


PR 2007/50 - Income tax: Primary Yield Lamb Project 2007

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Product Ruling

Income tax: Primary Yield Lamb Project 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

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 Primary Yield Lamb Project 2007 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 Graziers. Graziers 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 38 of this Ruling on or before 31 May 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 31 May 2007;
- do not pay the Application Money in full on or before 31 May 2007;
- participate in the scheme through offers made other than through the Information Memorandum;
- participate in the scheme through offers which do not qualify as a small scale offering as defined in section 1012E of the *Corporations Act 2001*; and
- enter into finance arrangements with Environinvest Ltd or entities associated with this Project (the word 'associate' has the meaning given in section 318 of the *Income Tax Assessment Act 1936* (ITAA 1936)).

Superannuation Industry (Supervision) Act 1993

5. This Product ruling does not address the provisions of the *Superannuation Industry (Supervision) Act 1993* (SISA 1993). The Tax Office gives no assurance that the product is an appropriate investment for a superannuation fund. The trustees of superannuation funds are advised that no consideration has been given in this Product Ruling as to whether investment in this product may contravene the provisions of SISA 1993.

Qualifications

6. 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 38 to 89 of this Ruling.

7. 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

9. This Product Ruling applies prospectively from 30 May 2007, the date this Product Ruling is made. It therefore applies only to the specified class of entities that enter into the scheme from 30 May 2007 until 31 May 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 for the income years up to 30 June 2009.

10. 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.

11. 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)).

12. 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.

13. 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

14. Although this Product Ruling deals with the laws enacted at the time it was issued, later amendments to the law 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.

15. 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

16. 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

17. 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 *Grazier*) 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

Application of this Ruling

18. Subject to the stated qualifications, this part of the Product Ruling sets out in detail the taxation obligations and benefits for a Grazier in the defined class of entities who enters into the scheme described at paragraphs 38 to 89 of this Ruling.

19. The Grazier's participation in the Project must constitute the carrying on of business of primary production. Provided the Project is carried out as described below, the Grazier's business of primary production will commence at the time of execution of their Management Agreement, Lease Agreement and Agistment Agreement, on or before 31 May 2007.

Minimum subscription

20. A Grazier is not eligible to claim any tax deductions until the Grazier's application to enter the Project is accepted and the Project has commenced. Under the terms of the Information Memorandum, a Grazier's application will not be accepted and the Project will not proceed until applications in respect of 11,000 Stock in aggregate are achieved.

The Simplified Tax System (STS)

Division 328

21. To be an 'STS taxpayer' a Grazier must be eligible to be an 'STS taxpayer' and must have elected to be an 'STS taxpayer' (Division 328 of the ITAA 1997). For a Grazier participating in the Project, the recognition of income and the timing of tax deductions is different depending on whether the Grazier was an 'STS taxpayer' prior to 1 July 2005 and 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*.

22. For such Graziers, 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

23. 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

Sections 6-5 and 17-5

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

Trading stock

Sections 70-35, 70-45 and 70-55

25. A Grazier who is not an 'STS taxpayer' may, in some years, hold Progeny, wool or skin 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 a Grazier must include the amount of that excess in assessable income.

26. 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, a Grazier may claim the amount of that excess as an allowable deduction.

27. Under section 70-45, the Grazier can elect to value trading stock on hand at the end of the income year at cost, market selling value or replacement value. Where the Grazier elects to value the trading stock at the end of the income year at cost, 'cost' would include only those expenses incurred until the Progeny, wool or skin became trading stock of the Grazier.

28. Under section 70-55, where the Grazier holds trading stock, being Progeny, that the Grazier acquired by natural increase, the Grazier can elect to value the cost of that Progeny at the actual cost of each animal or the cost prescribed by the regulations for each animal in the applicable class of livestock.

Section 328-285

29. A Grazier who is an 'STS taxpayer' may, in some years, hold Progeny, wool or skin that will constitute trading stock on hand. Where, for such a Grazier, for an income year, the difference between the value of all their trading stock at the start of an income year and a reasonable estimate of it at the end of the income year, 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)).

