PR 2007/32W - Income tax: Barossa Vines Project 2007 - Applicant Group 1

Notice of Withdrawal

Product Ruling

Income tax: Barossa Vines Project 2007 – Applicant Group 1

Product Ruling PR 2007/32 is withdrawn with effect from today.

1. Product Ruling PR 2007/32 sets out the Commissioner's opinion on the tax consequences for a defined class of entities participating in the Barossa Vines Project 2007 – Applicant Group 1 (the Project), a viticultural managed investment scheme with the purpose of establishing and maintaining a vineyard and producing wine grapes for sale.

2. This Product Ruling has been withdrawn in accordance with subsection 358-20(1) of Schedule 1 to the *Taxation Administration Act 1953,* which states the Commissioner may withdraw a public ruling either wholly or to an extent. Where the scheme described in the ruling is materially different from the scheme actually carried out, the ruling does not have any binding effect on the Commissioner, as the scheme entered into is not the scheme ruled upon.

3. All legislative references in this withdrawal notice are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated.

Overview

4. The Commissioner of Taxation issued Product Ruling PR 2007/32 for the Barossa Vines Project 2007 – Applicant Group 1 on 11 April 2007.

5. On 12 February 2012, The Commissioner of Taxation issued a Notice of Partial Withdrawal of PR 2007/32 due to a material difference in the implementation of the scheme. The material difference was that the Responsible Entity failed to complete or carry out services to the extent required which resulted in a significant delay in the establishment of the vineyard and consequently the production of assessable income. The partial withdrawal was for the income years ending 30 June 2008, 30 June 2009 and 30 June 2010. The Product Ruling continued to apply for the income year ending 30 June 2007.

Cessation of business

6. On 25 October 2011, Barossa Vines Ltd surrendered the leases over the land on which the Growers vineyard businesses had been established. As a result, Growers are no longer carrying on a business from this activity, there is a material difference in the arrangement.

PR 2007/32 is now fully withdrawn.

Deferral of losses from non-commercial business activities

7. Under the Notice of Partial Withdrawal, referred to in paragraph 5 above, the Commissioner was not satisfied that the conditions had been met to exercise his discretion under paragraph 35-55(1)(b) for the income years ending 30 June 2008, 30 June 2009 and 30 June 2010. The Commissioner has not exercised his discretion under paragraphs 35-55(1)(b) or 35-55(1)(c) for the income years ending 30 June 2011 or later income years. Growers relying on the discretion are not entitled to immediate deductions for the income year ending 30 June 2008 and later income years and losses from the Project in these years must be deferred under subsection 35-10(2), subject to paragraph 8 and 9 below.

8. The losses from the individual's business activity will not have to be deferred:

- under paragraph 35-10(2) for the income years ending 30 June 2008 and later income years if the individual meets at least one of the four business activity tests in Division 35 that apply to the business activity, and
- for the income year ending 30 June 2010 and later income years, if the individual meets the income requirement test in subsection 35-10(2E) or comes within the exception in subsection 35-10(4).

9. Amounts deferred under subsection 35-10(2) for the income years ending 30 June 2008 and later income years will only be deductible in a subsequent year if the business activity that gave rise to this amount, or one 'of a similar kind', is carried on in that subsequent year. For more information regarding 'Business activities of a similar kind' see paragraphs 49 to 54 of Taxation Ruling TR 2001/14 *Income Tax: Division 35 non-commercial business losses*.

10. If the activity, or one 'of a similar kind', is never carried on again, the entitlement to deduct the amount will be lost.

11. Deductions deferred under the non-commercial business activities provisions do not form part of the cost base of any asset associated with the business. They are not taken into account when calculating any capital gain or loss on the cessation of the business.

Costs after business activity ceases

12. Amounts incurred after the business activity ceased on 25 October 2011, for example, interest (refer paragraph 14 below), may still be deductible if incurred after 25 October 2011 as such deductions are not subject to Division 35 after the business activity has ceased.

Deductions for Management Fees, Vineyard Operating Costs and Licence Fees

13. The Table and Notes at paragraph 25 of PR 2007/32 set out the fees and expenses on a per Vineyard Lot basis for the income years ending 30 June 2007 to 30 June 2009. As outlined in paragraph 7 above, Growers relying on the non-commercial loss discretion are not entitled to immediate deductions for the income years ending 30 June 2008 and later income years and losses from the Project in these years must be deferred under subsection 35-10(2), subject to the exceptions in paragraphs 8 and 9 above.

Interest on loans with the Preferred Financier

14. Growers funding their participation in the Project with the Preferred Financier, as specified in paragraphs 93 to 98 of PR 2007/32, may incur interest expenses. As outlined in paragraph 7 above, Growers relying on the non-commercial loss discretion are not entitled to immediate deductions for interest expenses incurred prior to 25 October 2011 (the date the business ceased). Interest expenses from the Project incurred during this period must be deferred under subsection 35-10(2), subject to the exceptions in paragraphs 8 and 9 above. Interest expenditure incurred after the business ceased on 25 October 2011 will be deductible under section 8-1 provided Growers meet certain requirements outlined in Taxation Ruling TR 2004/4 *Income tax: deductions for interest incurred prior to the commencement of, or following the cessation of, relevant income earning activities.*

Deductions for capital expenditure on Trellising, Irrigation and Establishment of Grapevines

15. The Table and Notes at paragraph 26 of PR 2007/32 set out the deductions a Grower may claim for capital expenses on a per Vineyard Lot basis for the income years ending 30 June 2007 to 30 June 2009. PR 2007/32 referred to tax consequences for ‘STS taxpayers’ under Division 328. The term ‘STS taxpayer’ was replaced with ‘small business entity’ from the income year ending 30 June 2008.

