


PR 2007/70 - Income tax: Great Southern 2008 High Value Timber Project

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 This document has changed over time. This is a consolidated version of the ruling which was published on 4 June 2008



Product Ruling

Income tax: Great Southern 2008 High Value Timber Project

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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.

[**Note:** This is a consolidated version of this document. Refer to the Tax Office Legal Database (<http://law.ato.gov.au>) to check its currency and to view the details of all changes.]

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 'Great Southern 2008 High Value Timber 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 Growers. Growers will be those entities that are accepted to participate in the scheme specified below and who have executed the relevant Project Agreements set out in paragraph 27 of this Ruling on or before 30 June 2008. 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 1 July 2007 or after 30 June 2008;
- participate in the scheme through offers made other than through the Product Disclosure Statement (PDS);
- enter into finance arrangements with Great Southern Finance Pty Ltd, or with any associate of Great Southern Finance Pty Ltd that do not comply with the written undertaking given to the Tax Office by Great Southern Managers Australia Limited (GSMAL) dated 5 February 2007 (the word 'associate' has the meaning given in section 318 of the *Income Tax Assessment Act 1936* (ITAA 1936)); or
- enter into finance agreements with Great Southern Finance Pty Ltd, the Preferred Financier or entities associated with this Project other than those specified in paragraphs 63 to 72 of this Ruling (the word 'associate' has the same meaning given in section 318 of the 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 27 to 72 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 1 July 2007, the earliest date a Grower can be accepted for the purposes of this Product Ruling. It therefore applies to the specified class of entities that enter into the scheme from 1 July 2007 until 30 June 2008, 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 2010.

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 Grower) to be entitled to claim input tax credits for the GST included in its expenditure, it must be registered or required to be registered for GST and hold a valid tax invoice.

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 Grower in the defined class of entities who enters into the scheme described at paragraphs 27 to 72 of this Ruling.

19. The Grower'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 Grower's business of primary production will commence at the time of execution of their Land and Management Agreement.

The Simplified Tax System

Division 328

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

21. For these Growers only, 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 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**

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

Deduction for Establishment Services Fees, Loan Establishment Fee, Insurance Premiums and Interest**Section 8-1, section 25-25 and Division 27 of the ITAA 1997 and section 82KZMG of the ITAA 1936**

24. A Grower may claim tax deductions for the following fees and expenses on a per Woodlot basis, as set out in the Table below.

Fee Type	Year ending 30 June 2008	Year ending 30 June 2009	Year ending 30 June 2010
Establishment Services Fee	\$13,750 See Notes (i) & (ii)		
Interest on loans with Great Southern Finance Pty Ltd or the Preferred Financier		As incurred See Note (iii)	As incurred See Note (iii)
Loan Establishment Fee (for finance entered into with Great Southern Finance Pty Ltd or the Preferred Financier)	Must be calculated See Note (iv)	Must be calculated See Note (iv)	Must be calculated See Note (iv)
Insurance Premiums	Nil	Nil	As incurred See Note (v)

Notes:

- (i) If the Grower is registered or required to be registered for GST, amounts of outgoing would need to be adjusted as relevant for GST (for example, input tax credits): Division 27.
- (ii) Under section 82KZMG of the ITAA 1936 the Establishment Services Fee is expenditure for 'seasonally dependent agronomic activities' (see paragraphs 84 to 91 of this Ruling) and is deductible in the income year in which it is incurred.

- (iii) The deductibility or otherwise of interest arising from agreements entered into with financiers other than Great Southern Finance Pty Ltd or the Preferred Financier, is outside the scope of this Ruling. Prepayments of interest to any lender, including Great Southern Finance Pty Ltd and the Preferred Financier, are also not covered by this Product Ruling. Growers who enter into agreements with other financiers and/or prepay interest may request a private ruling on the deductibility of the interest incurred.
- (iv) The Loan Establishment Fee payable to either Great Southern Finance Pty Ltd or to the Preferred Financier is a borrowing expense and is deductible under section 25-25. It is incurred for borrowing money that is used or is to be used during that income year solely for income producing purposes. The deduction is spread over the period of the loan or 5 years, whichever is the shorter. The deductibility or otherwise of borrowing costs arising from loan agreements entered into with financiers other than Great Southern Finance Pty Ltd or the Preferred Financier is outside the scope of this Ruling.
- (v) Insurance Premiums will be payable annually commencing from the year ended 30 June 2010. These amounts are deductible in the income year in which they are incurred under section 8-1.