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

Deduction for Initial Management Fee, ongoing Management Fees, Third Party Expenses, Performance Bonus Fee, Lease Fee and Agistment Fee

Section 8-1 and Division 27 of the ITAA 1997 and sections 82KZME and 82KZMF of the ITAA 1936

31. A Grazier may claim tax deductions for the following fees and expenses on a per Stock 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
Initial Management Fee	\$91.30 See Notes (i) & (ii)	Nil	Nil
Ongoing Management Fees	Nil	\$31.90 plus indexation See Notes (i), (iii) & (iv)	\$20.90 plus indexation See Notes (i), (iii) & (iv)
Lease Fees	Nil	\$5.40 plus indexation See Notes (i), (iii) & (iv)	\$5.40 plus indexation See Notes (i), (iii) & (iv)
Agistment Fees	Nil	\$26.40 plus indexation See Notes (i), (iii) & (iv)	\$26.40 plus indexation See Notes (i), (iii) & (iv)
Third Party Expenses	Nil	As incurred See Notes (i), (iii) & (iv)	As incurred See Notes (i), (iii) & (iv)
Performance Bonus Fee	Nil	As incurred See Notes (i), (iii) & (iv)	As incurred See Notes (i), (iii) & (iv)

Notes:

- (i) If the Grazier is registered or required to be registered for GST, amount of outgoings would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (ii) The Initial Management Fee of \$91.30 per Stock is for initial management services, to be provided during the period from the Commencement date to 30 June 2007 and is deductible in the income year ending 30 June 2007.
- (iii) Where the Grazier pays the ongoing Management Fees, Lease Fees, Agistment Fees, Third Party Expenses and Performance Bonus Fee, in the relevant income years shown in the above table and set out in the Management, Lease and Agistment Agreements, those fees are deductible in full under section 8-1 in the year that they are incurred.
- (iv) This Ruling does not apply to Graziers who choose to prepay fees. 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 Grazier who prepays such amounts may request a private ruling on the taxation consequences of their participation in the Project.

Interest

32. The deductibility or otherwise of interest incurred by Graziers who finance their participation in the Project through a loan facility is outside the scope of this Ruling. Such Graziers may request a private ruling on the deductibility or otherwise of interest under such finance arrangements.

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

33. A Grazier 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.

34. Financial projections by Environinvest indicate that in each year of the Scheme the assessable income test in section 35-30 will be met.

35. Where a Grazier satisfies the assessable income test in an income year the Grazier will not be required to defer any loss attributable to their business activity, to a later year. Instead, this loss can be offset against other assessable income of the Grazier for the year in which the loss arises.

36. However, if a Grazier either fails to pass the assessable income test in the income year ended 30 June 2007 or later, or fails to pass one of the other tests in Division 35, they should seek a private ruling on how Division 35 will apply to their business activity for that income year.

Prepayment provisions and anti-avoidance provisions

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

37. For a Grazier who commences participation in the Project and incurs expenditure as required by the Management, Lease and Agistment Agreements, the following provisions of the ITAA 1936 have application as indicated:

- expenditure by a Grazier does not fall within the scope of sections 82KZME and 82KZMF (but see paragraphs 103 to 107 of this Ruling);
- 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

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

- Application for a Product Ruling received 2 January 2007 as constituted by documents received on 6 February; and additional correspondence, emails dated 14 February 2007, and 23 March 2007 and 5, 17, 18, 26, April 2007 and 1, 2, 3, and 4 May 2007;
- New application for a Product Ruling received 7 May 2007 as constituted by documents received 1, 2, 3 and 4 May and additional correspondence and emails dated 7, 8, 9, 11, 14, 15, 16, 17, 18, 21 and 22 May 2007;
- Information Memorandum for the Primary Yield Lamb Project 2007, to be issued by Environinvest Ltd (Environinvest) as Responsible Entity, received on 21 May 2007;

- Draft **Constitution** of the Primary Yield Lamb Project 2007, received 22 May 2007;
- Draft **Lease Agreement** between Environinvest and the Grazier received 18 May 2007;
- Draft **Agistment Agreement** between Environinvest and the Grazier received 18 May 2007;
- Draft **Management Agreement** between Environinvest and the Grazier received 22 May 2007;
- Farmer Management Agreement between Environinvest and the Farmer received 26 April 2007;
- Stock Lease Agreement between Environinvest and the Farmer received 2 January 2007;
- Farmer Agistment Agreement between Environinvest and the Farmer received 2 January 2007;
- Operations Management Agreement between Environinvest and Ausfarm Management Pty Ltd (Ausfarm), received 2 January 2007; and
- Draft Operations Agreement between Environinvest and Agriculture and Forestry Managers Pty Ltd (AFM).

