PR 2009/36 - Income tax: 2009 Grain Co-Production Project

Product Ruling

Income tax: 2009 Grain Co-Production Project

Contents Para

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, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is 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 Commissioner **does not** sanction or guarantee this product. Further, the Commissioner gives 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. The Commissioner recommends 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. In this Product Ruling this scheme is referred to as the 2009 Grain Co-Production Project or simply as 'the Project'.

2. All legislative references in this Product Ruling are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated. Where used in this Product Ruling, the word 'associate' has the meaning given in section 318 of the *Income Tax Assessment Act 1936* (ITAA 1936). In this Product Ruling, terms defined in the Project agreements have been capitalised.

Class of entities

3. This part of the Product Ruling specifies which entities:

- are subject to the taxation obligations; and
- can rely on the taxation benefits,

set out in the Ruling section of this Product Ruling.

4. 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 on or after the date this Product Ruling is made and who have executed the relevant Project Agreements set out in paragraph 26 of this Ruling on or before 31 May 2009. They will stay in the scheme until its completion and derive assessable income from this involvement.

5. 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:

- terminate their involvement in the scheme prior to its completion; or do not derive assessable income from it;
- are accepted into this Project before the date of this Ruling or after 31 May 2009;
- participate in the scheme through offers made other than through the Product Disclosure Statement, or who enter into an undisclosed arrangement with the promoter or an associate of the promoter, or an independent advisor that is interdependent with scheme obligations and/or scheme benefits (which may include tax benefits or harvest returns) in any way;
- contract for a Co-Production Unit (CPU) where the due diligence requirements listed at paragraph 40 of this Ruling have not been met;

- finance their participation in the Project through loans with Macro Funds Ltd or any of its associates; or
- are Macro Funds Ltd or any of its associates.

Superannuation Industry (Supervision) Act 1993

6. 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

7. 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 26 to 101 of this Ruling.

8. 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.

Date of effect

10. This Product Ruling applies prospectively from 20 May 2009, the date it is published. It therefore applies only to the specified class of entities that enter into the scheme from 20 May 2009 until 31 May 2009, 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 2011. This Product Ruling will continue to apply to those entities even after its period of application has ended for the scheme entered into during the period of application.

11. However this Product Ruling only applies to the extent that there is no change in the scheme or in the entity's involvement in the scheme.

Changes in the law

12. Although this Product Ruling deals with the income tax laws enacted at the time it was issued, later amendments may impact on this Product Ruling. Any such changes will take precedence over the application of this Product Ruling and, to that extent, this Product Ruling will have no effect.

13. 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

14. 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

15. 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 any creditable acquisition it makes, it must be registered or required to be registered for GST and hold a valid tax invoice.

Ruling

Application of this Ruling

16. 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 26 to 101 of this Ruling.

17. 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 Sub-Lease Agreement and Management Agreement.

18. A Grower is not eligible to claim any tax deductions until the Grower's application to enter the Project is accepted and the Project has commenced.

Small business concessions

19. From the 2007-08 income year, a range of concessions previously available under the Simplified Tax System (STS), will be available to an entity if it carries on a business and satisfies the $2 million aggregated turnover test (a 'small business entity').

20. A small business entity can choose the concessions that best suit its needs. Eligibility for some small business concessions is also dependent on satisfying some additional conditions. Because of these choices and the eligibility conditions the application of the small business concessions to Growers who qualify as a 'small business entity' is not able to be dealt with in this Product Ruling.

Assessable income

Section 6-5

21. 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.

Deductions for Initial Period Fee, Subsequent Period Fee, Rent, and other Project Pool Outgoings