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

Section 35-55 – exercise of Commissioner's discretion

25. A Grower who is an individual accepted into the Project in the year ended 30 June 2008 may have losses arising from their participation in the Project that would be deferred to a later income year under section 35-10. Subject to the Project being carried out in the manner described above, the Commissioner will exercise the discretion in paragraph 35-55(1)(b) for Growers for the income years ended **30 June 2008 to 30 June 2027**. This conditional exercise of the discretion will allow those losses to be offset against the Grower's other assessable income in the income year in which the losses arise.

Prepayment provisions and anti-avoidance provisions

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

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

- expenditure by a Grower does not fall within the scope of sections 82KZME and 82KZMF;
- section 82KL does not apply to deny the deductions otherwise allowable; and
- the relevant provisions in Part IVA will not be applied to cancel a tax benefit obtained under a tax law dealt with in this Ruling.

Scheme

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

- Application for a Product Ruling as constituted by documents provided on 12 September 2006 and additional correspondence including emails received 11 October 2006, 30 November 2006, 28 December 2006, 9 January 2007, 22 January 2007, 30 January 2007, 31 January 2007, 1 February 2007, 5 February 2007, 6 February 2007 and 21 May 2007;
- **Product Disclosure Statement** for the Great Southern 2008 High Value Timber Project received on 21 May 2007 dated 16 February 2007;
- **Constitution** establishing the Great Southern 2008 High Value Timber Project received on 21 May 2007;
- Compliance Plan for the Great Southern 2008 High Value Timber Project dated 13 February 2007 and received 21 May 2007;
- **Lease or Forest Right Agreement (Land Interest Agreement)** between each Grower and Great Southern Managers Australia Limited received on 21 May 2007 (Forest Right Agreement) and 21 May 2007 (Lease);
- Draft Management Services Agreement and Draft Plantation Management Agreement between Great Southern Managers Australia Limited and Great Southern Plantations Ltd received 12 September 2006;
- Draft Leases between Great Southern Managers Australia Limited and Great Southern HVT Holdings Pty Ltd received 2 February 2007;

- **Land and Management Agreement** to be entered into by each Grower and Great Southern Managers Australia Limited (the Manager), received 21 May 2007;
- Draft **Loan Deed** to be entered into by each Grower and Great Southern Finance Pty Ltd or the Preferred Financier, received 2 February 2007;
- further correspondence received 13 February 2008, 4 March 2008, 29 April 2008, 20 May 2008, and 21 May 2008; and
- Draft Application for Term Finance and the Term of Loan Deed received 20 May 2008.

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

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

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

30. The main features of the Great Southern 2008 High Value Timber Project are as follows:

Location	Northern Territory, Queensland, or in any other regions of Australia deemed suitable for the commercial production of African Mahogany and Teak
Type of business to be carried on by each Grower	Commercial growing of African Mahogany and Teak for the production of high value furniture and appearance grade timber
Term of the Project	Approximately 20 years
Number of hectares offered for cultivation	This PDS provides for 1,000 hectares to be planted, however, oversubscriptions may be accepted
Size of each Woodlot	0.5 hectares (0.25 hectare African Mahogany and 0.25 hectare Teak)
Minimum allocation per Grower	1 Woodlot
Minimum subscription	There is no minimum subscription for this Project
Initial cost	\$13,750

Ongoing costs	Growers are required to pay 13.75% of net harvest proceeds as management fees and 2.75% of net harvest proceeds as Land Interest Fees
Other costs	Growers will be charged for the cost of all insurance except Public Liability Insurance

31. The Project will be a registered managed investment scheme under the *Corporations Act 2001*. GSMAL has been issued with an Australian Financial Service Licence 240787 and will be the Responsible Entity for the Project.

