Owner must include the amount of that excess in assessable income.

29. Alternatively, where the value of trading stock on hand at the start of an income year exceeds the value of trading stock on hand at the end of an income year, an Owner may claim the amount of that excess as an allowable deduction.

30. The Responsible Entity will advise the Owner of the value of trading stock on hand at the end of the year.

#### **Section 328-285**

31. An Owner who is an STS taxpayer may, in some years, hold grapes (or bulk wine) that will constitute trading stock on hand. Where, for such an Owner, for an income year, the difference between the value of all their trading stock at the start and a reasonable estimate of it at the end, is less than \$5,000, they do not have to account for that difference under the ordinary trading stock rules in Division 70 (subsection 328-285(1)).

32. Alternatively, an Owner who is an STS taxpayer may choose to account for trading stock in an income year under the provisions of Division 70 (subsection 328-285(2)).

33. The Responsible Entity will advise the Owner of the value of trading stock on hand at the end of the year.

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

### ***Section 35-55 – exercise of Commissioner’s discretion***

34. An Owner who is an individual accepted into the Project by 30 June 2007 may have losses arising from their participation in the Project that would be deferred to a later income year under section 35-10. Subject to the Project being carried out in the manner described above, the Commissioner will exercise the discretion in paragraph 35-55(1)(b) for these Owners for the **2007 to 2011 income years**. This conditional exercise of the discretion will allow those losses to be offset against the Owner’s other assessable income in the income year in which the losses arise.

## **Section 82KL and Part IVA**

35. For a Owner who participates in the Project and incurs expenditure as required by the Constitution, 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.

## **Scheme**

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36. The scheme that is the subject of this Ruling is identified and described in the following documents:

- Application for Product Ruling as constituted by documents provided on 10 November 2006 and additional correspondence including emails received 1 December 2007 and 18 December 2006;
- Product Disclosure Statement (PDS), which includes the terms of the **Licence Agreement** and the **Land Sale Agreement** for the Limestone Coast Vignettes Project, dated 27 June 2005;
- Supplementary Product Disclosure Statement dated 14 October 2005;

- Additional Supplementary Product Disclosure Statement dated 9 October 2006;
- Draft **Constitution** of the Limestone Coast Vignettes Project, received 10 November 2006;
- Draft Compliance Plan for the Limestone Coast Vignettes Project, received 10 November 2006;
- Draft Custodian Agreement for the Limestone Coast Vignettes Project between Ironstone RE Limited (as Responsible Entity) and the Custodian, received 10 November 2006;
- Draft Resolution Agreement between Ironstone RE Limited and the Joint Venturer, received 10 November 2006;
- Joint Venture Agreement between Ironstone RE Limited and the Joint Venturer, dated 21 May 2004;
- Joint Venture Agreement between Ironstone RE Limited and the Joint Venturer, dated 14 August 2006;
- Option Agreement between the Landowner and the Joint Venturer, dated 14 August 2006;
- Draft Standby Option Agreement between the Landowner and the Ironstone RE Limited, received 10 November 2006;
- Draft Contract for the Sale and Purchase of Land between the Landowner and the Joint Venturer, received 10 November 2006;
- Draft Nomination Agreement between the Landowner, Joint Venturer and LC Land Proprietary Limited, received 10 November 2006;
- Draft Memorandum of Underlease for the Limestone Coast Vignettes Project between the Lessor and LC Land Proprietary Limited (as Underlessee), received 10 November 2006;
- Draft Community Title documents including the Decision Notification From, Conditions of Consent, Statement of Land Division Requirements, Scheme Description, By-Laws, Plan of Community Division, Application for Opinion and the Development Contract between Ironstone RE Limited and LC Land Proprietary Limited (as Developer), received 10 November 2006;
- Draft Grape Purchase Agreement between the Lessor and Ironstone RE Limited, received 10 November 2006; and

- Draft Vineyard Management Agreement between the Vineyard Manager and Ironstone RE Limited, received 10 November 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.

37. The documents highlighted (in bold) are those that an Owner 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 an Owner, or any associate of an Owner, will be a party to, which are a part of the scheme.

