

PR 2006/143 - Income tax: 2007/2008 Timbercorp (Single Payment) Timberlot Project (Post 30 June Growers)



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Product Ruling

Income tax: 2007/2008 Timbercorp (Single Payment) Timberlot Project (Post 30 June Growers)

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❶ This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

No guarantee of commercial success

The Tax Office **does not** sanction or guarantee this product. Further, we give no assurance that the product is commercially viable, that charges are reasonable, appropriate or represent industry norms, or that projected returns will be achieved or are reasonably based.

Potential participants must form their own view about the commercial and financial viability of the product. This will involve a consideration of important issues such as whether projected returns are realistic, the 'track record' of the management, the level of fees in comparison to similar products and how the product fits an existing portfolio. We recommend a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential participants by confirming that the tax benefits set out in the **Ruling** part of this document are available, **provided that** the scheme is carried out in accordance with the information we have been given, and have described below in the **Scheme** part of this document.

If the scheme is not carried out as described, participants lose the protection of this Product Ruling. Potential participants may wish to seek assurances from the promoter that the scheme will be carried out as described in this Product Ruling.

Potential participants should be aware that the Tax Office will be undertaking review activities to confirm the scheme has been implemented as described below and to ensure that the participants in the scheme include in their income tax returns income derived in those future years.

Terms of use of this Product Ruling

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

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates. In this Ruling this scheme is sometimes referred to as the 2007/2008 Timbercorp (Single Payment) Timberlot Project – Post 30 June Growers or simply as the Project.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
 - section 8-1 (ITAA 1997);
 - section 17-5 (ITAA 1997);
 - section 25-25 (ITAA 1997);
 - Division 27 (ITAA 1997);
 - Division 35 (ITAA 1997);
 - Subdivision 61-J (ITAA 1997);
 - Division 328 (ITAA 1997);
 - section 82KL of the *Income Tax Assessment Act 1936* (ITAA 1936);
 - section 82KZL (ITAA 1936);
 - sections 82KZME to 82KZMG (ITAA 1936); and
 - Part IVA (ITAA 1936).

Note: All legislative references in this Ruling are to the ITAA 1997 unless otherwise indicated.

Goods and Services Tax

3. All fees and expenditure referred to in this Ruling include the Goods and Services Tax (GST) where applicable. In order for an entity (referred to in this Ruling as a Post 30 June Grower or a Grower) to be entitled to claim input tax credits for the GST included in its expenditure, it must be registered or required to be registered for GST and hold a valid tax invoice.

Changes in the Law

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

5. Entities who are considering participating in the Project 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

6. Product Rulings were introduced for the purpose of providing certainty about tax consequences for entities in projects such as this. In keeping with that intention the Tax Office suggests that promoters and advisers ensure that entities are fully informed of any legislative changes after the Ruling is issued.

Class of entities

7. The class of entities to whom this Ruling applies consists of the entities more specifically identified in the Ruling part of this Product Ruling who enter into the scheme specified below on or after the date this Ruling is made. They will have a purpose of staying in the scheme until it is completed (that is, being a party to the relevant agreements until their term expires), and deriving assessable income from this involvement as set out in the description of the scheme. In this Ruling, these persons are referred to as Post 30 June Growers or as Growers.

8. The class of entities to whom this Ruling applies does not include Growers who:

- intend to terminate their involvement in the scheme prior to its completion, or who otherwise do not intend to derive assessable income from it;
- participate in the Project through offers made other than through the Product Disclosure Statement;
- who are accepted to participate in the Project prior to 30 June 2007 or after 30 June 2008; and
- Timbercorp Securities Limited and its associates.

Qualifications

9. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 17 to 68 of this Ruling.

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

- this 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 Ruling may be withdrawn or modified.

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Date of effect

12. This Ruling applies prospectively from 4 October 2006 the date this Ruling is made. However, the Ruling does not apply to entities to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the Gazette; or
- the relevant provisions are not amended.

13. If this Product Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

14. If this Product Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Product Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

15. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Withdrawal

16. This Product Ruling is withdrawn and ceases to have effect after 30 June 2010. The Ruling continues to apply, in respect of the relevant provision(s) ruled upon, to all entities within the specified class which enter into the scheme specified below. Thus, the Ruling continues to apply to those entities, even following its withdrawal, which entered into the specified arrangement prior to withdrawal of the Ruling. This is subject to there being no change in the arrangement or in the persons' involvement in the arrangement.