32. The Project will involve commercially growing African Mahogany and Teak plantations in various regions within Australia. The timber from the plantations is suitable for furniture and appearance grade timber.

33. An offer to participate in the Project will be made through a PDS. The offer under the PDS is for 1,000 hectares, which corresponds to 2,000 Woodlots in the Project.

34. For the purposes of this Ruling, Applicants who are accepted to participate in the Project and who execute the Land and Management Agreement on or before 30 June 2008 will become 'Growers'.

35. An entity that participates in the Project will do so by acquiring an interest in the Project on or before 30 June 2008, which will consist of a minimum of one Woodlot (0.5 hectares). A Woodlot consists of 0.25 hectares of African Mahogany trees and 0.25 hectares of Teak trees.

36. Applicants execute a Power of Attorney contained in the PDS. The Power of Attorney irrevocably appoints GSMAL to enter into, on behalf of the Grower, a Land and Management Agreement and a Land Interest Agreement and any other documents required to hold an interest in the Project.

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

38. GSHVT will acquire or lease land for the Project within Australia. Land utilised by the Project must meet the requirements set out by the Independent Forester as set out in section 5 of the PDS.

39. This Land will be subject to a capability survey to determine soil suitability, rainfall, fertiliser history and groundwater issues. Once deemed suitable an African Mahogany and Teak plantation will be developed by the Responsible Entity who will manage and maintain the plantation until the trees are harvested. The land will be divided into 0.5 hectare Woodlots and leased to the Growers accepted in the Project.

40. Each Grower will use their Woodlot(s) for the purpose of carrying on a business of cultivating and harvesting African Mahogany and Teak and the sale of harvested produce.

Constitution

41. The Constitution establishes the Project and operates as a deed binding all Growers and GSMAL. The Constitution sets out the terms and conditions under which GSMAL agrees to act as Responsible Entity and thereby manage the Project. Upon acceptance into the Project, Growers are bound by the Constitution by virtue of their participation in the Project.

42. In order to acquire an interest in the Project, the Grower must make an application for Woodlots in accordance with clause 4 of the Constitution. 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 payment of the Application Money in a form acceptable to the Responsible Entity.

43. Under clause 5 of the Constitution, GSMAL holds the Application Money on bare trust. GSMAL will deposit all Application Moneys received from applicants in a Project Account (clause 5.1).

44. Once GSMAL has accepted the application and all of the Land and Management Agreements have been executed and remain in force (clause 6.5) the Application Money may be transferred and applied against the fees due to Great Southern Managers Australia Limited (clause 8).

45. The Constitution also sets out provisions relating to GSMAL keeping a register of Growers (clause 29).

Compliance Plan

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

Land Interest Agreement (Lease, Forest Right Agreement, Forest Right Lease Agreement, Licence Agreement or other similar agreement)

47. Each Grower will enter into a Lease, Forest Right Agreement, Forest Right Lease Agreement, Licence Agreement or other similar agreement with the Responsible Entity as the Landholder. The Responsible Entity will grant to the Grower the right to exclusively possess, occupy, use and enjoy their Woodlots, for the conduct of the Grower's business and to harvest and sell the African Mahogany and Teak for a commercial profit.

48. Under the Land Interest Agreement Growers acquire an interest in land called a Woodlot. Each Woodlot will comprise of two separate areas of land being one Grower's Land Area of 0.25 hectares of African Mahogany and one Grower's Land Area of 0.25 hectares of Teak which will together total 0.5 hectare. Growers will have the right to use their Woodlot from the date of execution of the Land Interest Agreement to the termination date for the purpose of conducting their afforestation business.

49. Where a Grower's Woodlot or part of the Woodlot is located in the Northern Territory, the lease is for two terms being 12 years and 8 years each. The second term is dependant on receiving a Northern Territory planning approval.