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

39. The documents highlighted are those that a Grazier 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 Grazier, or any associate of a Grazier, will be a party to, which are a part of the scheme.

40. This Ruling does not apply unless the Grazier accepts a personal offer made in accordance with subsection 1012E(5) of the Corporations Act and does not breach the ceilings set in subsections 1012E(6) and (7) of the Corporations Act. Each of these categories is explained in paragraphs 90 to 93 of this Ruling.

41. 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

42. The main features of the Primary Yield Lamb Project 2007 are as follows:

Location	Kojonup in the south west of Western Australia and Cunnamulla in southern Queensland.
Type of business each participant will be carrying on	Medium term commercial breeding and production of lambs, wool and skin and selling for profit.
The term of the Project	7 Subsequent Years after the Application Year
Number of ewes involved in the breeding program	Up to 14,000 ewes (Stock)
Size of each Stock	1 ewe
Minimum allocation per Grazier	300 Stock
Minimum Subscription	11,000 Stock
Initial Cost	\$91.30 per Stock
Ongoing costs	<ul style="list-style-type: none"> • Ongoing Management Fees, Performance Bonus Fee and Third Party Expenses payable to the Responsible Entity for performing the services in each Subsequent Year. • Lease Fee for the lease of the Grazier's Stock. • Agistment Fees to agist the Grazier's Stock on the Land. • Taxes, levies, excise charge or duty imposed in entering into the Agreements.

43. The Project will involve the Grazier in carrying on a business of leasing, grazing sheep and for the production of lamb meat, wool and skin for sale.

44. A personal offer to participate in the scheme will be made through an Information Memorandum. A Grazier that participates in the Project will do so by acquiring an Interest in the Project which consists of a minimum of 300 Grazier Stock.

45. Applicants must complete and sign the Application Form and Power of Attorney contained in the Information Memorandum and make together with the Application Form a payment in full of the Initial Management Fee.

46. The Power of Attorney irrevocably appoints Environinvest to enter into, on behalf of the Grazier, a Lease Agreement, Agistment Agreement and Management Agreement and any other documents required to hold an interest in the Project.

47. Under the terms of the Information Memorandum, the Project will not proceed unless applications for at least 11,000 Stock are received and accepted. The Responsible Entity reserves the right to refuse any application to subscribe for an Interest in the Project.

48. This ruling only applies to Graziers who are accepted to participate in the Project and who have executed the Lease Agreement, the Agistment Agreement and the Management Agreement from the date of this ruling issued to 31 May 2007.

49. A Grazier will enter into a Lease Agreement with Environinvest. The Lease will comprise contractual rights in relation to the Grazier's Stock. Each Grazier will lease a minimum of 300 Stock on the terms and conditions of this agreement.

50. A Grazier will also be granted a licence under an Agistment Agreement to enter onto the Land for the purposes agisting the Grazier's Flock.

51. Under the Management Agreement each Grazier will engage Environinvest as manager of the Grazier's Business to carry out the services under the agreement during the term of the Project.

Constitution

52. The Constitution establishes the Project and each Grazier irrevocably appoints the Responsible Entity as its agent, representative and attorney in relation to the Project, subject to the terms and conditions of the Constitution and the Project Documents, clause 3.

53. The Responsible Entity will hold bank accounts for the Project, where the Responsible Entity will deposit the Application Money and all money generated from each Grazier's Business and the Project on behalf of the participants, clause 4.

54. To be a Grazier and be issued an interest in the Project, clause 5 states that an Applicant must:

- have made an application in the appropriate form as provided by clause 7;
- have been accepted by the Responsible Entity pursuant to clause 8; and
- either personally or by its attorney have entered into all of the necessary Project Documents with the Project Documents remaining in force.

55. This Product Ruling will only apply to Graziers who have their application for an Interest in the Project accepted, project documents executed, issued an Interest and application Money transferred to the Responsible Entity on or before 31 May 2007.