Scheme

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

- Application for a Product Ruling dated 1 August 2006 as constituted by documents provided on 2 August 2006, 7 August 2006, 15 September 2006, 21 September 2006 and 22 September 2006;
- Draft **Product Disclosure Statement** ('PDS') for the 2007/2008 Timbercorp (Single Payment) Timberlot Project, prepared for Timbercorp Securities Limited ('TSL'), ('the Responsible Entity'), undated, received on 2 August 2006;
- **Constitution of the 2007/2008 Timbercorp (Single Payment) Timberlot Project** between TSL and each Grower, undated, received on 11 September 2006;
- Draft Compliance Plan for the 2007/2008 Timbercorp (Single Payment) Timberlot Project, undated, received on 2 August 2006;
- Draft Custody Agreement between TSL and Trust Company of Australia, received on 2 August 2006;
- Draft **Agreement for Sub-lease (Post 30 June Growers)** between TSL and each Grower, undated, received on 2 August 2006;
- Draft **Deed of Sub-lease- Victoria (Post 30 June Growers)** between TSL and each Grower, undated, received on 2 August 2006;
- Draft **Deed of Sub-lease- South Australia (Post 30 June Growers)** between TSL and each Grower, undated, received on 2 August 2006;
- Draft **Deed of Sub-lease- Western Australia (Post 30 June Growers)** between TSL and each Grower, undated, received on 2 August 2006;

- Draft **Management Agreement (Post 30 June Growers)** between TSL and each Grower, undated, received on 22 September 2006;
- Draft Plantation Services Agreement (Post 30 June Growers) between TSL and Timbercorp Forestry Pty Ltd, undated, received on 2 August 2006;
- Draft Lease and Memorandum of Common Provisions, between TSL and an associate of TSL, undated, received on 11 September 2006 and 22 September 2006; and
- Draft Finance Package, 2007 Timbercorp Projects, containing **Loan Explanation and Loan Terms** received on 2 August 2006 and **Loan Application Form**, updated, received on 11 September 2006.

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

18. The documents highlighted are those that Growers 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 arrangement.

19. 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

20. The main features of the 2007/2008 Timberlot Project for Post 30 June Growers are as follows:

Location	Western Australian, Victoria or South Australia
Type of business to be carried on by each entity	Commercial growing and cultivation of Tasmanian Bluegum (<i>Eucalyptus globulus</i>) trees for the purpose of harvesting and selling timber
Number of hectares offered for cultivation	4,000 hectares (12,000 Timberlots)
Size of each interest	Approx 0.33 hectares in net plantable area
Minimum allocation	Three or less Timberlots at the absolute discretion of Timbercorp.
Minimum subscription	none
Number of trees per hectare	800-1100
Term of the Project	8-12 years
Initial cost	\$3080 per Timberlot
Ongoing costs	From the Net Proceeds defined to mean Proceeds (clause 1.1 Constitution) from the sale of Wood less all Harvesting and Delivery costs: <ul style="list-style-type: none"> • 3.3% for rent; and • 3.3% for Plantation Services.
Other costs	To the extent that they have not been deducted from the purchase price payable for the sale of the Wood, the prescribed proportion of the harvest, delivery and other costs; and Insurance fees where insurance is procured.

21. The Project is registered as a Managed Investment Scheme within the terms of the *Corporations Act 2001*. Applications to participate in the Project must be made on the Application form shown in the PDS. There is no minimum amount that must be raised under the PDS. A Custodian will be appointed under the Custody Agreement to protect the interests of the Post 30 June Growers in their dealings with TSL.

22. Under a Power of Attorney contained in the Application Form, Applicants that are accepted to participate in the Project will enter into agreements with TSL and its associates to establish, manage and Harvest *Eucalyptus globulus* (Tasmanian Bluegum) for the purpose of sale as woodchips for paper production.

23. Growers' Applications accepted after 30 June 2007 and on or before 30 June 2008 will commence participation as Post 30 June Growers. This Ruling only applies in respect of Post 30 June Growers. **Note that a separate Product Ruling has been issued for Growers who enter into the Project on or before 30 June 2007.**

24. A Grower will Sub-lease at least three identifiable allotments of land, called Timberlots in Victoria, South Australia or in Western Australia. Each allotment of land will be approximately 1/3 of a hectare each and will be leased from TSL. The Sub-lease is for a term expiring on the earlier of 30 June 2021 or the completion of Harvesting. TSL will manage the Project and will be responsible for planting, cultivating, and Harvesting the Trees and marketing the Wood on the Grower's behalf.

