Ellerston Asia Growth Fund (Hedge Fund)

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4 April 2024

Dear investor,

Update: application to Commissioner of Taxation for a class ruling in relation to the income tax implications of Ellerston Asian Investments Ltd (EAI) restructure.

As previously outlined in the Shareholder Booklet circulated by EAI to shareholders seeking approval for the restructure, EAI's taxation advisers, Ernst & Young (EY), prepared an application to the Commissioner of Taxation for a class ruling in relation to the income tax implications of the transaction.

Since that date, EY have been engaged in ongoing discussions with the Australian Taxation Office (ATO) in relation to the proposed class ruling. The taxation opinion expressed by EY as per Section 2.9 of the Shareholder Booklet, is that Shareholders who received the Special Dividend, should be required to include the amount of the dividend in their assessable income (details of EY's opinion are contained in Appendix B on pg. 7). EY maintains that this is the correct taxation treatment as per its opinion.

However, the ATO has indicated that there are different income tax implications of the transaction contrary to the position summarised in Section 2.9 of the Shareholder Booklet. An opinion was obtained from Mr Michael O'Meara SC, and shared with the ATO, which supports the opinion from EY (details of Mr O'Meara's opinion are contained in Appendix C on pg. 19). However, the ATO view is that:

- the Special Dividend forms part of the 'consideration' for the cancellation of EAI shares for the purposes of paragraph 202-45(k) of the ITAA 1997. The ATO view is that the Special Dividend is classed as an unfrankable distribution.
- to correctly calculate the net capital gain, the Special Dividend should additionally be included as capital proceeds.

Given the unlikelihood of a favourable class ruling on the transaction, EAI on the advice of EY, has withdrawn its class ruling application.

You may refer to the ATO's views contained in Appendix A on pg.2.

Investor position

We note that this is a complex matter and therefore have included communications from EY, ATO and Mr O'Meara's opinion in the appendices of this letter. We encourage you to review these documents.
Each investor's tax position will be unique and will impact them differently. You are encouraged to seek your own independent tax advice.
If you wish to submit or amend your tax return based on the ATO's guidance, we have provided an alternative distribution statement in alignment with the ATO's logic. Please be mindful that any amendments with the ATO must be lodged in a timely manner.
Based on the letter from ATO, EAI regards their current position as final.

Questions?
If you should have any questions regarding this matter, please don't hesitate to contact Ellerston's Investor Relations team on (02) 90217701 or via email at info@ellerstoncapital.com.

Authorised by Ian Kelly, Company Secretary

Australian Government
Australian Taxation Office

ELLERSTON ASIAN INVESTMENTS LIMITED
C/- ERNST & YOUNG
GPO BOX 2646
SYDNEY, NSW, 2001

Our Reference: [redacted]
Contact Officer:
Phone:
Client ID:
4 March 2024

Attention: [redacted]

Ellerston Asian Investments Limited – exchange of shares for units in Ellerston Asia Growth Fund

Dear Directors,

As Ellerston Asian Investments Limited (EAI) has withdrawn the class ruling application, the Commissioner has prepared this letter for EAI to circulate to all former shareholders, apart from ENSZ Nominees Pty Ltd (Exiting Shareholders), to advise them of the tax consequences in relation to the restructure of their investments in EAI on 5 June 2023, whereby each ordinary share held in EAI was exchanged for 0.13384 units in Ellerston Asia Growth Fund (EAGF), rounded down to the nearest unit (the 'EAI restructure').

The Commissioner notes that the Shareholder Booklet dated 19 April 2023, publicly circulated ahead of the then proposed restructure, provided a general summary of the potential income tax consequences of the transaction to shareholders (Shareholder Booklet).[1] The Shareholder Booklet also acknowledged that the Commissioner might express a view as to the income tax consequences that is contrary to that set out therein.

The Commissioner does have a view contrary to that set out in the Shareholder Booklet in respect of the dividend imputation and capital gains tax consequences. The Commissioner's view set out in this letter considered the information provided in the course of progressing the class ruling request (which has since been withdrawn).