50. The Land Interest Agreement incorporates the provisions of the Lease/Forest Right Agreement terms. Some of the terms are that the Grower will:

- not use the Woodlot for any purpose other than commercial silviculture and not residential, recreational or tourist purposes (clause 5.1);
- manage, cultivate and work the Woodlot in a proper and skilful manner (clause 5.2); and
- comply with all statutes, ordinances, proclamations, orders and regulations present or future affecting or relating to the Woodlot (clause 5.10).

Land and Management Agreement

51. Under the Land and Management Agreement the Grower appoints the Responsible Entity (as Manager) to manage the Woodlots and to carry out the management services subject to the terms and conditions of the Agreement. The Agreement will commence on the date of its execution and shall continue until it's termination as defined in clause 1.

52. The Responsible Entity will commence the provision of the Establishment Services on or after the Commencement Date and will use all reasonable endeavours to complete the Establishment Services within 12 months from this date (clause 5).

53. The Establishment Services include, amongst other things:

- ripping and mounding the Woodlot as necessary from the Commencement Date;
- otherwise preparing the Woodlot for planting as necessary from the Commencement Date;
- supply sufficient Teak and African Mahogany plants to the specifications recommended in the Management Plan as is reasonably required to complete the Planting Services;
- fertilising the Woodlot as necessary from the Commencement Date;
- spraying the Woodlot as necessary from the Commencement Date; and
- the Planting Services.

54. The Responsible Entity will commence the provision of the Ongoing Services after the completion of the Establishment Services and shall continue to provide the Ongoing Services until the termination of this Agreement.

55. The Ongoing Services being those to manage and maintain an African Mahogany and Teak Plantation include:

- cultivating, tending, culling, fertilising, replanting, spraying and otherwise caring for the trees as and when required;
- organising and arranging for the pruning of the trees as and when required;
- keeping in good repair and condition an access road or roads within the plantation, as required;
- undertaking pest control measures as required on the Woodlot to control rabbits and other vermin;
- keeping in good repair and condition adequate firebreaks within the Plantation;
- organising and arranging non-commercial thinning;
- organising and arranging commercial thinning and account for the Net Proceeds;
- organising and arranging for the trees to be clear felled when they have reached maturity and account for the Net Proceeds;
- selling the Timber Produce; and
- obtaining all necessary approvals and consents required in relation to the provision of the services listed.

56. The Responsible Entity will also obtain an independent report by 31 October 2009 and provide it to the Grower within 30 days and then within 30 days after 31 October in each year thereafter for the duration of the Project.

57. The Responsible Entity may, for the better performance of its obligations, employ agents, contractors, professional advisers and other consultants notwithstanding such persons are as those defined at clause 6.1 and the Land and Management Agreement.

Pooling of Timber and Grower's Entitlement to Net Proceeds

58. The Land and Management Agreement sets out provisions relating to the Grower's Entitlement to Harvest Proceeds. This Product Ruling only applies where the following principles apply to the pooling and distribution arrangements as outlined in clause 11 of the Land and Management Agreement:

- only Growers who have contributed African Mahogany and/or Teak are entitled to benefit from distributions of Harvest Proceeds from the pool; and
- any pooled African Mahogany and Teak must consist only of African Mahogany and Teak contributed by Growers of the same Project Class.

Fees

59. Under the terms of the Land and Management Agreement, a Grower will make payments as described below on a per Woodlot basis.

Fees payable under the Land and Management Agreement

60. The Application Money is to be paid by each Grower on application for the provision of the Establishment Services in the Initial Period. The Application Moneys (Establishment Services Fee) comprises of \$13,750 (GST inclusive).

61. Following the Initial Period, Ongoing Management Fees are payable to the Responsible Entity for providing the Ongoing Services as outlined in paragraph 55 of this Ruling. These are payable from the Net Harvest Proceeds (at harvest or commercial thinning depending on circumstances) being 13.75% for management and maintenance expenses.