56. Among the other things, the Constitution sets out details summarised as follows:

- the issue to each Grazier of a numbered Certificate setting out details of the Grazier, the Project, the Class of interest in the Project held by the Grazier and the number of Stock subscribed for by the Grazier, clause 10;
- the Responsible Entity's powers and duties, clause 14;
- the setting up and maintenance of a Register of Graziers, clause 15;
- the Responsible Entity's ability to appoint agents, clause 16;
- the Responsible Entity's entitlement to be receive remuneration, clause 17;
- procedures relating to the collection of all proceeds, deductions from the proceeds, and distribution of the proceeds, clause 18;
- resolution of complaints made by the Graziers in relation to the Project or the Responsible Entity, clauses 19 and 20;
- assignment of a Grazier's interest, clause 24;
- retirement and removal of the Responsible Entity, clause 26;
- procedures for calling a meeting of Graziers, clause 29; and
- events and procedures for winding up the Project, clause 33.

Lease Agreement

57. Graziers participating in the scheme will enter into a Lease Agreement with Environinvest to lease a minimum of 300 Stock from the Commencement Date until 30 June in the seventh Subsequent Year, clause 2.

58. Under clause 3 Environinvest is entitled to be paid, or reimbursed from the Grazier's Entitlement, the Lease Fee. Refer to paragraph 84 of this Ruling for details of the Lease Fee.

59. Environinvest warrants that the Grazier's Stock will be free from all abnormalities or genetic defects or deficiencies likely to have a detrimental effect on the Grazier's Stock or the Grazier's Progeny, clause 5.

60. Pursuant to clause 4 the Grazier covenants with Environinvest to ensure that:

- the Grazier's Stock remains free from any illness, disease or parasite;
- the Grazier's Stock receive all necessary pasture, feeding and supplementary feeding and water supplies to maintain the Stock in good condition and health in accordance with accepted animal husbandry practices of the sheep farming industry; and
- upon termination or expiry of this Agreement, or upon the retirement of any of the Grazier's Stock, to return the Grazier's Stock to Environinvest.

61. The Grazier acknowledges that Environinvest may replace the Grazier's Stock with Stock from Reserve Ewes, provided it is in the best interests of the Grazier. Environinvest will update the Register by substituting the initial Sock Identifiers listed in the Register with the Sock Identifiers for the Reserve Ewes, clause 4.2(a).

62. In each Subsequent Year Environinvest, without prior notification to the Grazier, may require the Grazier to sell to Environinvest up to 60% of the Grazier's ewe Progeny that are born in that Subsequent year. The Grazier must sell that ewe Progeny to Environinvest at a price equal to the average price Environinvest obtains for the sale of Cast-for-age ewes, clause 4.2(b).

63. Environinvest warrants that by 20 June of the Application Year the Grazier's Stock will be pregnancy tested and that all the Grazier's Stock will be found to be pregnant. Prior to 20 June in each Subsequent Year, Environinvest will replace any of the Grazier's Stock which have died, are not pregnant or unsuitable for breeding, with sheep found to be pregnant, clause 5.

Agistment Agreement

64. Environinvest will licence Land for the Project in Kojonup in the south west of Western Australia and Cunnamulla in southern Queensland. Specifically, the property in Kojonup is described as house block number 7083 and the property in Cunnamulla is described as 4490 RDP I1 KU14 & L3 KU18:Parish/Cotto Prop I.D. 3014077 in the Shire of Paroo.

65. From the Commencement Date until 30 June in the seventh Subsequent Year, the Grazier will be granted a licence to enter onto the Land for the purpose of agisting the Grazier's Flock (Stock and Progeny), clause 2.1.

66. Under clause 3 Environinvest is entitled to be paid, or reimbursed from the Grazier's Entitlement, the Agistment Fee. Refer to paragraph 84 of this Ruling for details of the Agistment Fee.

67. The Grazier and Environinvest covenant that the Grazier's Flock will not exceed the carrying capacity of the Land, clauses 4.1(b) and 5(c).

68. Among other things, the Agistment Agreement sets out details summarised as follows:

- the Grazier's and Environinvest covenants how the Project will be conducted, clause 4 and 5;
- the ability for Environinvest to sub-contract out any of the services it has agreed to perform under this agreement, clause 6;
- the power for Environinvest to impose interest on amount not paid, clause 10; and
- events and consequences of Event of Default and Termination, clause 11.