The Commissioner has prepared this letter to enable Exiting Shareholders understand and comply with their obligations under the tax law. Therefore, they will need to amend their tax return to be in line with the Commissioner's view.

Important note - enacted legislation with retrospective effect

The tax consequences set out in this letter are based on the income tax law as at the date of this letter. Relevantly, this takes into consideration legislative changes contained in the Treasury Laws Amendment (2023 Measures No. 1) Bill 2023, enacted as Act No. 101 of 2023 and receiving Royal Assent on 27 November 2023. These amendments include changes to the tax treatment of selective share cancellations carried out by listed public companies (the 'selective share cancellation amendment') which have impacted on the tax consequences that happened to EAI shareholders.

It is noted that the law changes which occurred with retrospective effect (from 18 November 2022), only impact the imputation consequences of the special dividend.[2] That is, the law changes do not affect the capital gains tax consequences.

[1] At [2.9] of the Shareholder Booklet.
[2] That which is discussed at Part B of the summarised taxation consequences below.

Summarised taxation consequences[3]

A. Capital gains tax consequences

CGT event C2 happened to Exiting Shareholders on the 5 June 2023 when their EAI shares were cancelled.

The amount of any capital gain or capital loss made on the cancellation of an Exiting Shareholders EAI shares is dependent on the cost base (and reduced cost base, in the case of a capital loss) of their shares. They will have made a capital gain where the amount of capital proceeds exceed the cost base of their cancelled EAI shares or a capital loss where the amount of capital proceeds is less than their reduced cost base.

The capital proceeds from the cancellation of each EAI share is equal to 82.2232 cents per share, being the sum of *both*:

- the selective capital reduction amount – the dollar value of which[4] was 74.2087 cents per share (Capital Reduction Distribution); and
- the special dividend – the dollar value of which was of 8.0145 cents per share (Special Dividend).

However, if Exiting Shareholders have made a capital gain, their capital gain (not capital proceeds) is reduced by the amount of the Special Dividend given that amount is included in that shareholder's assessable income as an assessable divided[5]. A capital loss is not increased by the amount of the Special Dividend, nor can a capital gain be reduced below zero to create a capital loss.

For the purposes of calculating the net capital gain, provided the other conditions in Subdivision 115-A of the *Income Tax Assessment Act 1997* (ITAA 1997) are satisfied, if an Exiting Shareholders EAI shares were acquired at least 12 months before the 5 June 2023, they can treat any capital gain made by them on the ending of their EAI shares as a discount capital gain.

Each EAGF unit distributed in specie by EAI has a date of acquisition of 5 June 2023, being the date when EAI disposed of those units to Exiting Shareholders. This is also the date Exiting Shareholders acquired their distributed unit for the purposes of the capital gains tax discount provisions. The first element of the cost base and reduced cost base of each EAGF unit acquired is the market value of that unit on 5 June 2023. On advice from EAI as to that value, the Commissioner accepts an acquisition cost for each distributed EAGF unit to be $6.1435.

B. Imputation consequences of special dividend

The Special Dividend is included in assessable income.

Notwithstanding any distribution statement from EAI stating an amount of franking credits being allocated to the Special Dividend, the dividend is unfrankable as a result of the selective share cancellation amendment. This is the impact of the Commissioner's position that the Special Dividend forms part of the consideration for the cancellation of shares in EAI as part of a selective reduction of capital.

As the Special Dividend is not a franked distribution, Exiting Shareholders do not include any franking credits on that distribution in their assessable income and they are not entitled to a tax offset equal to the franking credit.

[3] The consequences apply to Exiting Shareholders who are Australian residents for tax purposes.
[4] As advised by EAI.
[5] Refer Part B below.

Explanation of the taxation consequences

Capital gain or loss on ending of EAI shares

CGT event C2 generally happens if a person's ownership of an intangible asset ends because the asset expires or is redeemed, cancelled, released, discharged, satisfied, abandoned, surrendered or forfeited. A person makes a capital gain if the capital proceeds from the ending are more than the asset's cost base, and they make a capital loss if those capital proceeds are less than the asset's reduced cost base.