25. Suitable land for use in the Project is required to meet the following specifications. It must:

- be cleared agricultural land that has been pastured in accordance with Forestry Stewardship Council principles or previously used for plantation forestry;
- be within 150 km of either Bunbury or Albany, Western Australia or 200km from Portland, Victoria; and
- receive more than 600 mm average annual rainfall or have access to underground water.

Constitution

26. The Constitution is entered into by TSL and each Grower and sets out the terms upon which TSL, as Responsible Entity, will manage the Project.

27. The Grower irrevocably appoints TSL as their agent, representative and attorney to relation to the Project (clause 3).

28. TSL must hold all Application Moneys and any income earned on it as a bare trustee for the Grower (clause 4).

29. The Constitution also sets out provisions relating to:

- the application procedure for Timberlots and the acceptance or refusal of such applications by TSL at its discretion (clauses 5, 6 and 7);
- the preparation and entry into the:
 - a) Agreement for Sub-lease;
 - b) Sub-lease;
 - c) Management Agreement;
 - d) Wood Purchase Agreement; and
 - e) Carbon Agreement (clauses 8 and 9);

- the issue of Timberlot Statements to Growers within 2 months of the allotment of Timberlots and the setting up and maintenance of a Register of Growers (clause 10);
- TSL's powers and covenants (clause 11);
- keeping or causing to be kept a separate Agency Account for the purpose of depositing the Proceeds and any other money that TSL may hold for the Grower, other than Application Moneys and interest on Application Moneys (clause 12);
- the right of TSL to be remunerated for the services it provides (clause 13) and or any extraordinary expenses that arise (clause 16);
- the status and retention of Management Agreements, Sub-leases and Agreements for Sub-leases and the consequences of default and termination of those agreements (clause 16A);
- each Grower's right to inspect documents and to express opinions (clause 17);
- restrictions on the assignment and transmission by a Grower of their Timberlots (clause 19);
- meetings of Growers (clause 20);
- the liabilities and indemnities of TSL and Growers (clauses 21 and 22);
- the pooling of the Wood and Proceeds and distributions of the Proceeds to each Grower (clauses 22A and 23); and
- the termination of the Project (clause 25).

30. Although Clause 5.4 of the Constitution provides that Growers may pay the Application Moneys by instalments, **this Product Ruling does not apply to any Grower who enters into an arrangement to pay their Application Moneys by instalments.**

Compliance Plan

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

Lease and Memorandum of Common Provisions

32. Generally, land for the Project will be owned by a Timbercorp Limited subsidiary established to hold land for use in Timbercorp projects. The relevant Timbercorp Limited subsidiary and TSL will enter into a Lease and Memorandum of Common Provisions which will set out the terms and conditions under which it leases this land to TSL. Subject to land availability, TSL may also enter into leases with external land owners on arms length commercial terms.

Agreement for Sub-lease and Sub-lease

33. Either at the time their application is accepted or, when sufficient suitable land is available, each Grower will enter into a Sub-lease with TSL. To be suitable for allocation to a Grower under a Sub-lease the relevant land must meet the land selection criteria described in the Independent Forester's Report reproduced in the Product Disclosure Statement.

34. Where, at the time of accepting an application from a Grower, there is no suitable land available for allotment, a Grower will enter into an Agreement for Sub-lease with TSL.

35. An Agreement for Sub-lease will be entered where TSL believes it will be able to secure suitable plantation land and enter into the necessary project agreements in sufficient time to perform the Establishment Services and Planting Services and within the relevant Initial 12 month Establishment Period from the commencement of the first seasonally dependent agronomic activity.

36. Subsequently, when suitable land is secured, TSL will arrange entry into a Sub-lease on behalf of the Grower.

37. There are separate Sub-leases depending upon whether the land subject to the Sub-lease is located in Victoria, South Australia or Western Australia.

38. TSL grants a Sub-lease of a Timberlot or Timberlots to the Grower for the purpose of growing, tending and harvesting a plantation or plantations of eucalyptus trees (clause 3).

39. Each Sub-lease is conditional upon the obtaining of all local, State and Commonwealth government approvals, licences or permissions required for the establishment of the Trees within twelve months after the date of execution of the Sub-lease (clause 4.1) and conditional upon TSL entering into a Head Lease on or before the Commencement Date (clause 4.2.)

40. Among other obligations set out in the Sub-lease the Grower undertakes to use the relevant Timberlots solely for the purpose of growing, tending and harvesting a plantation or plantations of eucalyptus trees (clause 6).

41. TSL and the Grower agree that the Trees on the respective Timberlots are and will remain the property of the Grower during the Term of the Sub-lease (clauses 8.3 and 13.1). TSL grants each Grower an independent and severable grant of a proprietary interest in the relevant Timberlots (clause 13.3).