38. 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

39. The main features of the Limestone Coast Vignettes Project are as follows:

Location	Elgin Valley, South East Region of South Australia
Type of business to be carried on by each participant	Commercial growing of wine grapes for the purpose of harvesting and selling the produce (grapes and/or bulk wine)
Number of hectares offered for cultivation	67.4
Size of each Vignette	0.05 hectares
Number of vines per hectare	Approximately 2,020 vines
Term of the Project	Indefinite
Initial Cost per Vineyard Lot	\$6,325 (includes an amount for the purchase of land, prepaid fees for the 2008, 2009 and 2010 income years, irrigation, trellising and planting)
Ongoing and other costs	<ul style="list-style-type: none"> <li>• Annual Operating Costs</li> <li>• Bulk Wine Conversion cost (if applicable)</li> </ul>

40. The Project has been registered as a Managed Investment Scheme under the *Corporations Act 2001*. Ironstone RE Limited has been issued with Financial Services Licence Number 246672 and will be the Responsible Entity for the Project.

41. The Project involves the cultivation of grapevines and the harvest and sale of the grapes. The grapes may be converted to bulk wine at the discretion of the Responsible Entity.
42. An Owner that participates in the Project will do so by acquiring, after a process of subdivision, an equitable (or legal and equitable) interest in the Project which will consist of a minimum of one community lot (Vignette) of 0.05 hectares in a community title scheme set up under the South Australian *Community Titles Act 1996*.
43. An offer to participate in the Project will be made through a Product Disclosure Statement (PDS). The offer made under the PDS is for 67.4 hectares which corresponds to 920 Development Vignettes and 428 Mature Vignettes in the Project. The minimum subscription required under the PDS is 1,000 Vignettes. If the minimum subscription is not reached by 30 June 2007, the Responsible Entity will refund the Application Money and the Project will not proceed.
44. Applicants execute a Power of Attorney contained in the PDS. The Power of Attorney irrevocably appoints Ironstone RE Limited to enter into, on behalf of the Owner, any agreements required to hold an interest in the Project.
45. The Project will be conducted on land located on the Elgin Valley property, 20 kilometres east north east of Beachport in South Australia. Specifically, the property is described as Certificate of Title Register Book Volume 5666 Folio 44, being Allotment 20 in Deposited Plan 47351 in the Hundred of Symon in the area named Clay Wells.
46. **This Ruling only applies to participants whose application to purchase a Development Vignette(s) is accepted during the period from the 28 February 2007 to on or before 30 June 2007.** Product Ruling PR 2007/12 may apply to participants whose application to purchase a Mature Vignette(s) is accepted during the period from 28 February 2007 to on or before 30 June 2007.

### **Constitution**

47. The Constitution establishes the Project and operates as a deed binding on all Owners and Ironstone RE Limited. The Constitution sets out the terms and conditions under which Ironstone RE Limited agrees to act as Responsible Entity and thereby manage the Project. Upon acceptance into the Project, Owners are bound by the Constitution by virtue of their participation in the Project.
48. In order to acquire an interest in the Project, the Owner must make an application for a Vignette(s). Among other things, the application must be completed in a form approved by the Responsible Entity, signed by or on behalf of the Applicant, lodged at the registered office of the Responsible Entity and accompanied by the payment of the Application Money in a form acceptable to the Responsible Entity.

49. The Custodian will hold the Application Money on bare trust as agent for the Responsible Entity. Once the Responsible Entity has accepted the Owner's application and all of the Project agreements have been executed and remain in force, the Responsible Entity will instruct the Custodian to transfer the funds to be applied against the fees due under the Constitution.

50. If an Owner fails to contribute to operating expenses or is otherwise in breach of their obligations then the Responsible Entity may upon written notice to the Owner:

- suspend services to all or any of the Vignettes owned by the Owner;
- recover the Responsible Entity's time charges for executives at \$100 per hour (subject to CPI increase) and costs necessarily incurred in respect of the forfeiture;
- recover interest on the unpaid amount at the highest overdraft rate then charged by the MIS principal bankers to its customers;
- deduct the contribution and interest from any distribution otherwise payable to the Owner and apply that amount towards satisfaction of the contribution and interest;
- sue for the contribution and interest; and/or
- if the intention has been declared in the written notice, at any time until the matter is rectified declare the interest to be forfeited.

51. After an Interest is forfeited the Responsible Entity should:

- give to the Owner notice of the forfeiture;
- record the forfeiture and its date in the register of members; and
- either cancel the Interest or sell the Interest to any person willing to purchase at fair market value.

52. By signing the Application and Power of Attorney Form attached to the PDS, each Owner appoints any director of the Responsible Entity as their attorney to sell their forfeited Interest.

53. The Constitution also sets out provisions relating to:

- register of Owners, clause 24;
- Owners' income and distributions, clause 36;
- appointment of agents, clause 27;
- complaints handling, clause 47; and
- winding up the Project, clause 51.