The amount of capital proceeds received from a CGT event is worked out under Division 116 of the ITAA 1997. Under subsection 116-20(1) of the ITAA 1997, the capital proceeds from a CGT event are the total of the money received (or entitled to be received) and the market value of property received (or entitled to be received) 'in respect of the event happening'.

TR 2010/4[6] sets out the Commissioner's view on when a dividend will be included in capital proceeds, albeit in the context of CGT event A1. In particular, TR 2010/4 provides the Commissioner's view on the interpretation of the phrase 'in respect of the event happening' under subsection 116-20(1), which is informative in the present circumstances of CGT event C2. Specifically, the words 'in respect of', when used in section 116-20, require that the relationship between the event and the receipt of the target company dividend, or the entitlement to receive such a dividend, must be one based on more than mere coincidence or caused simply by temporal proximity.

In the present circumstances, the Commissioner has determined that there existed a more substantial causal and rational relationship between the cancellation of shares in EAI and the entitlement of the Exiting Shareholders to receive the Special Dividend. Specifically, the resolutions that Exiting Shareholders voted on reflect that the Special Dividend is part of the restructure which Exiting Shareholders bargained for in return for 'giving up' their EAI shares.

The Explanatory Memorandum[7] provided to all EAI shareholders ahead of the General and Special Meeting, and the resolutions proposed to (and as voted on favourably on 18 May 2023 by) EAI shareholders, evidence the Special Dividend as forming part of the bargain or understanding whereby Exiting Shareholders agreed to receive units in EAGF in consideration for giving up their EAI shares.

The in specie distribution, comprising both the Special Dividend and the Capital Reduction Distribution, was described to EAI shareholders as a key step in 'the Transaction'.[8] The in specie distribution was conditional (amongst other things) on 'each of the resolutions being approved by the [EAI] Shareholders'. That is, the payment of the Special Dividend was an integral part of the proposal put to shareholders, with no guarantee that the Special Dividend would have been paid irrespective of the EAI restructure proceeding.

On this basis, in determining the capital proceeds 'in respect of' the share cancellation, it is appropriate to take into account the market value of all property received by Exiting Shareholders under the restructure, including the Special Dividend.

The fact that one shareholder (ENSZ Nominees Pty Ltd) was entitled to the Special Dividend but did not participate in the Capital Reduction Distribution does not change the Commissioner's view. In voting to approve the Capital Reduction Distribution, the Special Dividend formed an integral component of what Exiting Shareholders bargained for, irrespective of the role of ENSZ Nominees Pty Ltd. This is evident in the conditionality of the resolutions as indicated above, including a resolution for the 'Approval of the Transaction' that itself includes payment of the Special Dividend. That is, from the perspective of each Exiting Shareholder and the capital proceeds received by them 'in respect of' the cancellation of their shares, the payment of the Special Dividend was an integral part.

[6] Taxation Ruling TR 2010/4 *Income tax: capital gains: when a dividend will be included in the capital proceeds from a disposal of shares that happens under a contract or a scheme of arrangements.*
[7] Forming part of the Shareholder Booklet, the general purpose of which is to provide shareholders with all information known to the company that is material to a decision on how to vote on the resolutions in any accompanying Notices of general or special meeting.
[8] at Item 2.1 of the Explanatory Memorandum.

Special Dividend not a frankable distribution

A distribution is a frankable distribution to the extent it is not unfrankable.

Section 202-45 of the ITAA 1997 sets out the circumstances under which an amount or distribution is taken to be unfrankable; it includes paragraph 202-45(k), which states:

> a distribution by a *listed public company that is consideration for the cancellation of a *membership interest in the company as part of a selective reduction of capital, including a selective reduction within the meaning of section 256B of the *Corporations Act 2001*.

At the time EAI distributed the Special Dividend to the Exiting Shareholders, EAI was a public listed company. Additionally, EAI undertook a selective reduction of capital for the purposes of sections 256B and 256C of the *Corporations Act 2001*. Therefore, the Special Dividend distributed will be unfrankable if the Special Dividend is consideration for the cancellation of an Exiting Shareholders EAI shares.