42. The Sub-lease also sets out:

- the Term of the Sub-lease (Part 3 of the Schedule) and circumstances under which it may be extended (clause 10.1);
- the Rent payable by the Growers (clause 5 and Part 4 of the Schedule);
- the obligations and rights of the Growers (clauses 6 and 8);
- the obligations and rights of TSL (clauses 7 and 9); and
- the early termination and reduction of the relevant Timberlots (clause 11).

Management Agreement

43. Each Grower will enter into a Management Agreement with TSL whereby the Grower appoints TSL as their project manager to carry out or cause to be carried out such services and duties as are set out in the Management Agreement and which are usual or necessary for carrying on the business of plantation forestry.

44. The Management Agreement becomes operative immediately upon acceptance of an application made by a Grower.

45. Each Grower will engage TSL as an independent contractor to carry out the Establishment Services and the Plantation Services and, as an agent, to Harvest and sell the Wood on behalf of the relevant Grower (clause 3).

46. The Establishment Services are seasonally dependent agronomic services, including the Planting Services, which will be carried out in within the Establishment Period. The Establishment Period commences on the day when the first seasonally dependent agronomic activity commences and ends on the earlier of 12 months thereafter or 30 June 2009.

47. The Establishment Services will be carried out in accordance with the Management Plan and includes the preparation of the Timberlots for planting, the procurement of the seedlings, and the planting of the seedlings on the relevant Timberlots (clause 6).

48. The Plantation Services are to be carried out following the completion of the Establishment Services. The Plantation Services consist of general management and maintenance services during the Term of the Project (clause 7).

49. TSL undertakes to market and sell, as agent for the Grower, the Wood grown or growing, processed or unprocessed on the relevant Timberlots to any bona fide purchaser for as high a price as it can reasonably achieve for the Wood (clause 7).

50. Unless otherwise agreed between TSL and the Growers the Harvest of the Trees and the Delivery of the Wood to a purchaser is required to take place between 30 September 2017 and 30 September 2021 (clause 8 and Part 2 of the Schedule).

51. TSL is required to advise Growers of the dates between which Harvesting will take place, the proposed Purchase Price of the Wood and provide Growers with a fixed quote for the Harvesting and Delivery of the Wood to the designated Facility or Facilities (clause 8).

52. The Management Agreement also identifies:

- the duties and rights of Timbercorp Securities (clause 9);
- the rights of each Grower (clause 11);
- certain mutual covenants (clause 10); and
- the rights of termination in the event of default (clause 14).

Pooling of amounts and distribution of Proceeds

53. The Constitution provides that TSL must pool and keep separate the Wood and Proceeds of Post 30 June Growers (clause 22A).

54. A Grower is entitled to a proportion of the aggregate of the Purchase Price payable to all Post 30 June Growers for all the Wood sold pursuant to the Management Agreement as represented by the Grower's own Timberlots to the total number of all Timberlots leased to all Post 30 June Growers (clause 7).

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

- only Growers who have contributed Wood to the sales pool are entitled to benefit from distributions of the Proceeds of sale from the pooled Wood; and
- any pooled Wood must consist only of Wood contributed by Post 30 June Growers in the Project.

Fees

56. A Grower is liable to pay TSL the following fees per Timberlot under the terms of the Management Agreement (Part 1 of the Schedule) and the Sub-lease (Part 4 of the Schedule):

- \$3,080 for Establishment Services payable on or before the Commencement Date;

- 3.3% of the Net Proceeds for Plantation Services provided during the Term of the Project;
- 3.3% of the Net Proceeds for Rent for the Sub-lease of the Grower's Timberlots during the Term of the Project; and
- to the extent that such costs have not been deducted from the Purchase Price payable under any agreement for the sale of Wood, the Prescribed Portion of the Harvesting, Delivery and other costs.

Plantation Services Agreement

57. TSL engages Timbercorp Forestry Pty Ltd as an independent contractor to carry out the Establishment Services (set out in clause 6) and Plantation Services (set out in clause 6A) during the Term of the Project in accordance with the Establishment and Maintenance Plan (clause 3).

Custody Agreement

58. Timbercorp will engage the Trust Company of Australia Limited to act as the custodian for the Project. The custodian will be responsible for holding the Scheme Assets on the terms and conditions set out in the Agreement. Scheme Assets are defined as the Subscription Moneys, until they are expended, and the Proceeds, until they are distributed, in accordance with the Constitution.

Finance

59. Growers can fund their participation in the Project themselves, borrow from Timbercorp Finance Pty Ltd (a lender associated with the Responsible Entity), or borrow from an independent lender external to the Project.