**Pooling of grapes and distribution of proceeds**

54. The Constitution (clauses 35 and 36) and the PDS set out the rules relating to the pooling of Owners' grapes and the distribution of the proceeds from the sale of each pool. The grapes from the Development Vignettes will only be pooled with the grapes from the Mature Vignettes when the Development Vignettes reach their fifth year of development.

55. This Product Ruling only applies where the following principles apply to the pooling and distribution arrangements:

- only Owners who have contributed grapes are entitled to benefit from distributions of harvest proceeds from the pool; and
- any pooled grapes must consist only of grapes contributed by Owners of the same Project class.

56. The net proceeds from each pool will be distributed to the Owners on the last day of the financial year for which the net proceeds were calculated. Owners are entitled to a share of proceeds in each pool to which they have contributed. The Owner's share of the pool is based on the proportion of the grapes contributed from their Vignettes in relation to the total pool. In the event of total or partial destruction of the vines/grapes on their Vignettes, the Owner's entitlement in relation to the sales proceeds will be reduced accordingly.

**Compliance Plan**

57. As required by the Corporations Act, a Compliance Plan has been prepared for the Project. Its purpose 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 Owners are protected.

**Purchase of Land and Water Allocation**

58. The Project Land is currently owned by the Landowner and leased by the Lessor. The Responsible Entity has entered into a Joint Venture Agreement with the 'Joint Venturer' to establish the Project. The Joint Venturer has been granted an option to purchase the land and water allocations under an Option Agreement dated 14 August 2006, between the Joint Venturer and the Landowner. The option must be exercised on or before 30 June 2007. Under the Joint Venture Agreement, the Responsible Entity and the Joint Venturer will divide the land by a plan of community division under the South Australian *Community Titles Act 1996*.

59. The Joint Venturer will exercise the option to purchase the land and water allocation upon minimum subscription for the Project being reached. The Joint Venturer has nominated LCL Land Pty Ltd to hold the legal title of the land as bare trustee on trust for the Joint Venturer. If the option is only exercised over a portion of the property, the Joint Venturer may exercise the option again in relation to the remaining land.

60. After the settlement of the sale of land and water allocations to LCL Land Pty Ltd (as trustee for the Joint Venturer), LCL Land Pty Ltd (as appointed by the Responsible Entity) will lodge a community plan with the Lands Titles Registration Office (South Australia) and subdivide the portion of the land purchased into:

- Vignettes (community lots) of 0.05 hectares each; and
- appropriate areas of common property, to be used for access roads, water bores and sheds.

61. After the community titles are issued from the Land Titles Registration Office, Owners enter into a Sale Agreement for their Vignette(s) with LCL Land Pty Ltd (as trustee) and the Joint Venturer (as vendor). LCL Land Pty Ltd will retain legal title to the land as bare trustee of each Owner separately. However, an Owner may require LCL Land Pty Ltd to transfer the legal title of the land into the Owner's name at any time.

62. In the event that the Joint Venturer does not exercise the option to purchase the land, the Landowner has granted Ironstone RE Limited an option to purchase the land under the Standby Option Agreement. This option will be exercised on or before 30 June 2007.

## **Underlease**

63. The Lessor's lease over the Project land will be surrendered when the title to the land is transferred from the Landowner to LCL Land Pty Ltd. The Lessor will grant an Underlease to LCL Land Pty Ltd for the period from the date the option to purchase the land is exercised (by the Joint Venturer or Ironstone RE Ltd) to the date on which the land is transferred to LCL Land Pty Ltd.

## **Licence Agreement**

64. Owners participating in the Project will enter into a Licence Agreement with LCL Land Pty Ltd for the period from commencement (the later of minimum subscription or when the Owner's application for the land is accepted) to so long as LCL Land Pty Ltd retains title to the land. Under the Licence, Owners are permitted to use their Vignettes for the purpose of conducting their wine grape growing business upon the terms and conditions set out in the Licence.

65. The Licence also includes a right to the benefit of any water allocation held by LCL Land Pty Ltd in connection with the land.

**Management Agreement**

66. Under the Management Agreement, the terms of which are specified at Part 10 of the Project's Constitution, the Owner appoints Ironstone RE Limited to develop the Vignettes and provide ongoing management services.

67. The development of an Owner's Vignettes will commence on 1 July 2007 and will be completed by 30 November 2007. The development work includes:

- if necessary, obtain planning and development consents for the use of the Vignette as part of a vineyard;
- to install and repair boundary fences and gate(s), access road(s), windbreaks, headlands, culverts, irrigation, frost control and other service infrastructure on the Vineyard of which the Vignette is part;
- clearing the land and soil and contour preparation;
- installing a irrigation system, trellising and providing frost control; and
- planting vine rootlings.