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

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

Fee Type	Year ending 30 June 2009	Year ending 30 June 2010	Year ending 30 June 2011
Initial Period Fee	$4,345 See Notes (i) and (ii)	$3,850 See Notes (i), (ii) and (iv)	$3,850 See Notes (i), (ii) and (iv)
Subsequent Period Fee		$423.50 See Notes (i), (ii) and (iv)	$423.50 See Notes (i), (ii) and (iv)
Rent	$55 See Notes (i) and (ii)	$247.50 See Notes (i), (ii) and (iv)	$247.50 See Notes (i), (ii) and (iv)
Harvest Period Costs		As incurred See Notes (i) and (ii)	As incurred See Notes (i) and (ii)
Manager Performance Bonus		As incurred See Notes (i) and (ii)	As incurred See Notes (i) and (ii)
Farmer Bonus		As incurred See Notes (i) and (ii)	As incurred See Notes (i) and (ii)
Farmer Bonus Adjustment		As incurred See Notes (i) and (ii)	As incurred See Notes (i) and (ii)
Managed Grain Pools & Harvest Loan Interest Costs		As incurred See Notes (i), (ii) and (iii)	As incurred See Notes (i), (ii) and (iii)
Warehouse Costs		As incurred See Notes (i) and (ii)	As incurred See Notes (i) and (ii)
Crop Insurance		As incurred See Notes (i) and (ii)	As incurred See Notes (i) and (ii)

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) The Initial Period Fee, Subsequent Period Fee, Rent Harvest Period Costs, Manager Performance Bonus, Farmer Bonus, Farmer Bonus Adjustment, Managed Grain Pools and Harvest Loan Interest Costs, Warehouse Costs, and Crop Insurance are deductible under section 8-1 in the income year in which they are incurred.

(iii) The Responsible Entity will inform the Grower each Season of the amount of any Managed Grain Pools and Harvest Loan Interest Costs and in which financial year the amount is paid and therefore incurred.

(iv) This Ruling does not apply to Growers who choose to prepay fees or who choose, or who are required to prepay interest under a loan agreement (see paragraphs 108 to 112 of this Ruling). 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 Grower who prepays such amounts may request a private ruling on the taxation consequences of their participation in the Project.

(v) The deductibility or otherwise of interest arising from agreements entered into with any financier(s) is outside the scope of this Ruling. Prepayments of interest to any lender are not covered by this Product Ruling. Growers who enter into agreements with financiers and/or prepay interest may request a private ruling on the deductibility of the interest incurred.

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

Section 35-55 – exercise of Commissioner's discretion

23. Growers who will stay in the Project until its completion will be considered to be carrying on a business of primary production. Such Growers who are individuals and accepted into the Project in the year ended 30 June 2009 may make losses from the Project that may be affected by the loss deferral rule in section 35-10.

24. The discretion in paragraph 35-55(1)(b) will be exercised for such Growers to whom the loss deferral rule would otherwise apply, for the income years ended 30 June 2009. Exercise of the discretion in this case however is also conditional on the Project being carried out in the manner described in paragraphs 26 to 101 of this Ruling, but will allow Growers referred to who make losses, to offset them against their other assessable income in the income years in which those losses arise.

Prepayment provisions and anti-avoidance provisions

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

25. For a Grower who commences participation in the Project and incurs expenditure as required by the Sub-Lease and Management Agreements, 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 (but see paragraphs 108 to 112 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

26. 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 and correspondence received on 20 February 2009, 9, 17, 30 March 2009, 7, 20, 24, 26, 28, 29, 30 April 2009, 4, 6, 7, 8, 11 and 13 May 2009;
- Draft Product Disclosure Statement for the 2009 Grain Co-Production Project received 11 May 2009;
- Lease Agreement between Australian Agricultural Contracts Ltd (AACL) and Macro Funds Ltd, received 20 February 2009;
- **Management Agreement** between Macro Funds Ltd (as Responsible Entity) and the Grower, received 28 April 2009;
- **Sub-Lease Agreement** between Macro Funds Ltd (as Responsible Entity) and the Grower, received 13 May 2009;
- **Constitution** for the 2009 Grain Co-Production Project, received 11 May 2009;
- Compliance Plan for the 2009 Grain Co-Production Project, received 20 February 2009;
- Custodian Agreement between Macro Funds Ltd and Stephen Josland, received 11 May 2009;
- Farmer Management Agreement between AACL and the Farmer, received 20 February 2009;

- Farm Lease Agreement between the Farm Lessor and AACL, received 20 February 2009; and
- Service Agreement between Macro Funds Ltd and AACL, received 20 February 2009.

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

27. 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.