60. Loans will be provided to Growers by Timbercorp Finance Pty Ltd under the following finance arrangements.

61. Two loan options are available to Growers.

62. Type A loans offered are principal and interest reducing loans for periods of between 3 and 8 years. The loan will be repayable by equal monthly instalments of principal and interest over the period of the loan. A Grower may borrow up to 90% of the GST inclusive value of the initial Application Moneys.

63. Type B loans offered are interest free loans payable within 12 months. The loan will be repayable by 12 equal monthly instalments of principal.

64. Both loans offered are full recourse and there are no circumstances in which a Grower will not be required to repay the borrowed moneys to the lender within the period set out in the loan agreement.

65. Common features contained in both Type A loans and Type B loans are that:

- on application the Grower will be required to pay the deposit, being the balance still to be paid for their Timberlots after deduction of the Loan Amount;
- the Grower is entitled to repay the whole or any part of the Total Amount Owed without penalty for early repayment;
- in the event that any amount is overdue, Timbercorp Finance Pty Ltd may charge interest at the Higher Interest Rate;
- during the Loan Term the Grower will assign and transfer over to Timbercorp Finance Pty Ltd by way of fixed charge all its rights, title and interest at any time in the Project including Timberlots and the Project Agreements;
- during the Loan Term the Grower must maintain fire, wind and storm insurance over the Timberlots on a full replacement basis; and
- an application and administration fee of \$250 is payable plus stamp duty if any, on the Loan Amount.

66. The terms specific to each optional Loan Term offered by Timbercorp Finance Pty Ltd are summarised below (interest rates quoted are indicative)

Type A – Loans with equal monthly instalments

- 3 year term with an interest rate of 9.0% per annum;
- 4 year term with an interest rate of 9.95% per annum; and
- 5 to 8 year term with an interest rate of 10.50% per annum;

Type B – Loans with an Interest Free Period

- 1 year term with an interest rate of 0% per annum; and
- the principal to be repaid by 12 equal calendar monthly instalments.

67. Growers cannot rely on this Product Ruling if a different finance arrangement is entered into with Timbercorp Finance Pty Ltd or if the full amount of application monies, including all loan monies, are not provided to TSL by the Grower or by Timbercorp Finance Pty Ltd on the Grower's behalf by 30 June 2008. Where an application is accepted subject to finance approval by any lending institution other than Timbercorp Finance Pty Ltd, Growers cannot rely on this Ruling if written evidence of that approval has not been given to the Responsible Entity by 30 June 2008.

68. 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 or the funding arrangements transform the Project into a 'scheme' to which Part IVA 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 Timbercorp Finance Pty Ltd, are involved or become involved in the provision of finance to Growers for the Project.

Ruling

Application of this Ruling

69. Subject to paragraph 8, this Ruling applies only to Growers who are accepted to participate in the Project after 30 June 2007 and on or before 30 June 2008. They must have executed a Management Agreement and an Agreement for Sub-lease or a Sub-lease on or before that date and their Timberlots must be established within the Establishment Period (see paragraph 46 of this Ruling).

70. The Grower's participation in the Project must constitute the carrying on of a business of primary production.

71. 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.

The Simplified Tax System (STS)

Division 328

72. To be an 'STS taxpayer' a Grower must be eligible to be an 'STS taxpayer' and must have elected to be an 'STS taxpayer' (Division 328 of the ITAA 1997). For a Grower participating in the Project, the recognition of income and the timing of tax deductions is different depending on whether the Grower who was an 'STS taxpayer' prior to 1 July 2005 continues to use the cash accounting method (called the 'STS accounting method') – see sections 328-120 and 328-125 of the *Income Tax (Transitional Provisions) Act 1997*.

73. For such Growers, a reference in this Ruling to an amount being deductible when 'incurred' will mean that amount is deductible when paid and a reference to an amount being included in assessable income when 'derived' will mean that amount is included in assessable income when received.

25% entrepreneurs tax offset

Subdivision 61-J

74. For the first income year starting on or after 1 July 2005, Subdivision 61-J provides for a tax offset of 25% of income tax liability related to the business income of a business in the STS with annual group turnover of less than \$75,000. Entitlement to the offset varies depending on the type of entity and is therefore outside the scope of this Ruling.

Assessable income

Section 6-5

75. 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 in the income year in which that income is derived.

Deductions for fees for Establishment Services, borrowing costs and Interest**Section 8-1 and section 25-25**

76. A Grower may claim, on a per Timberlot basis, tax deductions under section 8-1 of the ITAA 1997, for the expenses set out in the Table below.