Management Agreement

69. Under clause 3 the Grazier appoints Environinvest to manage the Grazier's Business and to carry out the management services subject to the terms and conditions of the Agreement. The Agreement will commence on the Commencement Date and shall continue until its termination under clause 3.

70. Environinvest will commence the provision of the initial management services on or after the Commencement Date and will use all reasonable endeavours to complete the initial management services on or before 30 June 2007, clause 4.1.

71. The initial management services include, amongst other things:

- assess the Grazier's Stock for pregnancy;
- select the Grazier's Stock and complete the Annexure to the Lease Agreement;
- maintain standard and necessary breeding information and records in respect of the Grazier's Stock;
- prepare relevant marketing reports; and
- provide all reasonable services required in respect of crutching and vaccination of the Grazier's Stock.

72. Environinvest will provide management services of each Subsequent Year and shall continue to provide the ongoing management services until the termination of this Agreement, clause 4.2.

73. The ongoing management services provided to the Grazier in each Subsequent Year include, amongst other things:

- selection and induction of any replacement of the Grazier's Stock as required under the Lease Agreement;
- managing the selection and joining of the Grazier's Stock;
- pregnancy testing of the Grazier's Stock;
- the effective identification of the Grazier's Stock and Progeny to ensure correct identification of ownership and accurate recording of livestock;
- weaning of the Grazier's Progeny;
- providing the necessary feed and ancillary services required to rear the Grazier's Progeny for the purpose of sale;
- providing all reasonable services required in respect of shearing and crutching of the Grazier's Stock; and
- pooling the Grazier's Progeny with other Progeny for the purpose of sale of the Product (which the Grazier expressly authorises Environinvest to do).

74. Under clause 5 Environinvest is entitled to be paid, or reimbursed from the Grazier's Entitlement, the Initial Management Fee, Management Fee, Performance Bonus Fee and Third Party Expenses. Refer to paragraph 84 of this Ruling for details of these fees.

75. Environinvest will on or prior to 31 May of each Subsequent Year prepare a report for the Grazier containing an estimate of the Grazier's Entitlement and the fees, costs and expenses likely to be payable by the Grazier in accordance with the Project Documents for that Subsequent Year, clause 9(b).

76. Environinvest will pay to the Grazier the Grazier's Entitlement, after the deduction by Environinvest of all fees and expenses for which the Grazier is liable for under this Agreement, the Lease Agreement, the Agistment Agreement and the Constitution, by the end of the Subsequent Year in which the Sale Proceeds are received, clause 6.3.

Third Party Agreements

77. The Responsible Entity will enter into the following third party agreements.

Stock Lease Agreement

78. The Responsible Entity will enter into this agreement to secure rights in respect of Stock in order to grant to the Grazier a lease under the Lease Agreement. The Farmer must ensure that the Stock are tested pregnant in lamb and must replace any Stock that do not test pregnant between 15 June 2007 and 20 June 2007 and prior to the Breeding Season each Financial Year.

79. Subject to the direction, supervision and consent of Environinvest, the Farmer will retire and sell any Stock that, in accordance with accepted livestock practices are unfit for breeding, provided always that the Farmer replaces the equivalent number of Stock at the start of each Breeding Season from the Reserve Ewes that test pregnant.

80. Under the terms of this agreement Environinvest, prior to each Breeding Season, must sell to the Farmer an equivalent number of female Progeny produced by the Grazier's Stock to replace any Stock that die or are sold during the immediately proceeding Breeding Season. The Progeny sold to the Farmer will become part of the Reserve Ewes. Environinvest shall not be required to sell more than 60% of the ewe Progeny produced by the Grazier's Stock.

Farmer Agistment Agreement

81. The Responsible Entity will enter into this agreement to secure a non-exclusive licence to use the Land for the purposes of agisting the Flock. The Farmer covenants with the Responsible Entity:

- that the land has sufficient pasture and feed to maintain the Flock for each Breeding Season in each Financial Year for the term of this Agreement;
- to give priority to the Flock and their requirements for sufficient pasture over any other livestock or farming activities undertaken on the Land;
- to manage and maintain the Land in accordance with accepted livestock industry practices; and
- not to run livestock other than the Stock, Progeny and Reserve Ewes on the Land such that the stocking rate of the Land is exceeded.