28. 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

29. The main features of the 2009 Grain Co-Production Project are as follows:

Location	The Australian grain-belt
Type of business to be carried on by each participant	Wheat, barley and canola farming
Number of hectares offered for cultivation	Approximately 100,000 hectares
Size of each CPU	Between approximately 10 and 40 hectares (depending on productivity)
Minimum interest	6 Co-Production Units
Term of the Project	Approximately 52 months
Initial cost per CPU (2009 Season)	$4,400
Initial cost per interest (6 CPU – 2009 Season)	$26,400
Ongoing costs	Initial Period Fees, Rent, Subsequent Period Fee, Harvest Period Costs, Warehouse Costs, Harvest Loan Costs, Manager Performance Bonus, Farmer Bonus, Farmer Bonus Adjustment, Crop insurance.

30. The Project is registered as a managed investment scheme under the *Corporations Act 2001*. Macro Funds Ltd (Macro) has been issued with Australian Financial Service Licence No 254421 and will be the Responsible Entity for the Project.

31. The Project will involve the planting, growing and harvesting of wheat, barley and canola for sale. A wheat, barley or canola crop will be planted in the 2009, 2010 and 2011 Seasons.

32. An offer to participate in the Project will be made through the Product Disclosure Statement (PDS). The offer under the PDS is for approximately 100,000 hectares of land to be planted with wheat, barley and canola.

33. A Grower who participates in the Project will do so by acquiring an interest in the Project which will consist of a minimum of six Co-Production Units. Thereafter, a Grower may apply for interests in increments of six Co-Production Units (CPUs).

34. Applicants execute a Power of Attorney contained in the PDS. The Power of Attorney grants Macro Funds Ltd as the Responsible Entity the power to enter into, on behalf of the Grower, a Sub-Lease Agreement and a Management Agreement and any other documents required to hold an interest in the Project.

35. For the purposes of this Ruling, Applicants who are accepted to participate in the Project and who execute the Sub-Lease Agreement and the Management Agreement on or before 31 May 2009 will become Growers.

36. The land on which the Project will be conducted is situated on various grain properties throughout the Australian Grain-belt. Australian Agricultural Contracts Ltd (AACL) will enter into Farm Lease Agreements with various Farm Lessors for the provision of land for the Project.

37. This Land will be leased by AACL to the Responsible Entity under the Lease Agreement. The Responsible Entity will then sub-lease the land to Growers in the form of allocated CPUs.

38. The area of a CPU will range from approximately 10 to 40 hectares based on productivity of between one and four tonnes of grain per hectare. The actual size of a CPU will depend on the expected productivity of the land.

39. Each Grower will use their CPUs for the purpose of carrying on a business of cultivating and harvesting wheat, barley and canola and the sale of harvested produce.

Due diligence

40. In addition to satisfying the conditions set out in sections 11 and 12 of the PDS and clause 9 of the Farmer Management Agreement, land will not be included in the Project unless it meets the following requirements:

- all land selected must be established wheat or barley land and is recognised to be situated in the Australian Grain-belt as defined by ABARE;
- each farmer entering the Project must have completed a Farmer Expression of Interest form;
- each Farmer entering the Project must have a suitable credit rating and credit history;
- each Farmer entering the Project must have appropriate farm management qualifications or experience;
- each farm to be included in the Project must have an average production history of one tonne per hectare or greater over the last 10 years;
- a qualified agricultural consultant must have inspected the land prior to contracting and certified that the land is suitable;
- the qualified agricultural consultant must have inspected the land and confirm that each paddock to be included in the Project has a yield range of one ton per hectare or greater.
- historical production history must be confirmed by at least one independent source;
- each farm to be included in the Project must have the requisite capital equipment required to efficiently undertake grain production; and
- a qualified agricultural consultant must inspect the land post seeding to confirm that contractual obligations are being met.

Constitution

41. The Constitution establishes the Project and operates as a deed binding on all of the Growers and Macro. The Constitution sets out the terms and conditions under which Macro agrees to act as Responsible Entity and thereby manage 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 CPUs in accordance with clause 10. Among other things, the Application must be completed in a form approved by the Responsible Entity, signed by or on behalf of the Applicant, lodged at the registered office of the Responsible Entity and accompanied by payment of the application money in a form acceptable by the Responsible Entity.

43. Under clause 11 of the Constitution, the Responsible Entity holds the Application Funds as bare trustee. The Responsible Entity will deposit all Application money in the Project Fund (clause 3.5).

44. Once the Responsible Entity has accepted the Application and all of the project documents have been executed and remain in force (clause 13) the application money will be transferred and applied against the fees due to the Responsible Entity (clause 11.6).