68. The ongoing management services that will be provided include:

- procuring insurance against public and product liability;
- if required by an Owner and at the Owners own expense, the Responsible Entity may also negotiate insurance cover for the loss or destruction of the Owner's vines/grapes;
- manage watering, mulching, pruning, salinity, frost protection, stringing and training and pruning of vines, nutrition of vines, replacement of dead or defective vines and also keep down soil or plant diseases, weeds, pests and fire;
- supply such goods and materials as the Responsible Entity thinks reasonable;
- pay outgoings for rates, taxes, levies, electricity, water, diesel and other consumables. However, the Responsible Entity will not pay the municipal council rates for an Owner's Vignettes where the legal title of the Vignettes has been transferred to the Owner's name. In this situation, the Owner will be liable to pay its own municipal council rates;
- harvest grapes;

- as agent for the Owner, sell grapes harvested in such manner (as grapes or, after processing and storage, as bulk juice or wine) and at such times as the Responsible Entity thinks desirable in order to increase profits or minimise losses; and
- to any extent not otherwise required by law, give to the Owner at least once each calendar year a report on the management of the vineyard (clause 42 of the Constitution).

69. Under the Vineyard Management Agreement, the Responsible Entity will engage the Vineyard Manager, to carry out the above services on the terms and conditions contained in the agreement. The Vineyard Manager will be subject to the direction of the Responsible Entity in matters relating to the Vineyard Management Services.

70. For the services provided, the Owner will contribute the annual 'Vineyard Operating Costs', which are described at paragraphs 86 to 87 of this Ruling.

## **Fees**

71. Under the Constitution (clause 16) the Owner is required to pay the following:

- Application Money; and
- Vineyard Operating Costs.

72. These costs are described below.

## ***Application Money***

73. Application Money of \$6,325 per Vignette is payable on application. The Application Money will be applied towards the following:

- \$753 to purchase the land;
- \$166 for development costs for the period from 1 July 2007 to 30 November 2007;
- \$1,480 for trellising, to be installed during the period from 1 July 2007 to 30 June 2008;
- \$969 for irrigation, to be installed during the period from 1 July 2007 to 30 November 2007;
- \$1,087 for land preparation and vine planting to be conducted during the period from 1 July 2007 to 30 November 2007; and
- \$1,870 for Vineyard Operating Costs for the period from 1 December 2007 to 30 June 2010 (that is, \$550 for 1 December 2007 to 30 June 2008, \$660 for 1 July 2008 to 30 June 2009 and \$660 for 1 July 2009 to 30 June 2010).

***Vineyard Operating Costs***

74. Contributions for Vineyard Operating Costs are due annually in advance on 1 July, commencing on 1 July 2010. The Vineyard Operating Costs due are an estimate of the next income year's costs and will be notified to the Owner at about May of each year before each due date.

75. If the actual Vineyard Operating Costs for an income year exceed the estimated Vineyard Operating Costs for the income year, the Responsible Entity may recoup the shortfall in the following income year's contribution of Vineyard Operating Costs, or require Owners to pay the shortfall by 30 June. If the actual costs for the current income year are less than the total estimated, the Responsible Entity will credit the excess against the next income year's contribution to operating costs.

**Finance**

76. An Owner who does not pay the Application Money in full upon application can borrow from an independent lender external to the Project. An Owner who enters into a finance arrangement with an independent lender external to the Project may request a private ruling on the deductibility or otherwise of interest under the finance arrangement.

77. Owners cannot rely on any part of this Ruling if the Application Money is not paid in full on or before 30 June 2007 by the Owner or, on the Owner's behalf, by a lending institution. Where an application is accepted subject to finance approval by any lending institution, Owners cannot rely on this Ruling if written evidence of that approval has not been given to the Responsible Entity by the lending institution by 30 June 2007.

78. This Ruling does not apply if the finance arrangement entered into by the Owner 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
- the Responsible Entity or an 'associate' of the Responsible Entity (the word 'associate' has the meaning given in section 318 of the ITAA 1936) is involved or becomes involved in the provision of finance to Owners for the Project.

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**Commissioner of Taxation**

28 February 2007

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## **Appendix 1 – Explanation**

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**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 Owner carrying on a business?**

79. For the amounts set out in paragraphs 30 and 32 of this Ruling to constitute allowable deductions, the Owner's viticulture activities as a participant in the Limestone Coast Vignettes Project must amount to the carrying on of a business of primary production.

80. Two Taxation Rulings are relevant in determining whether an Owner will be carrying on a business of primary production.

81. The general indicators used by the Courts are set out in Taxation Ruling TR 97/11 Income tax: am I carrying on a business of primary production?

