


PR 2009/37 - Income tax: Rewards Group Premium Vineyard Project 2009

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Product Ruling

Income tax: Rewards Group Premium Vineyard Project 2009

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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, 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 Product Ruling relates. In this Product Ruling the scheme is referred to as the Rewards Group Premium Vineyard Project 2009 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 31 of this Ruling on or before 15 June 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 15 June 2009;
 - participate in the scheme through offers made other than through the Product Disclosure Statement (PDS), 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;

- subject to paragraph 77 of this Ruling, Growers whose application money is not paid in full to the Responsible Entity on or before 15 June 2009, either by the Grower and/or on the Grower's behalf by a lending institution; or
- Growers who finance their participation in the Project with loans from QPR Capital Finance Pty Ltd or the Preferred Financier other than as described at paragraphs 78 to 80 of this Ruling.

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 31 to 80 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.

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Date of effect

10. This Product Ruling applies prospectively from 20 May 2009, the date this Product Ruling is made. It therefore applies to the specified class of entities that enter into the scheme from 20 May 2009 until 15 June 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 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 Product Ruling as a Grower) to be entitled to claim input tax credits for the GST included in any creditable acquisitions it makes, it must be registered or required to be registered for GST and hold a valid tax invoice.

Ruling

Application of this Product 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 31 to 80 of this Ruling.

17. The Grower's participation in the Project must constitute the carrying on a business of primary production. Provided the Project is carried out as described below, the Grower's business of primary production will commence at the time of execution of their Sub-lease and Management Agreement.

Minimum subscription

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. Under the terms of the PDS, a Grower's application will not be accepted and the Project will not proceed until the minimum subscription of 50 Groves is achieved.

Concessions for 'small business entities'¹

19. From the 2007-08 income year, a range of concessions previously available under the simplified tax system (STS), became 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

Sections 6-5 and 17-5

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.

¹ The meaning of 'small business entity' is explained in section 328-110.

22. For gross sales proceeds attributable to the Joint Venture Growers:

- the First Joint Venturer will be assessable on 28%; and
- the Second Joint Venturer will be assessable on the balance of 72%,

less any GST payable on those proceeds.

Deductions for Project fees

Sections 8-1 and 25-25 and Division 27 of the ITAA 1997 and sections 82KZME and 82KZMF of the ITAA 1936

23. A Grower may claim tax deductions for the following fees and expenses on a per Grove 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
Management Services (Fixed Component) Fees	\$8,124.23 See Notes (i) & (ii)	\$1,753.08 See Notes (i) & (iii)	\$1808.71 See Notes (i), (ii) & (iv)
Rent	\$87.77 See Notes (i) & (ii)	\$1,053.25 See Notes (i), (ii) & (iii)	\$1,053.25 (indexed) See Notes (i), (ii) & (iv)
Management Services (Harvest Component) Fee	Nil	As incurred See Notes (i) & (ii)	As incurred See Notes (i) & (ii)
Harvest costs	Nil	As incurred See Notes (i) & (ii)	As incurred See Notes (i) & (ii)
Costs of sale	Nil	As incurred See Notes (i) & (ii)	As incurred See Notes (i) & (ii)
Credit card merchant fee	As incurred See Notes (i) & (v)	As incurred See Notes (i) & (v)	As incurred See Notes (i) & (v)
Interest	As incurred See Notes (i), (iv) & (vi)	As incurred See Notes (i), (iv) & (vi)	As incurred See Notes (i), (iv) & (vi)
Borrowing fee	Must be calculated See Note (vii)	Must be calculated See Note (vii)	Must be calculated See Note (vii)