45. In summary, the Constitution also sets out provisions relating to:

- how the Responsible Entity is to hold Scheme Property for the Growers (clause 4);
- complaint handling (clause 5);
- the obligations and powers of the Responsible Entity (clause 9);
- sale proceeds and their distribution to Growers (clause 12);
- general powers and duties of the Responsible Entity (clause 15);
- Register of Growers (clause 16); and
- winding up of the Scheme (clause 24).

Compliance Plan

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

Lease Agreement

47. Subject to the execution of a Service Agreement, Macro will enter into a Lease Agreement with AACL each Season to lease CPUs for the Project. The Property for each Subsequent Years Lease Agreement may change at the discretion of the Project Manager.

48. The Responsible Entity must use the CPUs for the purpose of growing wheat, barley and canola for sale.

49. The Term of the Lease Agreement is from the Commencement Date (on or before 31 May for the relevant Season) to the day after the grain has been harvested but in any event not exceeding the term of the Farm Lease Agreement.

Sub-lease Agreement

50. Each year the Grower will execute a Sub-Lease Agreement with the Responsible Entity as the lessor. The Sub-Lease sets out the rights and obligations of the parties to the Agreement.

51. The Responsible Entity will grant to the Grower the opportunity to sub-lease CPUs in accordance with the terms and conditions contained in this Agreement. The Sub-Lease Agreement is conditional on the Grower executing a Management Agreement with the Responsible Entity (clause 2.1).

52. A Grower's allocated CPUs for each Subsequent Year's Sub-Lease Agreement may change at the Responsible Entity's discretion (clause 2.3).

53. The Term of each Sub-Lease Agreement extends from the Commencement Date to the day after the Crop has been harvested from the Co-Production Unit in accordance with the Management Agreement but in any event not exceeding the term of the Lease Agreement.

54. In the first Season, the Term is from the Commencement Date (on or before 31 May 2009) to the day after the wheat, barley and canola has been harvested from the CPUs. The Commencement Date for the Sub-Lease Agreements in the two subsequent Seasons will be prior to planting but before 31 May of the relevant year.

55. If the Grower is unable to plant a Crop on a CPU in any Season due to weather conditions or the inability of the Responsible Entity to source suitable land by 15 June each year, then the Responsible Entity must repay any Rent already paid by the Grower by no later than 20 June in the financial year in which it was paid (clause 10).

Management Agreement

56. Under the Management Agreement, the Grower appoints the Responsible Entity to manage the CPUs and to carry out management services subject to the terms and conditions of the Agreement. The Management Agreement will commence no later than 31 May 2009 and shall continue for an expected 52 months after the Commencement Date or until its termination under clause 14.

57. The Management Agreement is conditional on the Grower entering into a Sub-Lease Agreement with the Responsible Entity (clause 2).

58. Each Season of the Project will have an Initial Period and a Subsequent Period. The Initial Period is the period from Season Commencement until the following 30 June (of years 2009, 2010 and 2011) during which planting of the Crop occurs. Season Commencement is the date the new Crop planting is commenced, being no later than 15 June for each Season. The Responsible Entity will commence the provision of services in the Initial Period and will complete the services by 30 June in the relevant Season.

59. Clause 3.1 of the Management Agreement specifies the services referred to as 'duties' to be performed by the Responsible Entity in the Initial Period. These include:

- establish and maintain suitable access to the CPUs;
- supply, propagate and husband the Seed for the CPUs;
- carry out planting and sowing of the Seed;
- supply and maintain a pest and weed control programme including spraying;
- supply and spread fertiliser on the CPU;
- maintain firebreaks; and
- conduct regular checks on the progress of the Crop on each of the CPUs.

60. In each Season of the Project, the Responsible Entity will commence services in the Subsequent Period from 1 July to the date on which the Crop is harvested.

61. Clause 3.2 of the Management Agreement specifies the services referred to as 'duties' to be performed by the Responsible Entity in the Subsequent Period. These include:

- maintain suitable access to the CPUs;
- maintain firebreaks;
- maintain a pest and weed control programme including spraying as required;
- supply and spread fertiliser on the CPU as required;
- arrange compulsory crop insurance (if available) for the Grower;
- harvest the Crop from the CPU by such means as the Manager in its absolute discretion shall deem reasonably necessary;
- transport, store, stock or handle the Crop in such manner so as to ensure the Crop is preserved and protected until such time as it can be sold; and
- undertake by marketing or other means the sale of the Crop as soon as practically possible after its harvest.