82. Taxation Ruling TR 2000/8 Income tax: investment schemes, particularly paragraph 89, is more specific to arrangements such as the Limestone Coast Vignettes Project. As Taxation Ruling TR 2000/8 sets out, the relevant principles have been established in court decisions such as *Commissioner of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

83. Having applied these principles to the arrangement set out above, an Owner in the Limestone Coast Vignettes Project is accepted to be carrying on a business of growing and harvesting grapes (and/or converting grapes to bulk wine) for sale.

### **The Simplified Tax System**

#### ***Division 328***

84. Subdivision 328-F sets out the eligibility requirements that an Owner must satisfy in order to enter the Simplified Tax System (STS) and Subdivision 328-G sets out the rules for entering and leaving the STS.

85. The question of whether an Owner 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 Owner 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 Vineyard Operating Costs**

### ***Section 8-1***

86. The Vineyard Operating Costs are deductible under section 8-1 (see paragraphs 43 and 44 of Taxation Ruling TR 2000/8). A 'non-income producing' purpose (see paragraphs 47 and 48 of Taxation Ruling TR 2000/8) is not identifiable in the arrangement and there is no capital component evident in the Vineyard Operating Costs.

87. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply. Provided that the prepayment provisions do not apply, a deduction for these amounts may be claimed in the year in which they are incurred (Note: the meaning of incurred is explained in Taxation Ruling TR 97/7).

## **Prepayment provisions**

### ***Sections 82KZL to 82KZMF***

88. 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.

89. For this Project, the only prepayment provisions that are relevant are section 82KZL of the ITAA 1936 (an interpretive provision) and sections 82KZME and 82KZMF of the ITAA 1936 (operative provisions).

### ***Application of the prepayment provisions to this Project***

90. The expenditure incurred by an Owner in the Project for the Vineyard Operating Costs for the 2008, 2009 and 2010 income years 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.

91. The prepaid Vineyard Operating Costs incurred by Owners do not fall within any of the 5 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 will apportion the deduction for prepaid Vineyard Operating Costs over the period that the services for which the prepayment is made are provided.

92. The Vineyard Operating Costs for the 2011 income year onwards are incurred annually. Accordingly the prepayment provisions in sections 82KZME and 82KZMF of the ITAA 1936 have no application to these amounts.

93. However, sections 82KZME and 82KZMF of the ITAA 1936 may also have relevance if an Owner in this Project prepays all or some of the costs referred to in paragraph 104 of this Ruling or prepays interest under a loan agreement. Where such a prepayment is made these prepayments provisions will also apply to 'STS taxpayers' because there is no specific exclusion contained in section 82KZME that excludes them from the operation of section 82KZMF.

94. Owners who prepay any fees or interest are not covered by this Product Ruling and may instead request a private ruling on the tax consequences of their participation in this Project.

### **Expenditure of a capital nature**

#### ***Division 40 and Division 328***

95. Any part of the expenditure of an Owner 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 the trellising, the irrigation system and the establishment of the grapevines is of a capital nature. This expenditure falls for consideration under Division 40 or Division 328.

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

97. The tax treatment of capital expenditure has been dealt with in a representative way in the Table and the accompanying notes of paragraph 32 of this Ruling.

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

#### ***Section 35-55 – exercise of Commissioner's discretion***

98. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the 2007 to 2011 income years, 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 the 2007 to 2011 income years:

- it is because of its nature the business activity of a Owner will not satisfy one of the four tests in Division 35; and

- there is an objective expectation that within a period that is commercially viable for the viticulture industry, an Owner's business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

99. An Owner who would otherwise be required to defer a loss arising from their participation in the Project until a later income year under subsection 35-10(2), is able to offset that loss against their other assessable income.

100. 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, an Owner will need to apply for a private ruling on the application of section 35-55 to those changed circumstances.

## **Section 82KL– recouped expenditure**

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

## **Part IVA – general tax avoidance provisions**

102. 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).

103. The Limestone Coast Vignettes Project will be a 'scheme'. An Owner will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 30 and 32 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.

104. Owners to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the grapes. There are no facts that would suggest that Owners have 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**

105. The following is a detailed contents list for this Ruling:

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## References

### *Previous draft:*

Not previously issued as a draft

### *Related Rulings/Determinations:*

TR 97/7, TR 97/11; TR 98/22;  
TR 2000/8; TR 2001/14;  
TR 2002/6, TR 2002/11;  
PR 2007/12

### *Subject references:*

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

### *Legislative references:*

- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
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- ITAA 1936 82KZMD
- ITAA 1936 82KZME
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