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 Management Services (Fixed Component) Fees, Rent, Management Services (Harvest Component) Fees, Harvest costs and costs of sale are deductible under section 8-1 in the income year that the relevant fee is incurred.
- (iii) The Management Services (Fixed Component) Fee and Rent due on or before 1 October 2009 may be prepaid at the time of application. If these amounts are prepaid at the time of application they will not be deductible in the year incurred. Deductions for these amounts must be determined using the formula in subsection 82KZMF(1) of the ITAA 1936 (see paragraphs 91 to 95 of this Ruling). This provision operates to apportion expenditure over the eligible service period. The eligible service period is from 1 July 2009 to 30 June 2010. Therefore, no amount is deductible in the year ended 30 June 2009 and amounts of \$1,753.08 (Management Services (Fixed Component) Fee) and \$1,053.25 (Rent) per Grove are deductible in the income year ending 30 June 2010.
- (iv) Other than as described in note (iii) above, this Ruling does not apply to Growers who choose to prepay management fees or rent or who choose to, or are required to prepay interest under a finance arrangement. 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 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) Growers who use their credit card to pay the fees for this Project may incur a merchant fee for the use of their credit card. This fee will be deductible under section 8-1.
- (vi) Interest payable to QPR Capital Finance Pty Ltd (QPR) or the Preferred Financier under the finance arrangements described at paragraphs 78 and 79 of this Ruling is deductible section 8-1 in the income year in which it is incurred. The deductibility or otherwise of interest arising from agreements entered into with financiers other than QPR or the Preferred Financier is outside the scope of this Ruling.

- (vii) The loan application fee (being 0.25% of the finance application amount, subject to a minimum charge of \$250) payable to either QPR or the Preferred Financier is a borrowing cost and is deductible under section 25-25. Any stamp duty payable by the Growers is also a borrowing cost and deductible under section 25-25. These fees are 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 arrangements entered into with financiers other than QPR or the Preferred financier is outside the scope of this ruling.

Joint Venturer Growers

24. The First Joint Venturer Grower may claim the following deductions per Grove in respect of the items described in the table above (and accompanying Notes):

- the Management Services (Fixed Component) Fee and Rent for the period from commencement to 30 June 2009;
- 28% of the Management Services (Harvest Component) Fees;
- 28% of Harvest costs and costs of sale; and
- if applicable, credit card merchant fee, interest and loan Application Fee.

The Second Joint Venturer Grower may claim the following deductions per Grove in respect of the items described in the table above (and accompanying Notes):

- the Management Services (Fixed Component) Fee and Rent for the period from 1 July 2009;
- 72% of the Management Services (Harvest Component) Fees;
- 72% of Harvest costs and costs of sale; and
- if applicable, insurance and credit card merchant fee.

Deductions for capital expenditure**Division 40**

25. A Grower will be entitled to tax deductions relating to a 'landcare operation' and grapevines. All deductions shown in the following Table are determined under Division 40.

Fee Type	ITAA 1997 Section	Year ending 30 June 2009	Year ending 30 June 2010	Year ending 30 June 2011
Landcare Services Fee	40-630	\$1,185.94 See Notes (i) & (viii)	Nil	Nil
Establishment of horticultural plants (including Planting Fee)	40-515	Nil	Nil	Must be calculated See Notes (i) & (ix)

Notes:

- (viii) Any capital expenditure incurred for a 'landcare operation' (as defined in section 40-635) is fully deductible in the year in which it is incurred under Subdivision 40-G, section 40-630. Accordingly the expenditure incurred on drainage works and the installation of measures to prevent soil erosion is deductible in the year ending 30 June 2009.
- (ix) Grapevines are a 'horticultural plant' as defined in subsection 40-520(2). As Growers hold the land under a Sub-lease, one of the conditions in 40-525(2) is met and a deduction for horticultural plants' is available under paragraph 40-515(1)(b) for their decline in value. The deduction for the grapevines is determined using the formulae in section 40-545 and is based on the capital expenditure incurred that is attributable to their establishment. If the grapevines have an 'effective life' of greater than 13 but fewer than 30 years for the purposes of section 40-545, this results in a straight-line write-off at a rate of 13%. The deduction is allowable when the grapevines enter their first commercial season (section 40-530, item 2). The Project Manager will inform Growers of when the grapevines enter their first commercial season and the amount incurred by the Manager in establishing the grapevines.

Joint Venture Growers

26. The First Joint Venturer Grower may claim the following deductions per Grove in respect of the items described in the table above (and in accordance with the accompanying Notes):

- Landcare Services Fee; and
- the initial capital expenditure for the establishment of horticultural plants, being the first year Planting Fee.

27. The Second Joint Venturer Grower may claim deductions for the capital expenditure for the establishment of horticultural plants, being the second year Planting Fee, as calculated according to the Notes.

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

Section 35-55 – exercise of Commissioner’s discretion

28. 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 income year ended 30 June 2009, may make losses from the Project that may be affected by the loss deferral rule in section 35-10.