62. If the Grower is unable to plant a Crop on a CPU in any Season due to weather conditions or the inability of the Responsible Entity to source suitable land by 15 June each year, then the Responsible Entity must repay any Initial Period Fees already paid by the Grower by no later than 20 June in the financial year in which they were paid (clause 10).

Service Agreement

63. The Responsible Entity will enter into a Service Agreement with AACL engaging them as Project Manager for the purpose of managing and producing wheat, barley and canola subject to the terms and conditions of the Agreement. AACL will in turn enter into a Farm Management Agreement with various Farmers engaging them to carry out management duties on their behalf.

64. The Service Agreement is conditional on the execution of a Lease Agreement between Macro and AACL.

Crop insurance

65. The Responsible Entity will arrange compulsory crop insurance (subject to availability and market conditions) for each CPU. Crop insurance will cover the Grower against risks such as fire and hail.

66. The cost of the crop insurance will be at the expense of the Grower and will be payable prior to 30 June of the year immediately following Harvest from the Grower's share of the proceeds in the Project Fund. If the proceeds are insufficient the Grower must pay the shortfall.

Pooling of Crops and Grower's Entitlement to Net Proceeds

67. The 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:

- only Growers who have contributed their Farm Produce to wheat, barley and canola pools or insurance proceeds are entitled to benefit from distributions of harvest proceeds from those pools; and
- any pooled Farm Produce must consist only of pools of wheat, barley or canola contributed by Growers of the Project.

68. The proceeds from the each of the Project Pools will be deposited into the Project Fund. The Grower will be entitled to a distribution of the sale proceeds in proportion to the number of CPUs held by the Grower in the Project Pool.

69. The Responsible Entity is entitled to deduct from the Grower's share of the sale proceeds any Project Pool Outgoings. The balance will then be distributed to the Growers on a proportionate basis.

Fees

70. Under the terms of the Management Agreement and the Sub-lease Agreement, a Grower will make payments as described below on a per CPU basis.

Fees and outgoings payable under the Management Agreement

71. The following fees and outgoings are payable by the Grower under the Management Agreement:

- Initial Period Fee for each Season (clause 9.1);
- Subsequent Period Fee for each Season (clause 9.3);
- Manager Performance Bonus (clause 9.4);
- Farmer Production Bonus (clause 9.5);
- Farmer Bonus Adjustment (clause 9.11); and
- Crop insurance (clause 4.2.5).

72. In addition, under clause 8.2 of the Management Agreement, the Responsible Entity will pay all Project Pool Outgoings for each Season from the Project Fund. Project Pool Outgoings include Harvest Period Costs, Warehouse Costs and Harvest Loan Costs.

73. If the funds available in the Grower's Project Pool Entitlement are insufficient to pay any Project Pool Outgoings then the Grower must pay the shortfall prior to 30 June immediately following Harvest (clause 9.16).

Initial Period Fee

74. For the 2009 Season, the Initial Period Fee is $4,345 per CPU. The Initial Period Fee is paid for services from the Commencement Date to 30 June 2009.

75. For each of the 2010 and 2011 Seasons the Initial Period Fee is $3,850 per CPU. The Responsible Entity may recover the Initial Period Fees from the Grower's share of the proceeds in the Project Fund. If the proceeds are insufficient, the Grower must pay the shortfall to the Responsible Entity by 31 May 2010 and 31 May 2011, respectively (clause 9.14).

Subsequent Period Fee

76. The Subsequent Period Fee of $423.50 per CPU is payable in each year of the Project for services performed by the Responsible Entity from 1 July to the date on which the Crop has been harvested from the CPU.

77. The Subsequent Period Fee is payable prior to 30 June of the year immediately following Harvest from the Grower's share of the proceeds in the Project Fund (clause 9.3). If the proceeds are insufficient the Grower must pay the shortfall to the Responsible Entity by 30 June immediately following harvest (clause 9.16).

Farmer Bonus

78. The Farmer Bonus is made up of:

- the Farmer Production Bonus; and
- the Farmer Lease Bonus.