Farmer Management Agreement and Operations Management Agreement

82. The Responsible Entity will enter into these agreements to appoint the Farmer and Ausfarm as independent contractors to provide services on the terms and conditions set out in the relevant agreements.

Pooling of Produce and Grazier's Entitlement to Net Proceeds

83. Clause 6 of the Management Agreement and clause 18 of the Constitution set out provisions relating to the Grazier's Entitlement to participate in the Sale Proceeds from the sale of Produce. This Product Ruling only applies where the following principles apply to the pooling and distribution arrangements:

- only Graziers whose Business activities have contributed Sale Proceeds into the proceeds fund are entitled to benefit from distributions from the pool; and
- any pooled Produce must consist only of Produce contributed by Graziers of Primary Yield Lamb Project 2007.

Fees

84. Under the terms of the Management Agreement, Lease Agreement and Agistment Agreement, a Grazier will make payments as described below on a per Stock basis.

Fees payable under clause 5 of the Management Agreement

- **Initial Management Fee** of \$91.30 per Stock payable on application to Environinvest for services to be provided from the Commencement Date up to 30 June 2007;
- **Management Fee** of \$31.90 per Stock, varied by indexation, payable out of Grazier's Entitlement for ongoing management services to be provided in the first Subsequent Year from 1 July 2007 up 30 June 2008. Following the first Subsequent Year and up to and including the final Subsequent Year, Management Fee of \$20.90 per Stock, varied by indexation, is payable out of Grazier's Entitlement;
- Grazier's share of **Third Party Expenses** as determined by Environinvest, payable in each Subsequent Year out of Grazier's Entitlement; and
- **Performance Bonus Fee** that the Grazier is liable for to be paid from the Grazier's Entitlement in each Subsequent Year. The Performance Bonus Fee in respect of each Subsequent Year shall be calculated by Environinvest in accordance with clause 5.3(c) of the Management Agreement.

Fees payable under clause 3 of the Lease Agreement

- **Lease Fee** of \$5.40 per Stock, varied by indexation, payable in each Subsequent Year out of Grazier's Entitlement.

Fees payable under clause 3 of the Agistment Agreement

- **Agistment Fee** of \$26.40 per Stock, varied by indexation, payable in each Subsequent Year out of Grazier's Entitlement.

85. If the Grazier's Entitlement in that Subsequent year is insufficient to cover the fees due under the respective Project Agreements, the Grazier must pay the fees the Grazier is liable for under the Project Documents, in full by 30 June of the Subsequent Year to which the fees relate.

Finance

86. A Grazier can fund their involvement in the Project themselves or borrow from an independent lender external to the Project.

87. A Grazier who enters into a finance arrangement with an independent lender external to the Project may request a private ruling on the deductibility of interest incurred under the finance arrangement.

88. Graziers cannot rely on any part of this Ruling if the Application Money is not paid in full on or before 31 May 2007 by the Grazier or, on the Grazier's behalf, by a lending institution.

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

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL of the ITAA 1936 or the funding arrangements transform the Project into a 'scheme' to which Part IVA of the ITAA 1936 may apply;
- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;

- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project, are involved or become involved in the provision of finance to Graziers for the Project.

Commissioner of Taxation

30 May 2007

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.*

Corporations Act

90. For this Ruling to apply, an offer for an interest in the Project must be an offer which qualifies as a small scale offering as defined in section 1012E of the Corporations Act.
91. Small scale offers do not require a product disclosure statement.
92. Under section 1012E of the Corporations Act, a Grazier may participate in the Project by accepting a 'personal offer' for an interest in the Project. Offers made under section 1012E cannot be accepted by more than 20 investors in any 12 month period and these investors, in aggregate, must not invest more than \$2 million dollars (subsection 1012E(2)).
93. An offer will be a 'personal offer' where it can only be accepted by the person to whom it is made, and it is made to a person who is likely to be interested in the offer because of previous contact, or professional or other connection with the person making the offer, or because they have indicated that they are interested in offers of that kind (subsection 1012E(5) of the Corporations Act).

Is the Grazier carrying on a business?