29. 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 years ending 30 June 2009 to 30 June 2012. Exercise of the discretion in this case however is conditional on the Project being carried out in the manner described in paragraphs 31 to 80 of this Ruling and 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

30. For a Grower who commences participation in the Project and incurs expenditure as required by the Sub-Lease and Management 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 (but see paragraphs 89 to 95 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 Product Ruling.

Scheme

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

- Application for a Product Ruling received on 12 February 2009 and additional correspondence between the Tax Office and the Applicant dated 13 February 2009, 9 April 2009, 14 April 2009, 15 April 2009, 16 April 2009, 17 April 2009, 22 April 2009, 23 April 2009, 24 April 2009, 30 April 2009, 6 May 2009, 12 May 2009 and 13 May 2009;
- Draft Product Disclosure Statement received on 14 April 2009;
- Draft Replacement Constitution received on 14 April 2009;
- Draft Lease between the Lessor and the Responsible Entity received on 12 February 2009;
- Draft **Sub-Lease** between the Responsible Entity and the Grower received on 14 April 2009;
- Draft **Management Agreement** received 14 April 2009;
- Draft Compliance Plan received on 12 February 2009;
- Draft Viticultural Expert Report received on 12 February 2009;
- Draft Management Plan (Pemberton) received on 12 February 2009;
- Draft Grape Sale and Purchase Agreement received 12 February 2009;
- Draft Operations Agreement received 14 April 2009;
- Origination Deed between the Rewards Group Ltd and the Preferred Financier, received 8 April 2009; and
- **Loan Application** package for finance to be provided by the Preferred Financier, received 14 April 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.

32. The documents highlighted (in bold font) are those that a Grower may enter into. For the purposes of describing the scheme to which this Product 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.

33. 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

34. The main features of the Rewards Group Premium Vineyard Project 2009 are as follows:

Location	Pemberton, Western Australia
Type of business to be carried on by each Grower	Viticulture
Term of the Project	Approximately 20 years
Size of the Project	150 hectares
Size of each Interest	0.25 hectares
Minimum allocation per Grower	One Grove
Minimum subscription	50 Groves
Initial cost to Growers	\$9,900
Ongoing costs	Management Services (Fixed Component) Fee, Rent, Harvest and costs of sale, Management Services (Harvest Component) Fee

35. The Project will be a registered managed investment scheme under the *Corporations Act 2001*. Rewards Projects Ltd has been issued with an Australian Financial Service Licence No. 224000 and will be the Responsible Entity for the Project.

36. The Project will involve the establishment and maintenance of vineyards for the purpose of producing wine grapes for sale.

37. An offer to participate in the Project will be made through a Product Disclosure Statement (PDS). The offer under the PDS is for 150 plantable hectares, which corresponds to 600 Groves in the Project each of 0.25 hectares.

38. A Grower will participate in the Project by acquiring an interest which will consist of a minimum of one Grove.

39. Applicants execute a Power of Attorney contained in the PDS. The Power of Attorney irrevocably appoints Responsible Entity to enter into, on behalf of the Grower the Management Agreement, Sub-lease and any other documents required to hold an interest in the Project.

40. For the purposes of this Product Ruling, Applicants who are accepted to participate in the Project on or before 15 June 2009 will become Growers. The term of the Project is approximately 20 years.

41. Under the terms of the PDS, the interests in the Growers' Groves will be issued after a minimum subscription of 50 Groves has been achieved.
42. The Responsible Entity will lease established Vineyards and establish new Vineyards which will be located in the Pemberton appellations. Each Grove will be comprised of approximately 50% fully established vines, 25% established vines that are less than 2 years of age and 25% newly established vines.
43. The properties are more specifically described as:
- Stirling Road, Pemberton – Lot 11938 on Deposited Plan 161273 being the whole of the land in Certificate Title Volume 1849 Folio 197
 - Kemp Road, Pemberton – Lot 500 on Deposited Plan 60842 being the whole of the land in Certificate Title Volume 2698 Folio 67.
44. The water supply required to irrigate the properties will come from storage dams located on the properties. To ensure a year-round water supply, the landowner will make available all water from their dams as it relates to the land leased for the project.