16. As outlined in paragraph 7, Growers relying on the non-commercial loss discretion are not entitled to offset any loss as a result of capital expenses for the income years ending 30 June 2008 and later income years and losses from the Project in these years must be deferred under subsection 35-10(2), subject to the exceptions in paragraphs 8 and 9 of this ruling.

17. Growers ceased to hold an interest in the trellising, irrigation and grapevines when the leases were surrendered on 25 October 2011. The tax consequences for Growers on surrender of the leases will vary depending on the number of Vineyard Lots acquired and whether the Grower is a ‘small business entity’. Growers should refer to the Table and Notes at paragraph 26 of PR 2007/32 to determine how they originally claimed a tax deduction for the capital expense.

Trellising

18. Growers incurred capital expenditure of $358 per Vineyard Lot which is attributable to the installation of trellising. The trellising is a ‘depreciating asset’. Growers stopped holding the depreciating asset when the Project leases were surrendered.

19. Growers who are a ‘small business entity’ will need to calculate their balancing adjustment where the trellising was allocated to a ‘general small business pool’ (section 328-215). A balancing adjustment event occurs when you stop using a depreciating asset for any purpose or you dispose of, sell, lose or destroy the asset.

20. Growers who are not a ‘small business entity’ calculated the decline in the value of the asset using the formula in either subsection 40-70(1) or subsection 70-75(1) and will need to calculate a balancing adjustment on disposal of the asset pursuant to section 40-285. Non-small business entities who allocated the trellising to a low value pool will need to calculate a balancing adjustment to the closing pool balance pursuant to section 40-445.

21. A capital gain or capital loss made from a CGT event (that is also a balancing adjustment event) that happens to a depreciating asset is disregarded for CGT purposes (subsection 118-24(1)) if the asset was an asset held, by an individual, or if a partner, an asset of the partnership, where the decline in value of the asset was worked out under Division 40 (the decline in value of a depreciating asset) or the deduction for the asset was calculated under Division 328 (the depreciating asset).

Irrigation

22. Growers incurred capital expenditure of $302 per Vineyard Lot which is attributable to the installation of irrigation. Growers stopped holding the asset when the Project leases were surrendered. Growers should refer to the Table and Notes at paragraph 26 of PR 2007/32 to determine how they originally claimed a tax deduction for the capital expense.

23. For small business entities if the asset was not treated as a 'low cost asset' a balancing adjustment event occurs when an individual stops using a depreciating asset for any purpose or where an individual disposes of, sells, loses, or destroys the asset. Small Business Entity Growers who allocated the irrigation system to a general STS pool will need to calculate their balancing adjustment pursuant to section 328-215.

24. A capital gain or capital loss made from a CGT event (that is also a balancing adjustment event) that happens to a depreciating asset is disregarded for CGT purposes (subsection 118-24(1)) if the asset was an asset held, by an individual or if a partner, an asset of the partnership where the deduction for the asset (the depreciating asset) was calculated under Division 328. A capital gain or loss from the disposal of the irrigation system is not disregarded from the application of CGT rules if it relates to a depreciating asset for which the taxpayer or another entity has deducted or can deduct under Subdivision 40-F (subsection 118-24(2)). Growers who claimed a deduction for the irrigation under Subdivision 40-F will need to determine whether they have a capital loss or capital gain from the disposal of the asset.

Grapevines

25. Growers incurred capital expenditure of $121 per Vineyard Lot which is attributable to the establishment of the grapevines. Growers were originally entitled to claim a deduction for the decline in value of the grapevines from the time the grapevines entered their first commercial season (section 40-530, item 2). However, the grapevines did not enter into their first commercial season before the Project leases were surrendered and therefore, there is no entitlement for Growers to claim a deduction for the decline in value of the grapevines. Growers are not entitled to claim a deduction under section 40-880 for capital expenditure attributable to the establishment of the grapevines.

26. A horticultural plant is a CGT asset (section 104-5). Growers disposed of the CGT asset when the leases over the land were surrendered (subsection 104-10(2)). Growers will need to calculate whether they had made a capital gain or capital loss from the disposal of the horticultural plant.

Shares

27. Shares in Barossa Vines Landholding Ltd are CGT assets (section 108-5). An amount paid by a Grower to acquire the shares is an outgoing of capital and not allowable as a deduction. The amounts paid for each share will represent the first element of the cost base of the share (subsection 110-25(2)). Any disposal of the shares by a Grower will be a CGT event and may give rise to a capital gain or loss.

Commissioner of Taxation

2 April 2014

ATO references

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