Fee Type	Year ended 30 June 2008	Year ended 30 June 2009	Year ended 30 June 2010
Establishment Services	\$3,080 See Notes (i) & (ii) below		
Interest paid to Timbercorp Finance Pty Ltd	As incurred See Note (iii)	As incurred See Note (iii)	As incurred See Note (iii)
Borrowing costs for loans with Timbercorp Finance Pty Ltd	Must be calculated- See Note (iv)	Must be calculated- See Note (iv)	Must be calculated- See Note (iv)

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: Division 27.
- (ii) Under section 82KZMG of the ITAA 1936 the fee for Establishment Services is expenditure for 'seasonally dependent agronomic activities' (see paragraphs 105 to 109 of this Ruling) and is deductible in the income year in which it is incurred.
- (iii) The deductibility of interest arising from agreements entered into with financiers other than Timbercorp Finance Pty Ltd is outside the scope of this Ruling. However, all Growers in the Project should read carefully the discussion of the prepayment rules in paragraphs 100 to 101 of this Ruling as those rules may be applicable if interest is prepaid.

- (iv) The Loan Application Fee payable to Timbercorp Finance Pty Ltd is a borrowing expense and is deductible under section 25-25. It is incurred for borrowing moneys that are used or are to be used during that income year solely for income producing purposes. The deduction is spread over the period of the loan or 5 years, whichever is the shorter. The deductibility or otherwise of borrowing costs arising from loan agreements entered into with financiers other than Timbercorp Finance Pty Ltd is outside the scope of this Ruling.

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

Section 35-55 – exercise of Commissioner's discretion

77. A Post 30 June Grower who is an individual accepted into the Project by 30 June 2008 may have losses arising from their participation in the Project that would be deferred to a later income year under section 35-10. Subject to the Project being carried out in the manner described above, the Commissioner will exercise the discretion in paragraph 35-55(1)(b) for each Grower for the income years ending **30 June 2008 to 30 June 2021** or the income year preceding the Harvest (whichever occurs sooner). This conditional exercise of the discretion will allow those losses to be offset against the Grower's other assessable income in the income year in which the losses arise.

Sections 82KZME to 82KZMF, 82KL and Part IVA of the ITAA 1936

78. For a Grower who participates in the Project and incurs expenditure as required by the Management Agreement and, where relevant, a loan with Timbercorp Finance Pty Ltd, the following provisions of the ITAA 1936 have application as indicated:

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

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?

79. For the amounts set out in the Table above to constitute allowable deductions the Grower's afforestation activities as a participant in the Project must amount to the carrying on of a business of primary production.

80. Where there is a business, or a future business, the gross proceeds from the sale of the Wood will constitute gross assessable income in their own right. The generation of 'business income' from such a business, or future business, provides the backdrop against which to judge whether the outgoings in question have the requisite connection with the operations that more directly gain or produce this income.

81. For schemes such as this, Taxation Ruling TR 2000/8 sets out in paragraph 89 the circumstances in which the Grower's activities can constitute the carrying on of a business. As TR 2000/8 sets out, these circumstances have been established in court decisions such as *Commissioner of Taxation v. Lau* (1984) 6 FCR 202; 84 ATC 4929; (1984) 16 ATR 55.

82. Generally, a Grower will be carrying on a business of afforestation, and hence primary production, if:

- the Grower has an identifiable interest (by lease) or rights over (by licence) the land on which the Grower's trees are established;
- the Grower has a right to harvest and sell the Wood produced from those trees;
- the afforestation activities are carried out on the Grower's behalf;
- the afforestation activities of the Grower are typical of those associated with a afforestation business; and
- the weight and influence of general indicators point to the carrying on of a business.

83. In this Project, each Grower enters into a Management Agreement and a Sub-lease.

84. Under the Sub-lease, each individual Grower will have rights over one or more specific and identifiable areas of land, each known as a Timberlot. The Sub-lease provides the Grower with an ongoing interest in the specific trees on the sub-leased area for the term of the Project. Under the Sub-lease, the Grower must use the land in question for the purpose of carrying out afforestation activities, and for no other purpose. The Sub-lease allows TSL and the Timbercorp Forestry Pty Ltd to come onto the land to carry out their obligations under the Management Agreement and the Plantation Services Agreement.