Constitution

45. The Constitution establishes the Project and operates as a deed binding all Growers and the Responsible Entity. The Constitution sets out the terms and conditions under which Rewards Projects Ltd 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.
46. The Constitution does not specify the required form of an application – though the Responsible Entity produces an Application Guide which includes an Application Form.
47. Under clause 8.2 of the Constitution, the Responsible Entity will hold all application moneys on trust for the applicants in a 'Subscription Fund'.
48. According to clause 3.3, moneys may not be released from the Subscription Fund until:
- minimum subscription has been reached;
 - a legal expert advises that the lessor can grant the sub-leases to the Growers and the Project land is not subject to any detrimental encumbrances;
 - the Sub-lease and Management Agreements are in the proper form and any other matters necessary for the creation of these Agreements have been attended to; and
 - there are no material breaches of the Constitution.

49. Upon acceptance of an application:

- the application money will remain in the same trust bank account, but will be deemed to be the Project Fund (clause 8.3);
- the applicant becomes a Grower in the Project (clause 3.4);
- and money can be released from the Project Fund for payment of Project Fees (clause 3.6).

50. The Responsible Entity will hold the application moneys on bare trust in the Project Fund. Once the Responsible Entity has accepted the Applications and all of the Project documents have been executed and remain in force, the Application Fees will be transferred from the Project Fund to the Responsible Entity for the conduct of the Project.

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

- powers and responsibilities of the Responsible Entity (clause 6);
- sale of a Grower's interest in the Project if a Grower default in payment of Project Fees (clause 9.4);
- payment of monies from the Proceeds Fund (clause 11);
- complaints, alternative dispute resolution and legal proceedings (clause 12);
- commencement and termination of the Project (clause 14);
- Grower's rights (clause 15);
- destruction and insurance of Groves (clauses 18 and 19); and
- Joint Venturers (clause 20).

Compliance Plan

52. As required by the *Corporations Act 2001*, Rewards Project Ltd 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.

Head Lease

53. The Responsible Entity will enter into Head Leases with the Lessor(s) in respect of Land required for the Project. The Project Land will be located in Pemberton in Western Australia.

54. Under the Head Lease, the Responsible Entity is able to sub-lease the Land or any part of the Land to Growers in the Project for a term equivalent of the term of the lease.

55. The Responsible Entity and Growers must use the Land only for the purpose of growing wine grapes for commercial sale.

Sub-lease

56. Each grower will execute a Sub-lease with the Responsible Entity as the Sub-Lessor. The Responsible Entity will grant to the Grower the right to exclusively possess, occupy, use and enjoy the Groves for the conduct of the Grower's business of growing, harvesting and selling wine grapes for commercial profit.

57. The Sub-lease Agreement sets out the rights and obligations of the parties to the Agreement. Clause 5.3 specifies that the Responsible Entity (as Sub-Lessor) shall at no additional cost to the Grower install or procure suitable irrigation systems for the new vineyards on or before 30 June 2009. The Sub-Lessor shall allow water stored in dams on the Land to be used for irrigation of the Groves.

58. Clause 5.4 specifies that suitable trellis systems will be installed by the Sub-Lessor for the new vineyards, with no additional cost to the Grower on or before 30 June 2009.

Operations Agreements

59. The Responsible Entity will enter into an Operations Agreement with Rewards Management Pty Ltd, whereby the latter is appointed as Manager to carry out, in accordance with sound agricultural and environmental practices adopted within the agricultural industry, the Responsible Entity's obligations under the Management Agreement.

Management Agreements

60. The Responsible Entity is appointed under the Management Agreement to carry out Initial Services and Ongoing Services, on behalf of each Grower. The Initial Services are detailed at Annexure A of the Management Agreement and include:

- Planting Services being the supply of suitable rootlings, preparation of land and planting the rootlings in the new vineyard;
- landcare services;
- negotiating sales agreements with wineries; and
- pruning, fertilising, weed control, and replacing plant mortality for the established vineyards.

61. Planting Services relating to the supply of rootlings and the preparation of land will be completed by 30 June 2009. The remaining Planting Services will be completed by 30 September 2009 (clause 1).

62. Ongoing Management Services are detailed in Annexure B of the Management Agreement.

63. The Responsible Entity is irrevocably appointed to arrange each harvest at any time deemed appropriate (clause 6).

Pooling of Crops and Grower's entitlement to proceeds

64. The Management Agreement at clause 6.3 requires the Responsible Entity to pool all Fruit from each harvest. The Constitution and the Management Agreement set out provisions relating the Grower's entitlement to the proceeds of harvest.