Fees payable under the Land Interest Agreement

62. For the Term of the Project Land Interest Fees are payable being an amount of 2.75% of the Net Harvest Proceeds.

Finance

63. A Grower who does not pay the Establishment Services Fee in full upon application can borrow from Great Southern Finance Pty Ltd, borrow from the Preferred Financier, or borrow from an independent lender external to the Project.

64. Only the finance arrangements set out below are covered by this Product Ruling. A Grower cannot rely on this Product Ruling if they enter into a finance arrangement with Great Southern Finance Pty Ltd or with the Preferred Financier that materially differs from that set out in the documentation provided to the Tax Office with the application for this Product Ruling. A Grower who enters into a finance arrangement with an independent lender external to the Project other than the Preferred Financier may request a private ruling on the deductibility or otherwise of interest incurred under finance arrangements not covered by this Product Ruling.

65. Growers cannot rely on any part of this Ruling if the Establishment Services Fee (exclusive of GST) is **not paid in full** on or before 30 June 2008 by the Grower or, on the Grower's behalf, by a lending institution. Where an application is accepted subject to finance approval by any lending institution other than Great Southern Finance Pty Ltd, Growers 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 2008.

Finance offered by Great Southern Finance Pty Ltd

66. A Grower can finance the cost of their Establishment Services Fee by borrowing that amount from Great Southern Finance Pty Ltd (as the Lender).

67. Subject to Great Southern Finance Pty Ltd accepting the Grower's application, the Grower will be bound by the terms and conditions of the Application included with the Product Disclosure Statement, Application for Term Finance, and Term of Loan Deed.

68. Finance offered by the Great Southern Finance Pty Ltd provides two options the first being a 12 months interest free loan. It requires that:

- equal monthly principal instalments are paid over a period of 12 months;
- instalments are paid by direct debit commencing from 15 July 2008;
- Grower's can borrow a maximum of \$12,500 per Woodlot under 12 months interest free finance. The \$1,250 balance of the Establishment Services Fee is invoiced on execution of the Land and Management Agreement; and
- no interest is applicable.

69. The second option under finance offered by Great Southern Finance Pty Ltd provides principal and interest finance loans with a repayment term of two years up to a term of no more than 15 years and requires that:

- equal monthly principal and interest repayments over the term of the loan commence no later than 31 July 2008;
- interest rates will be fixed for the period of the loan and are set on an arms length basis with reference to a commercial margin over the inter bank SWAP rate for that term;
- Grower's can borrow a maximum of \$13,750 per Woodlot under long term finance. If less than \$13,750 is borrowed, the balance of the Establishment Services Fee is invoiced on execution of the Land and Management Agreement; and
- under the Loan Deed, a Loan Establishment Fee, comprising an application fee of up to 1.1% of the loan advance and a fee to cover legal costs and expenses of up to \$275 (GST inclusive) may be charged. Great Southern Finance Pty Ltd, however, may charge a lesser fee, and at time of issue of this addendum the total Loan Establishment Fee is generally calculated as 0.5% of the loan amount; and
- the security for the loan is taken over the Grower's interest under the Land and Management Agreement and subsequent Land Interest issued.

Finance offered by the Preferred Financer

70. The finance offered by the Preferred Financer provides two options the first being a 12 months interest free loan. It requires that:

- equal monthly principal instalments are paid over a period of 12 months;
- instalments are paid by direct debit commencing from 15 July 2008;
- Grower's can borrow a maximum of \$12,500 per Woodlot under 12 months interest free finance. The \$1,250 balance of the Establishment Services Fee is invoiced on execution of the Land and Management Agreement; and
- no interest is applicable.