85. Under the Management Agreement, TSL is engaged by the Grower to provide Establishment Services and Plantation Services on the Grower's identifiable area of land during the term of the Project. Under the Plantation Services Agreement, TSL subcontracts the Establishment Services and the Plantation Services to Timbercorp Forestry Pty Ltd which has provided evidence that it holds the appropriate professional skills and credentials to provide the management services to establish and maintain the Timberlot on the Grower's behalf during the Term of the Project.

86. TSL is also engaged to harvest and sell, on the Grower's behalf, the Wood grown on the Grower's Timberlots.

87. The general indicators of a business, as used by the Courts, are described in Taxation Ruling TR 97/11. Positive findings can be made from the Project's description for all the indicators.

88. The activities that will be regularly carried out during the term of the Project demonstrate a significant commercial purpose. Based on reasonable projections, a Grower in the Project will derive assessable income from the sale of the Wood that will return a before-tax profit, i.e. a profit in cash terms that does not depend in its calculation on the fees in question being allowed as a deduction.

89. The pooling of the Wood from the Trees grown on the Grower's Timberlot with the Wood of other Growers in the Project is consistent with general afforestation practices. Each Grower's proportionate share of the sale proceeds of the pooled Wood will reflect the proportion of the Growers Timberlot to the entire number of Timberlots contributing to the pool.

90. Services to be provided by Timbercorp Forestry Pty Ltd are also consistent with general silvicultural practices. They are of the type ordinarily found in afforestation ventures that would commonly be said to be businesses. While the size of a Timberlot is relatively small, it is of a size and scale to allow it to be commercially viable.

91. The Grower's degree of control over the TSL as evidenced by the Constitution and Management Agreement, and supplemented by the *Corporations Act 2001*, is sufficient. During the term of the Project, the TSL is required to provide the Grower with regular progress reports on the Grower's Timberlot and the activities carried out on the Grower's behalf. Growers are able to terminate arrangements with TSL in certain instances, such as cases of default or neglect.

92. The afforestation activities, and hence the fees associated with their procurement, are consistent with an intention to commence regular activities that have an 'air of permanence' about them. For the purposes of this Ruling, the Growers' afforestation activities in the 2007/2008 Timbercorp (Single Payment) Timberlot Project – Post 30 June Growers will constitute the carrying on of a business.

The Simplified Tax System

Division 328

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

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

Deductibility of fees for Establishment Services

Section 8-1

95. Consideration of whether the fees for Establishment Services are deductible under section 8-1 begins with the first limb of the section. This view proceeds on the following basis:

- the outgoing in question must have a sufficient connection with the operations or activities that directly gain or produce the taxpayer's assessable income;
- the outgoings are not deductible under the second limb if they are incurred when the business has not commenced; and
- where all that happens in a year of income is that a taxpayer is contractually committed to a venture that may not turn out to be a business, there can be doubt about whether the relevant business has commenced, and hence, whether the second limb applies. However, that does not preclude the application of the first limb in determining whether the outgoing in question has a sufficient connection with activities to produce assessable income.

96. The fees for Establishment Services associated with the afforestation activities will relate to the gaining of income from the Grower's business of afforestation (see paragraph 92 of this Ruling), and hence have a sufficient connection to the operations by which income (from the Harvesting and sale of the Wood) is to be gained from this business. They will thus be deductible under the first limb of section 8-1. Further, a 'non-income producing' purpose in incurring the fee is not identifiable under the scheme. The fee appears to be reasonable. There is no capital component of the fee. The tests of deductibility under the first limb of section 8-1 are met. The exclusions do not apply.

Interest deductibility

Section 8-1

(i) Growers who use Timbercorp Finance Pty Ltd as the finance provider

97. Some Growers may finance their participation in the Project through a loan facility with Timbercorp Finance Pty Ltd. Whether the resulting interest costs are deductible under section 8-1 depends on the same reasoning as that applied to the deductibility of fees for Establishment Services under the Management Agreement.

98. The interest incurred will be in respect of a loan to finance the Grower's business operations - the cultivation and growing of trees that will continue to be directly connected with the gaining of 'business income' from the Project. Such interest will, therefore, have a sufficient connection with the gaining of assessable income to be deductible under section 8-1. In the absence of any application of the prepayment provisions (see paragraph 103 of this Ruling) interest is deductible in the income year in which it is incurred.

(ii) Growers who DO NOT use Timbercorp Finance Pty Ltd as the finance provider

99. The deductibility of interest incurred by Growers who finance their participation in the Project through a loan facility with a bank or financier other than Timbercorp Finance Pty Ltd is outside the scope of this Ruling. Product Rulings only deal with arrangements where all details and documentation have been provided to, and examined by the Tax Office.