65. The Responsible Entity is authorised to appoint Fruit Agents to negotiate the sale of the Harvested Fruit, and must ensure that the Fruit Agent negotiates the highest price practicable, and the pooled Fruit will be sold collectively (clause 7).

66. Receipts, being the proceeds from the sale of Grower's Fruit or insurance proceeds from claims in respect of Growers' Vineyards, are to be held in the Proceeds Fund (clause 6.1(u) of the Constitution).

67. The balance in the Proceeds Fund shall be distributed to Growers after deducting the following payments (clause 11.1 of the Constitution):

- costs of harvest and sale;
- project fees, and other fees, costs, interest or taxes payable to the Responsible Entity under the Constitution;
- reasonable estimates of the amount of Project Fees payable by the Grower in the following 12 months under the Management Agreement;
- amounts owing to the Sub-Lessor; and
- any other amounts owed by the Grower to the Responsible Entity.

68. Each Grower's share of the Proceeds Fund is restricted to their proportionate share (after costs). The 'Rights to Receipts' of Joint Venture Growers are set out in clause 20.5 of the Constitution.

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

- only Growers who have contributed Fruit or insurance proceeds are entitled to benefit from distributions from the Proceeds Fund; and
- any pooled Fruit and or Receipts must consist only of Fruit or Receipts contributed by Growers of the same Project Class.

Fees

70. The initial subscription payable by a Grower is \$9,900 per Grove, consisting of:

- **Management Services Fee** (Fixed Component) of \$8,124.23 for services to be provided from the Commencement Date to 30 June 2009 (item 2 of the Schedule to the Management Agreement);
- **Landcare Services Fee** of \$1,185.94 for services to be provided from the Commencement Date to 30 June 2009 (items 3 of the Schedule to the Management Agreement);
- **Planting Fee** of \$502.06 per Grove payable to the Responsible Entity from the Commencement Date to 30 June 2009; and
- **Rent** of \$87.77 for the period from the Commencement Date to 30 June 2009 (item 4 of the Schedule to the Sub-lease).

The fees payable **per Grove** from 1 July 2009 are:

- **Management Services (Fixed Component) Fees** (Item 2 of the Schedule to the Management Agreement) of:
 - \$1,753.08 per Grove for services to be provided from 1 July 2009 to 30 June 2010, payable on or before 1 October 2009; and;
 - \$1,808.71 per Grove for services to be provided from 1 July 2010 to 30 June 2011, payable on or before 1 October 2010; and;
 - \$1,891.86 per Grove for services to be provided from 1 July 2011 to 30 June 2012, payable on or before 1 October 2011, and;
 - Thereafter until the end of the Project, the fee is calculated with reference to the previous year's fee increased by the Index Factor. The Management Services (Fixed Component) Fee is payable on or before 1 October of the relevant year.
- **Planting Fee** of \$93.67 to supply vines and prepare the land for planting during the period from 1 July 2009 to 30 September 2009, payable on or before 1 October 2009 (item 4 of the Schedule to the Management Agreement);

- **Management Services (Harvest Component) Fee** equal to 11% of the Grower's share of the net sale proceeds of each harvest after deducting the Harvest costs and the costs of sale (Item 5 of the Schedule to Management Agreement);
- **Harvest costs**, being all costs incidental or otherwise for picking, packing and transport of Fruit from the Groves, payable out of the Receipts of the (clause 6.2 of Management Agreement and clause 11.1 of the Constitution);
- the Grower's share of the **costs of sale** of any saleable Fruit derived from Vineyards including royalties or sale commissions, payable out of the Receipts of the Project (clause 7.5 of Management Agreement and clause 11.1 of the Constitution);
- **Optional vine insurance** for the period after 30 June 2009; and
- **Rent** (Item 4 of the Schedule to the Sub-leases) of:
 - \$1,053.25 for the period 1 July 2009 to 30 June 2010, payable on or before 1 October 2009;
 - thereafter until the end of the Term, the fee is calculated with reference to the previous year's fee increased by the Index Factor. Rent is payable on or before 1 October of the relevant financial year.