The question of whether the special dividend constitutes 'consideration for' the cancellation of shares closely follows the analysis evidencing the special dividend being capital proceeds 'in respect of' the CGT event as set out earlier in this letter. The phrase 'consideration for' was considered in *Chief Commissioner of State Revenue (NSW)* v. *Dick Smith Electronics Holdings Pty Ltd* (2005) 221 CLR 496. The relevance of this case in interpreting the CGT provisions follows the approach set out in TR 2010/4.

In line with the approach set out earlier in this letter, the Special Dividend is consideration for the cancellation of the EAI shares as part of a selective reduction of capital, thereby satisfying paragraph 202-45(k) of the ITAA 1997.

Therefore, the Special Dividend paid to all Exiting Shareholders is an unfrankable distribution.

Requesting amendment to assessments

If Exiting Shareholders have lodged their tax returns contrary to the position set out in this letter, they will need to request an amendment to their assessment for the income year ended 30 June 2023 to:

- reduce assessable income and tax offsets by the amount of the franking credits, and
- increase a net capital gain (or reduce a net capital loss) in respect of the capital gains tax consequences, that is, to ensure the Special Dividend is included in capital proceeds.

Information on how to request an amendment can be found at, Amend your tax return | Australian Taxation Office (ato.gov.au).

Penalties and interest

Any additional amount of tax that becomes payable as a result of an assessment being amended is subject to penalty and shortfall interest charge (SIC). However, you can ask the Commissioner to exercise their discretion to reduce (remit) the penalty or SIC in full or in part.

In deciding whether to reduce the penalty or SIC in full or in part, the Commissioner will consider, amongst other things:

- shareholders may have lodged their tax returns based on the general summary of the potential income tax consequences outlined in the Shareholder Booklet, and
- shareholders being subsequently advised of the Commissioner's position outlined in this letter.

Objection

Exiting Shareholders who disagree with the position set out in this letter can consider lodging an objection.

Information on how to object can be found at, Object to an ATO decision | Australian Taxation Office (ato.gov.au).

Information on how to contact the Australian Taxation Office for further information can be found at, Contact us | Australian Taxation Office (ato.gov.au).

Yours sincerely,

Deputy Commissioner of Taxation

Appendix B

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Building a better working world

The Directors
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SYDNEY NSW 2000

8 March 2024

Tax Letter for Shareholders

Dear Directors

We have been requested by Ellerston Asian Investments Pty Ltd (**EAI** or **Company**) to prepare a letter for circulation to shareholders in relation to the restructure of their investments in EAI restructure into units in the Ellerston Asia Growth Fund (**Transaction**) which occurred on 5 June 2023.

1. Background

The Shareholder Booklet circulated by EAI to shareholders in advance of the Transaction stated that EAI was in the process of making an application to Commissioner of Taxation for a class ruling in relation to the income tax implications of the Transaction.

EAI has been engaged in ongoing discussions with the Australian Taxation Office (**ATO**) in relation to the proposed class ruling. Through those discussions, the ATO has indicated that it has a view of the income tax implications of the Transaction which is contrary to the implications which were summarised in Section 2.9 of the Shareholder Booklet (and which represent EY's views). Given the views expressed by the ATO, the extended time taken to consider the application to this point and subsequent improbability of obtaining a class ruling which is consistent with Section 2.9 of the Shareholder Booklet, EAI in consultation with its professional advisers withdrew the class ruling application.

In light of the views expressed by the ATO, EAI sought the views of Michael O'Meara SC. Michael O'Meara is a barrister who specialises in taxation law amongst other matters. He was appointed Senior Counsel in 2019.

Mr O'Meara provided an opinion to EAI which is contained in an attachment to this letter. His opinion was consistent with the tax implications set out in Section 2.9 of the Shareholder Booklet.

This letter contains a summary of the income tax implications which were set out in Section 2.9 of the Shareholder Booklet along with worked examples to illustrate the potential tax implications for EAI shareholders. The worked examples also illustrate the potential impact of the ATO's views on the application of the tax law to the Transaction. The ATO has provided the letter contained in an attachment to this letter as an explanation of their view of the tax law.