71. The second option offered by the Preferred Financier requires that:

- principal and interest loans from 2 years up to no more than 16 years are entered into; or
- loans with interest only payments for up to 3 years followed by principal and interest repayments for the remainder of the term; provided that the loan term cannot be less than 5 years or greater than 16 years are entered into;
- where an interest only period is applicable, equal monthly interest payments followed by equal monthly principal and interest repayments for the term of the loan commencing 31 July 2008;
- interest rates will be fixed for the period of the loan and are set on an arms length basis with reference to a commercial margin over the inter bank SWAP rate for that term;
- Grower's can borrow a maximum of \$13,750 per Woodlot under long term finance. If less than \$13,750 is borrowed, the balance of the Establishment Services Fee is invoiced on execution of the Land and Management Agreement;
- under the Loan Deed, a Loan Establishment Fee, comprising an application fee of up to 1.1% of the loan advance and a fee to cover legal costs and expenses of up to \$275 (GST inclusive) may be charged. The Preferred Financier, however, may charge a lesser fee, and at time of issue of this addendum the total Loan Establishment Fee is generally calculated as 0.5% of the loan amount; and
- the security for the loan is taken over the Grower's interest under the Land and Management Agreement and subsequent Land interest issued.

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

- there are split loan features of a type referred to in Taxation Ruling TR 98/22;
- there are indemnity arrangements or other collateral agreements in relation to the loan designed to limit the borrower's risk;
- 'additional benefits' are or will be granted to the borrowers for the purpose of section 82KL of the ITAA 1936 or the funding arrangements transform the Project into a 'scheme' to which Part IVA of the ITAA 1936 may apply;

- the loan or rate of interest is non-arm's length;
- repayments of the principal and payments of interest are linked to the derivation of income from the Project;
- the funds borrowed, or any part of them, will not be available for the conduct of the Project but will be transferred (by any mechanism, directly or indirectly) back to the lender or any associate of the lender;
- lenders do not have the capacity under the loan agreement, or a genuine intention, to take legal action against defaulting borrowers; or
- entities associated with the Project, other than Great Southern Finance Pty Ltd or the Preferred Financier, are involved or become involved in the provision of finance to Growers for the Project.

Appendix 1 – Explanation

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

Is the Grower carrying on a business?

73. For the amounts set out in paragraph 24 of this Ruling to constitute allowable deductions the Grower's afforestation activities as a participant in the Great Southern 2008 High Value Timber Project must amount to the carrying on of a business of primary production.

74. Two Taxation Rulings are relevant in determining whether a Grower will be carrying on of a business of primary production.

75. 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?

76. Taxation Ruling TR 2000/8 Income tax: investment schemes, particularly paragraph 89, is more specific to arrangements such as the 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.

77. Having applied these principles to the arrangement set out above, a Grower in the Project is accepted to be carrying on a business of growing and harvesting African Mahogany and Teak for sale.

The Simplified Tax System

Division 328

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

79. Changes to the STS rules apply from 1 July 2005. The question of whether a Grower is eligible to be an 'STS taxpayer' is outside the scope of this Product Ruling (but refer to Taxation Ruling TR 2002/6 and Taxation Ruling TR 2002/11). Therefore, any Grower who relies on those parts of this Ruling that refer to the STS will be assumed to have correctly determined whether or not they are eligible to be an 'STS taxpayer'.

Deductibility of the Establishment Services Fee, Insurance Premiums and interest on loans with Great Southern Finance Pty Ltd or the Preferred Financier

Section 8-1

80. The Establishment Services Fee, Interest and Insurance Premiums 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 Establishment Services Fees or Land Interest Fees (see paragraphs 49 to 51 of TR 2000/8).

81. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply. Subject to the prepayment provisions (see paragraphs 84 to 85 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.)

82. Some Growers may finance their participation in the Project through a Loan Agreement with Great Southern Finance Pty Ltd or the Preferred Financier. Applying the same principles as that used for the Establishment Services Fee and the Land Interest Fee, interest incurred under such a loan has sufficient connection with the gaining of assessable income to be deductible under section 8-1.

83. Other than where the prepayment provisions apply (see paragraphs 86 to 91 of this Ruling), a Grower can claim a deduction for such interest in the year in which it is incurred.

Prepayment provisions

Sections 82KZL to 82KZMG

84. 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 income year, then it is not expenditure to which the prepayment rules apply.