Joint Venturers

71. Two entities can enter the Project as a Joint Venturers. The obligations, rights and interests of such applicants are set out in clause 20 of the Constitution.

72. The First Joint Venturer will pay the following amounts:

- \$9,900 initial subscription fee; and
- 28% of each of the Management Services (Harvest Component) Fee, Harvest costs, costs of sale and any other amounts due to the Responsible Entity under the Constitution, Sub-Lease, or Management Agreement.

73. The Second Joint Venturer will pay the following amounts from 1 July 2009:

- Management Services (Fixed Component) Fees,
- Planting Fee,
- Rent,
- any Optional insurance, and

- 72% of each of the Management Services (Harvest Component) Fee, Harvest costs, costs of sale, and any other amounts due to the Responsible Entity under the Constitution, Sub-Lease, or Management Agreements.

74. The First Joint Venturer and Second Joint Venturer are entitled to 28% and 72% respectively of the Receipts associated with the joint venture Groves.

Finance

75. To finance all or part of the cost of their participation in the Project a Grower can enter into a finance arrangement with QPR Capital Finance Pty Ltd (QPR), or the Preferred Financier or, alternatively, borrow from an independent lender external to the Project.

76. A finance package has been provided for this Project which outlines the terms and conditions upon which finance will be provided by either QPR or the Preferred Financier. The finance offered by each of these parties is set out below and only those arrangements are covered by this Product Ruling. A Grower cannot rely on this Product Ruling if they enter into a finance arrangement with QPR or the Preferred Financier that materially differs from that set out in the documentation provided with the application for this Product Ruling.

77. The deductibility of interest for Growers who enter into finance arrangements other than with QPR or the Preferred Financier is not covered by this Ruling. Such Growers may request a private ruling on the deductibility or otherwise of interest incurred under finance arrangements not covered by this Product Ruling. A Grower cannot rely on any part of this Ruling if the Application Fees are not paid in full on or before 15 June 2009 by the Grower or, on the Grower's behalf by a lending institution.

Finance offered by the Preferred Financier

78. The Preferred Financier is an arm's length third party and will provide loans up to 100% of the Application Price on full recourse commercial terms. The Loan Agreement offered by the Preferred Financier provides the following features:

- the financier will take security over the Growers' Grove;
- a loan Application Fee of 0.25% of the loan amount is payable subject to a minimum amount of \$250;
- the interest rate will be set at a specific rate on 15 June 2009;
- default interest on overdue amounts will be charged at an additional 4.5% interest per annum. Default interest will be calculated daily and accrued monthly;

- monthly repayments of principal and interest are due in the manner indicated by the (loan) application guide and in accordance with the Loan Agreement, commencing in July 2009;
- an interest only period of up to 3 years is available for loan periods between 5 and 15 years;
- a Monthly Loan Service Fee of \$20 is payable for all loans; and
- Borrowers can drawdown funds to cover the Management Services (Fixed Component) Fees and Rent for the Initial Period and the first year.

Finance offered by QPR

79. The full terms of the Loan Agreement offered by QPR are included in the PDS at section 9 of the Application Guide. The Loan Agreement provides the following features:

- the financier will take security over the Growers' Grove;
- a loan Application Fee of 0.25% of the loan amount is payable on 15 June 2009 subject to a minimum amount of \$250;
- the Loan Term is 12 months;
- the loan is interest free except that interest will be charged on overdue amounts at the Base Rate plus 4.5% interest per annum. Default interest will be calculated daily and accrued monthly; and
- monthly repayments are due in the manner indicated by the Finance Application and in accordance with the Loan Agreement, commencing in July 2009.

80. 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 QPR or the Preferred Financier, are involved or become involved in the provision of finance to Growers for the Project.

Commissioner of Taxation20 May 2009

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?

81. For the amounts set out in paragraphs 23 of this Ruling to above to constitute allowable deductions, the Grower’s viticulture activities as a participant in the Rewards Group Premium Vineyard Project 2009 must amount to the carrying on of a business of primary production.

82. 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?

83. More recently, and in relation to a managed investment scheme similar to that which is the subject of this Product 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).

84. Application of these principles to the arrangement set out above leads to the conclusion that Growers (as described in paragraphs 4 and 5 of this Ruling), who stay in the Project until its completion, will be carrying on a business of primary production involving growing and harvesting of grapes for sale.