Shareholders should seek their own independent advice to confirm the consequences of the views set out in this letter and the position that they should adopt in lodging their tax return. Where Shareholders choose to take a position which is contrary to the ATO's view of the law they may be the subject of

compliance activity, including potentially issuing amended assessments to such Shareholders. The ATO may seek to impose interest or penalties. Shareholders would have rights to object to their assessments and / or appeal rights to have the position adjudicated by a court or tribunal.

2. Executive summary

The following comments should be read subject to the detailed comments contained in this letter.

- The ATO has not agreed to issue a class ruling which is consistent with the tax implications set out in section 2.9 of the Shareholder Booklet and the tax implications set out in sections 4.1 and 4.2 of this letter. The ATO disagrees with certain of the positions reflected in those tax implications. The ATO has stated their views in the letter which is set out in an attachment to this letter.
- The impact of the ATO's position is that, compared with the tax implications set out in sections 4.1 and 4.2 of this letter:
  - As the ATO do not consider the Special Dividend is a frankable distribution, no franking credits would be available to Shareholders in respect of the Special Dividend; and
  - As the ATO considers that the Special Dividend forms part of Shareholders' capital proceeds for the cancellation of their EAI shares, the capital losses of a Shareholder would be reduced by up to the amount of the Special Dividend received by that Shareholder.
- EY's views with respect to tax implications of the Transaction remains unchanged. These views are set out in sections 4.1 and 4.2 of this letter and are consistent with the comments contained in section 2.9 of the Shareholder Booklet.
- EY's views are supported by a detailed opinion obtained from Michael O'Meara SC which provides a comprehensive analysis of the relevant tax laws.
- EY are of the view that the ATO's position is inconsistent with the fact that the special dividend was received by all shareholders including those who did not participate in the selective capital reduction.
- Shareholders will need to determine whether to adopt the position described in sections 4.1 and 4.2 (which reflects EY's view and which is supported by Michael O'Meara SC's opinion) or the ATO's view. Where Shareholders choose to adopt an approach which is contrary to the ATO's view, the ATO may take compliance action which could ultimately result in interest and penalties being applied by the ATO. Shareholders would have certain objection / appeal rights in the event that the ATO took compliance action with respect to the Shareholder's position in relation to the Transaction.

3. Relevant Transaction steps

Relevantly, the Transaction included the following steps:

- On 31 May 2023, EAI transferred all of its assets (**EAI Assets**) excluding a cash reserve to meet, among other things, its estimated tax liabilities and transaction costs.

- On that date, in consideration for the transfer, the responsible entity for Ellerston Asia Growth Fund (**EAGF**) issued units (**EAGF Units**) to EAI.
- On 5 June 2023, EAI paid a dividend (**Special Dividend**) to all Shareholders of 8.0145 cents per share, fully franked at a 25% tax rate. The Special Dividend included franking credits of 2.6715 cents per share.
- On that date, EAI also made a selective capital reduction (**Capital Reduction Distribution**) to all Shareholders except for ENSZ Nominees Pty Ltd, which retained a nominal shareholding in the Company to facilitate its winding up, of 74.2087 cents per share.
- Payment of the Special Dividend and the Capital Reduction Distribution was satisfied through the in-specie transfer of the EAGF Units held by EAI to the relevant Shareholders (**In Specie Distribution**). Shareholders (other than ENSZ Nominees Pty Ltd) received 0.13384 EAGF Units per EAI share which they held, rounded down to the nearest unit.

4. Summary of tax implications

The following is a general summary of the potential Australian income taxation consequences of the Transaction to shareholders of EAI.

The following comments do not purport to be a complete analysis or to identify all potential tax consequences. The comments only apply to Shareholders who are resident in Australia for tax purposes and who hold their Shares in the Company on capital account for Australian income tax purposes. This section therefore does not consider Shareholders who are not Australian tax residents, who either hold their Shares as trading stock or on revenue account, are not subject to Australian income tax, or are subject to the Taxation of Financial Arrangements rules under Australian income tax law. Non-resident Shareholders should obtain tax advice on the implications of the Transaction to their Australian tax position and the tax rules in their country.