Farmer Production Bonus

79. In consideration for the performance by the Responsible Entity of Initial Period Services and Subsequent Period Services the Responsible Entity is entitled to a Farmer Production Bonus at Harvest in each Season subject to a Grower's CPU producing Crop above the Target Value – Tier 2 of $5,016.

80. The Farmer Production Bonus forms part of the Farmer Bonus and is paid where the Grower's CPU achieves a Harvest Surplus (clause 9.9). A Harvest Surplus refers to that part of the Crop produce harvested from the Grower's CPU that is above the Target Value – Tier 2.

81. The Responsible Entity will retain 20% of the Harvest Surplus in the Project Fund pending the calculation of the Farmer Bonus Adjustment. This is called the Farmer Bonus Retention (clause 9.10).

82. Harvest Surplus less the Farmer Bonus Retention is referred to as Distributable Harvest Surplus (Item 12 of the Schedule to the Management Agreement).

83. The Farmer Production Bonus is 50% of the Distributable Harvest Surplus and is deducted from the Project Fund and paid in cash (Item 12 of the Schedule to the Management Agreement).

84. In calculating the Farmer Production Bonus the Responsible Entity must determine the Delivered Price under the method set out in Item 9 of the Schedule to the Management Agreement. Unless the Responsible Entity decides that the method for calculating the Delivered Price under Item 9 is no longer an appropriate price for the Grain, the Delivered Price is calculated under Item 9 (clause 9.6).

Farmer Bonus Adjustment

85. The Farmer Bonus Adjustment is calculated by the Responsible Entity at the Determination Date (clause 9.11).

86. The Determination Date means the earliest of:

(i) the date that all Project Pool Produce have been received as determined by the Responsible Entity; or

(ii) in respect of each season no later than the following dates:

- Season 2009 – 30 April 2010;
- Season 2010 – 30 April 2011;
- Season 2011 – 30 April 2012.

87. The calculation of the Farmer Bonus Adjustment is based on the Final Value of the Grain rather than the Delivered Value and is set out in Item 18 of the Schedule to the Management Agreement.

88. The Farmer Bonus Adjustment is payable in each Season of the Project and is paid from the proceeds in the Project Fund. If the funds available in the Project Fund are insufficient then the Grower must pay the shortfall prior to 30 June immediately following Harvest (clause 9.11).

Manager Performance Bonus

89. The Manager Performance Bonus is payable to the Responsible Entity at Harvest in each season subject to the Delivered Value on a CPU being greater than Target Value – Tier 1 of $4,620.

90. The Manager Performance Bonus is deducted from the Project Fund in the form of dollars at Harvest.

91. The Manager Performance Bonus is calculated in accordance with item 13 of the Schedule to the Management Agreement.

Fees payable under the Sub-Lease Agreements

92. Under the Sub-Lease Agreements, the following fees are payable by the Grower:

- Initial Period Rent;
- Subsequent Period Rent; and
- Farm Lease Bonus (clause 5).

Rent

93. The Grower will pay the Responsible Entity Rent of $247.50 for the 2009, 2010 and 2011 Seasons of the Project consisting of:

- $55 payable in respect of the Initial Period from season commencement to 30 June; and
- $192.50 for the Subsequent Period, from 1 July until the completion of Harvest in each Season.

94. For the 2009 Season the Initial Period Rent is payable on Application. The Subsequent Period Rent is payable prior to 30 June 2010 from the Grower's share of the proceeds in the Project Fund. If the proceeds are insufficient the Grower must pay the shortfall.

95. For the 2010 and 2011 Seasons the Initial Period Rent and the Subsequent Period Rent will be payable prior to 30 June of the year immediately following Harvest from the Grower's share of the proceeds in the Project Fund. If the proceeds are insufficient the Grower must pay the shortfall.

Farm Lease Bonus

96. In consideration of the performance by the Responsible Entity in the selection of the land for the Project the Responsible Entity is entitled to a Farm Lease Bonus (clause 5.3).

97. The Farm Lease Bonus is payable at Harvest each Season and its entitlement is subject to a Grower's CPU producing Crop above the Target Value – Tier 2 of $5,016 (clause 5.6).

98. The Farm Lease Bonus is calculated as 50% of the Distributable Harvest Surplus and is deducted from the Project Fund and paid in cash.