94. For the amounts set out in paragraph 31 of this Ruling to constitute allowable deductions the Grazier's sheep breeding activities as a participant in the Primary Yield Lamb Project 2007 must amount to the carrying on of a business of primary production.
95. Two Taxation Rulings are relevant in determining whether a Grazier will be carrying on of a business of primary production.
96. 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?
97. Taxation Ruling TR 2000/8 Income tax: investment schemes, particularly paragraph 89, is more specific to arrangements such as the Primary Yield Lamb Project 2007. 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.
98. Having applied these principles to the arrangement set out above, a Grazier in the Primary Yield Lamb Project 2007 is accepted to be carrying on a business of leasing and grazing sheep and for the production of lamb meat, wool and skin for profit.

The Simplified Tax System

Division 328

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

100. Changes to the STS rules apply from 1 July 2005. The question of whether a Grazier 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 Grazier 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'.

Deduction for Initial Management Fee, ongoing Management Fees, Third Party Expenses, Performance Bonus Fee, Lease Fee and Agistment Fee

Section 8-1

101. The Initial Management Fee, ongoing Management Fees, Third Party Expenses, Performance Bonus Fee, Lease Fee and Agistment Fee are deductible under section 8-1 (see paragraphs 43 and 44 of TR 2000/8). A 'non-income producing' purpose (see paragraphs 47 and 48 of TR 2000/8) is not identifiable in the arrangement and there is no capital component evident in the Initial Management Fee, Management Fees, Third Party Expenses, Performance Bonus Fee, Lease Fee and Agistment Fee (see paragraphs 49 to 51 of TR 2000/8).

102. 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 (see paragraphs 103 to 107 of this Ruling) a deduction for these amounts can 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

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 Stock or licensing 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, 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

105. Under the scheme to which this Product Ruling applies ongoing Management Fees, Third Party Expenses, Performance Bonus Fee, Lease Fee and Agistment Fee are incurred annually. Accordingly, the prepayment provisions in sections 82KZME and 82KZMF of the ITAA 1936 have no application to this scheme.

106. However, sections 82KZME and 82KZMF of the ITAA 1936 may have relevance if a Grazier in this Project prepays all or some of the expenditure payable under the Management, Lease and Agistment Agreements, or prepays interest under a loan agreement. Where such a prepayment is made these prepayment 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.

107. As noted in the Ruling section above, Graziers who prepay 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.

Division 35 – deferral of losses from non-commercial business activities and the Commissioner's discretion

Sections 35-10 and 35-55

108. A Grazier 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.

109. Financial projections by the Responsible Entity indicate that in each year if the Project the assessable income test in section 35-30 will be met. The assessable income test requires that a Grazier derives at least \$20,000 of assessable in an income year from their business of selling lambs, wool and skin for profit. For the purposes of the assessable income test in the income year in which the Grazier commences to carry on their Business the Grazier can use a reasonable estimate of what would have been the amount of their assessable income if they had carried on their Business throughout the whole of that financial year.

110. Where a Grazier satisfies the assessable income test in an income year the Grazier will not be required to defer any loss attributable to their business activity, to a later year. Instead, this loss can be offset against other assessable income of the Grazier for the year in which the loss arises.

111. However, if a Grazier either fails to pass the assessable income test in the income year ended 30 June 2007 or later, or fails to pass one of the other tests in Division 35, they should seek a private ruling on how Division 35 will apply to their business activity for that income year.

Section 82KL – recouped expenditure

112. 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

113. 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).

114. The Primary Yield Lamb Project 2007 will be a 'scheme'. A Grazier will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at 31 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.

115. Graziers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the sale of Progeny, wool and skin. There are no facts that would suggest that Graziers 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.

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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

Subject references:

- carrying on a business
- commencement of business
- fee expenses
- management fees
- non-commercial losses
- producing assessable income
- product rulings
- public rulings
- tax avoidance
- taxation administration
- trading stock

Legislative references:

- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
- ITAA 1936 82KZMD
- ITAA 1936 82KZME
- ITAA 1936 82KZMF
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)

- ITAA 1936 318
- ITAA 1997 6-5
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- ITAA 1997 17-5
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- ITAA 1997 Div 35
- ITAA 1997 35-10
- ITAA 1997 35-30
- ITAA 1997 35-55
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- ITAA 1997 328-285
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