85. For this Project, the only prepayment provisions that are relevant are section 82KZL of the ITAA 1936 (an interpretive provision) and section 82KZMG of the ITAA 1936 (an operative provision). References to sections 82KZME and 82KZMF of the ITAA 1936 are made only in respect their interaction with section 82KZMG and to confirm that these provisions have no application to expenditure incurred by Growers who participate in the scheme set out in this Ruling.

Application of the prepayment provisions to this Project***Sections 82KZME and 82KZMF***

86. The Ongoing Management Fees payable under the scheme to which this Product Ruling applies are payable out of harvest proceeds and the interest payable to Great Southern Finance Pty Ltd or to the Preferred Financier is incurred monthly in arrears. Accordingly, the prepayment provisions in sections 82KZME and 82KZMF of the ITAA 1936 have no application to expenditure incurred by Growers under this scheme.

87. However, sections 82KZME and 82KZMF of the ITAA 1936 may have relevance if a Grower in this Project prepays interest under a loan agreement (including loan agreements with lenders other than Great Southern Finance Pty Ltd or the Preferred Financier. Where such a prepayment is made these prepayment provisions will also apply to 'STS taxpayers' because there is no specific exclusion in section 82KZME that excludes them from the operation of section 82KZMF.

88. As noted in the Ruling part above, Growers 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.

Section 82KZMG

89. Expenditure that meets the requirements of section 82KZMG of the ITAA 1936 is excluded from the application of the prepayment rules in sections 82KZME and 82KZMF of the ITAA 1936 that would otherwise apply. Section 82KZMG provides a '12 month rule' that, in effect, facilitates an immediate deduction for certain prepaid expenditure incurred under a plantation forestry managed agreement. The 12 month rule applies to expenditure for 'seasonally dependent agronomic activities' that will be carried out during the establishment period of a particular planting of trees. Seasonally dependent agronomic activities are explained in Taxation Determination TD 2003/12. Whilst the establishment period itself may exceed 12 months, each seasonally dependent agronomic activity must be completed within 12 months of commencement of its eligible service period (as defined in subsection 82KZL(1) of the ITAA 1936), and by the end of the following income year.

90. Under the Land and Management Agreement each Grower incurs an Establishment Services Fee of \$13,750 per Woodlot for 'seasonally dependent agronomic activities' that will be carried out during the 'establishment period' of the Trees.

91. The expenditure for 'seasonally dependent agronomic activities' meets all other requirements of section 82KZMG of the ITAA 1936 and, therefore, a deduction is allowable in the income year ended 30 June 2008 for the full amount of expenditure incurred by the Grower for the Establishment Services Fee.

Sections 35-10 and 35-55 – deferral of losses from non-commercial business activities and the Commissioner’s discretion

92. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for **30 June 2008 to 30 June 2027** based on the evidence supplied, the Commissioner has determined that for those income years:

- it is because of its nature the business activity of a Grower 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 afforestation industry, a Grower’s business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

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

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

Section 82KL – recouped expenditure

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

Part IVA – general tax avoidance provisions

96. 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).

97. The Great Southern 2008 High Value Timber Project will be a 'scheme'. A Grower will obtain a 'tax benefit' from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraph 24 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.

98. Growers to whom this Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the African Mahogany and Teak. There are no facts that would suggest that Growers have the opportunity of obtaining a tax advantage other than the tax advantages identified in this Ruling. There 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:

TD 2003/12; TR 97/7; TR 97/11;
TR 98/22; TR 2000/8;
TR 2002/6; TR 2002/11

Subject references:

- carrying on a business
- commencement of business
- fee expenses
- non-commercial losses
- primary production
- primary production expenses
- producing assessable income
- product rulings
- public rulings
- seasonally dependent
agronomic activity
- tax avoidance
- tax benefits under tax avoidance
schemes
- tax shelters
- tax shelters project
- taxation administration

Legislative references:

- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
- ITAA 1936 82KZM
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
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- ITAA 1936 82KZME
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- ITAA 1936 318
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- ITAA 1997 25-25
- ITAA 1997 Div 27
- ITAA 1997 Div 35
- ITAA 1997 35-10
- ITAA 1997 35-10(2)
- ITAA 1997 35-55
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