Deductions for Project Fees

Section 8-1

85. The Management Services (Fixed Component) Fees, Rent, credit card merchant fees, Harvest costs, costs of sale, and interest on loans with the Responsible Entity or the Preferred Financier 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 Management Services Fees or Rent.

86. 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 89 to 94 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.)

87. Some Growers may finance their participation in the Project through a Loan Agreement with QPR or the Preferred Financier. Applying the same principles as that used for the Management Services (Fixed Component) Fees etc above, interest incurred under such a loan has sufficient connection with the gaining of assessable income to be deductible under section 8-1.

88. Other than where the prepayment provisions apply (see paragraphs 89 to 95 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 82KZMF

89. 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.

Application of the prepayment provisions to this Project

90. 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).

91. Under the scheme to which this Product Ruling applies Management Services Fees, Rent and other fees are incurred annually and the interest payable to QPR Finance Pty Ltd or 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 this scheme.

92. However, the Management Services (Fixed Component) Fee and Rent for the year ending 30 June 2010 may be prepaid under a financing agreement with the Preferred Financier. In this case, sections 82KZME and 82KZMF of the ITAA 1936 will apply to apportion the expenditure and allow a deduction over the period that the benefits are provided.

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

93. In the formula 'eligible service period' (defined in subsection 82KZL(1) of the ITAA 1936) means, the period during which the thing under the agreement is to be done. The eligible service period begins on the day on which the thing under the agreement commences to be done or on the day on which the expenditure is incurred, whichever is the later, and ends on the last day on which the thing under the agreement ceases to be done, up to a maximum of 10 years.

94. Sections 82KZME and 82KZMF of the ITAA 1936 may also have relevance if a Grower in this Project prepays any other amount of the expenditure payable under the Management Agreement and/or the Sub-lease(s), or prepays interest under a loan agreement (including loan agreements with lenders other than the Responsible Entity or the Preferred Financier). 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.

95. As noted in the Ruling section above, Growers who prepay fees, other than the Management Services (Fixed Component) Fee and Rent as described above at paragraph 92 of this Ruling, are not covered by this Product Ruling and may instead request a private ruling on the tax consequences of their participation in this Project.

Expenditure of a capital nature

Division 40

96. Any part of the expenditure of a Grower that is attributable to acquiring an asset or advantage of an enduring kind is generally capital or capital in nature and will not be an allowable deduction under section 8-1. In this Project, expenditure attributable to landcare and the establishment of the grapevines is of a capital nature. This expenditure falls for consideration under Division 40.

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

Sections 35-10 and 35-55

97. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis for the income years ended 30 June 2009 to 30 June 2012, 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 viticultural industry, a Grower's business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

98. 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.

99. 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 Product Ruling during the income years specified. If the Project is carried out in a materially different way to that described in this Product 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

100. 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

101. 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).

102. The Rewards Group Premium Vineyard Project 2009 will be a scheme. A Grower will obtain a tax benefit from entering into the scheme, in the form of tax deductions for the amounts detailed at paragraphs 23 to 27 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.

103. Growers to whom this Product Ruling applies intend to stay in the scheme for its full term and derive assessable income from the harvesting and sale of the grapes. There are no facts that would suggest that Growers have the opportunity of obtaining a tax advantage other than the tax advantages identified in this Product Ruling. There is no non-recourse financing or round robin characteristics, and no indication that the parties are not dealing at arm's length or, if any parties are not dealing at arm's length, that any adverse tax consequences result. Further, having regard to the factors to be considered under paragraph 177D(b) of the ITAA 1936 it cannot be concluded, on the information available, that participants will enter into the scheme for the dominant purpose of obtaining a tax benefit.

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

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

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
- tax avoidance
- taxation administration

Legislative references:

- ITAA 1936
- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL
- ITAA 1936 82KZL(1)
- 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 82KZMF(1)
- 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
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- ITAA 1997 17-5
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- ITAA 1997 Div 35
- ITAA 1997 35-10
- ITAA 1997 35-10(2)
- ITAA 1997 35-55
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- ITAA 1997 Subdiv 40-G
- ITAA 1997 40-515
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- Hance v. FC of T; Hannebery v. FC of T [2008] FCAFC 196; 2008 ATC 20-085

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