99. The calculation of the Farm Lease Bonus is set out in Item 10 of the Schedule to the Sub-Lease Agreement.

Finance

100. There is no financing facility offered by the Responsible Entity or any other party to the arrangement. Growers can fund their investment in the Project themselves, or borrow from an independent lender. Growers cannot rely on any part of this Ruling if the Application money is not paid in full on or before 31 May 2009. Subject to assurances provided by Macro on 13 May 2009, where the Application money is being financed through a lending institution written evidence of approval must be provided to the Responsible Entity by the lending institution on or before 15 June 2009. The lending institution must provide the full amount of the loan monies to the Responsible Entity no later than 30 June 2009.

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

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

Commissioner of Taxation
20 May 2009

Appendix 1 – Explanation

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?

102. For the amounts set out in paragraph 22 of this Ruling to constitute allowable deductions the Grower's grain growing activities as a participant in the 2009 Grain Co-Production Project must amount to the carrying on of a business of primary production.

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

104. More recently, and in relation to a managed investment scheme similar to that which is the subject of this Ruling, the Full Federal Court in *Hance v. FC of T*; *Hannebery v. FC of T* [2008] FCAFC 196; 2008 ATC 20-085 applied these principles to conclude that 'Growers' in that scheme were carrying on a business of producing almonds (at FCAFC 90; ATC 90).

105. Application of these principles to the arrangement set out above leads to the conclusion that Growers (as described in paragraphs 3 and 4), who stay in the Project until its completion, will be carrying on a business of primary production involving growing and harvesting of wheat, barley and canola for sale.

Deductibility of Initial Period Fee, Subsequent Period Fee, Rent, and other Project Pool Outgoings

Section 8-1

106. The Initial Period Fee, Subsequent Period Fee, Rent, and other Project Pool Outgoings are deductible under section 8-1. A 'non-income producing' purpose is not identifiable in the arrangement and there is no capital component evident in the fees payable under the Management and Sub-Lease Agreements.

107. 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 108 to 112 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

108. The prepayment provisions contained in Subdivision H of Division 3 of Part III of the ITAA 1936 affect the timing of deductions for certain prepaid expenditure. These provisions apply to certain expenditure incurred under an agreement in return for the doing of a thing under the agreement (for example, the performance of management services or the leasing of land) that will not be wholly done within the same year of income as the year in which the expenditure is incurred. If expenditure is incurred to cover the provision of services to be provided within the same year, then it is not expenditure to which the prepayment rules apply.

109. 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

110. Under the scheme to which this Product Ruling applies Initial Period Fees, Subsequent Period Fees, Rent and other Project Pool Outgoings are incurred annually. Accordingly, the prepayment provisions in sections 82KZME and 82KZMF of the ITAA 1936 have no application to this scheme.

111. However, sections 82KZME and 82KZMF of the ITAA 1936 may have relevance if a Grower in this Project prepays all or some of the expenditure payable under the Management Agreement and the Sub-Lease Agreement, or prepays interest under a loan agreement with lenders. Where such a prepayment is made these prepayment provisions will also apply to 'small business entities' because there is no specific exclusion contained in section 82KZME that excludes them from the operation of section 82KZMF.

112. As noted in the Ruling section 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.

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

113. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income year ended 30 June 2009, based on the evidence supplied, the Commissioner has determined that for that income year:

- 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 Grain industry, a Grower's business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

114. 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.

115. The exercise of the Commissioner's discretion under paragraph 35-55(1)(b) for Growers who will stay in the Project until its completion 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

116. 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

117. 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).

118. The 2009 Grain Co-Production 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 22 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.

119. 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 wheat, barley and canola. 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.

Appendix 2 – Detailed contents list

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

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 97/7; TR 97/11; TR 98/22

Subject references:

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

Legislative references:

- ITAA 1936
- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZLA
- 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
- ITAA 1997 6-5
- ITAA 1997 8-1
- ITAA 1997 17-5
- ITAA 1997 Div 27
- ITAA 1997 Div 35
- ITAA 1997 35-10
- ITAA 1997 35-10(2)
- ITAA 1997 35-55
- ITAA 1997 35-55(1)(b)
- SISA 1993
- Copyright Act 1968
- Corporations Act 2001

Case references:

- Hance v. FC of T; Hannebery v. FC of T [2008] FCAFC 196; 2008 ATC 20-085

ATO references

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