Prepayment provisions***Sections 82KZL to 82KZMG of the ITAA 1936***

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

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

Application of the prepayment provisions to this Project***Sections 82KZME and 82KZMF of the ITAA 1936***

102. Other than the Establishment Fee (see below) the Rent and the Plantation Services Fees payable under scheme to which this Product Ruling applies are only payable as a percentage of the Net Proceeds from Harvest, or from insurance proceeds, and the interest payable to Timbercorp Finance Pty Ltd is incurred monthly in arrears. Accordingly, the prepayment provisions in sections 82KZME and 82KZMF of the ITAA 1936 have no application to expenditure incurred by Growers under this scheme.

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

104. As noted in the Ruling section above, Growers who prepay interest are not covered by this Product Ruling and may instead request a private ruling on the tax consequences of their participation in this Project.

Section 82KZMG of the ITAA 1936

105. Expenditure that meets the requirements of section 82KZMG of the ITAA 1936 is excluded from the application of the prepayment rules in sections 82KZME and 82KZMF of the ITAA 1936 that would otherwise apply.

106. Section 82KZMG provides a '12 month rule' that, in effect, facilitates an immediate deduction for certain prepaid expenditure incurred under a plantation forestry managed agreement. The '12 month rule' applies to expenditure for 'seasonally dependent agronomic activities' that will be carried out during the establishment period of a particular planting of trees.

107. Seasonally dependent agronomic activities are explained in Taxation Determination TD 2003/12. Whilst the establishment period itself may exceed 12 months, each seasonally dependent agronomic activity must be completed within 12 months of commencement of its eligible service period (as defined in subsection 82KZL(1) of the ITAA 1936), and by the end of the following income year.

108. Under the Management Agreement on the Commencement Date each Grower incurs a fee for Establishment Services of \$3,080 per Woodlot for 'seasonally dependent agronomic activities' that will be carried out during the Establishment Period.

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

Division 35 – deferral of losses from non-commercial business activities**Section 35-55 – exercise of Commissioner's discretion**

110. In deciding to exercise the discretion in paragraph 35-55(1)(b) on a conditional basis from the income year ending **30 June 2008 to the sooner of the income year ended 30 June 2021 or the income year preceding the Harvest** the Commissioner has applied the principles set out in Taxation Ruling TR 2001/14 Income tax: Division 35 – non-commercial business losses. Accordingly, based on the evidence supplied, the Commissioner has determined that for those income years ended 30 June 2008 up to and including 30 June 2021 of the income year preceding the Harvest whichever occurs sooner:

- it is because of its nature the business activity of a Grower will not satisfy one of the four tests in Division 35; and
- there is an objective expectation that within a period that is commercially viable for the afforestation industry, a Grower's business activity will satisfy one of the four tests set out in Division 35 or produce a taxation profit.

111. Therefore, 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.

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

Section 82KL of the ITAA 1936 – recouped expenditure

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

Part IVA of the ITAA 1936 – general tax avoidance provisions

114. 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).

115. The 2007/2008 Timbercorp (Single Payment) Timberlot Project – Post 30 June Growers 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 76 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.

116. 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 Wood. 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) 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

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TD 2003/12; TR 97/11;
TR 98/22; TR 2000/8;
TR 2001/14; TR 2002/6;
TR 2002/11

Subject references:

- advance deductions and expenses for certain forestry expenditure
- carrying on a business
- commencement of a business
- establishment fees
- fee expenses
- forestry agreement
- interest expenses
- management fees
- non-commercial losses
- producing assessable income
- product rulings
- public rulings
- seasonally dependent agronomic activity
- taxation administration
- tax avoidance
- tax benefits under tax avoidance schemes
- tax shelters
- tax shelters project

Legislative references:

- ITAA 1936 82KL
- ITAA 1936 Pt III Div 3 Subdiv H
- ITAA 1936 82KZL

- ITAA 1936 82KZL(1)
- ITAA 1936 82KZM
- ITAA 1936 82KZME
- ITAA 1936 82KZMF
- ITAA 1936 82KZMG
- ITAA 1936 Pt IVA
- ITAA 1936 177A
- ITAA 1936 177C
- ITAA 1936 177D
- ITAA 1936 177D(b)
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- ITAA 1997 8-1
- ITAA 1997 17-5
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- ITAA 1997 35-10(2)
- ITAA 1997 35-55
- ITAA 1997 35-55(1)(b)
- ITAA 1997 Subdiv 61-J
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- ITAA 1997 Subdiv 328-F
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Case references:

- Commissioner of Taxation v Lau (1984) 6 FCR 202; 84 ATC 4929; (1984)16 ATR 55

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