The summary of potential Australian income tax consequences described below are statements of general principle only and Shareholders should be aware that the actual Australian tax implications may differ from those summarised below, depending on the individual circumstances of each Shareholder. This summary does not constitute tax advice and should not be relied upon as such. Shareholders should obtain and rely on their own tax advice in relation to taxation consequences of the Transaction having regard to their particular circumstances. We do not accept any responsibility or liability in respect of such consequences.

This section is based on Australian income tax legislation, public taxation rulings, determinations, and administrative practice as at the date of this letter. The comments do not take into account or anticipate changes in Australian tax law, administrative practice or future judicial interpretations of Australian tax law after the date this letter. Future amendments to taxation legislation, or its interpretation by the court or the taxation authorities, may take effect retrospectively and/or affect the conclusions drawn.

4.1 Special Dividend received from the Company

Shareholders who received the Special Dividend of 8.0145 cents per share should be required to include the amount of the dividend in their assessable income.

Generally, provided you are a "qualified person" in relation to the Special Dividend and the ATO does not make a determination under the dividend streaming rules to deny the benefit of the franking credits attached to the Special Dividend, Shareholders should:

- also include the franking credits of 2.6715 cents per share which were attached to the Special Dividend in their assessable income, and
- subject to special rules which apply where a partnership or trust receives the dividend, qualify for a tax offset for the 2.6715 cents per share of franking credits attached to the Special Dividend, which can be applied against a Shareholder's income tax liability for the relevant income year.

The ATO has not indicated that they intend to apply dividend streaming rules to deny the benefit of franking credits.

Certain rules concerning distributions which are consideration for the cancellation of shares under a selective share capital reduction can also have the effect of preventing Shareholders from benefiting from franking credits attached to the Special Dividend. The application of these rules is discussed in section 4.1.1 below. The ATO consider that these rules applied to treat the Special Dividend as an unfrankable distribution, meaning that the franking credits attached to the Special Dividend were not able to be distributed.

A Shareholder should be a "qualified person" in relation to the Special Dividend if the "holding period rule" and the "related payments rule" are satisfied. Generally:

- to satisfy the "holding period rule", a Shareholder must have held their Shares "at risk" for at least 45 days (not including the days of acquisition and disposal) within the period beginning on the day after the day on which the Shares were acquired and ending 45 days after the Shares become ex-distribution. This means that once a Shareholder satisfies the "holding period rule" in relation to a distribution on Shares, the Shareholder does not need to satisfy it again in relation to those Shares for subsequent distributions, unless the Shareholder makes a "related payment" (refer below), and
- under the "related payments rule", if a Shareholder is obligated to make a "related payment" (essentially a payment passing on the benefit of the Special Dividend) in respect of the Special Dividend, the Shareholder must hold the Shares "at risk" for at least 45 days (not including the days of acquisition and disposal) within each period beginning 45 days before, and ending 45 days after, they become ex-distribution.

To be held "at risk", a Shareholder must retain 30% or more of the risks and benefits associated with holding the Shares. Where a Shareholder undertakes risk management strategies in relation to their Shares (e.g. by the use of limited recourse loans, entering into put or call options in relation to the Shares or other derivatives), a Shareholder's ability to satisfy the "at risk" requirement and thus to be a "qualified person" may be affected.

Individual Shareholders are automatically treated as a "qualified person" for these purposes if the total amount of tax offsets in respect of all franked amounts to which the individual is entitled in an income year does not exceed A$5,000. This is referred to as the "small shareholder rule". However, an individual will not be a "qualified person" under the small shareholder rule if "related payments" have been made, or will be made, in respect of these amounts.

Certain other anti-avoidance rules may also deem a person not to be a ”qualified person” with respect to a dividend, including where a franked dividend is streamed to certain shareholders or where there is a dividend stripping or dividend washing arrangement.

Australian tax resident individuals and complying superannuation funds may be able to receive a cash tax refund from the ATO if the tax offset equal to the franking credits attached to the Special Dividend exceeds the tax payable on their total taxable income.

As noted above, special rules apply in relation to franked dividends received by partnerships or trusts. Where the franked dividend “flows indirectly” to the partners in the partnership or the beneficiaries of a trust, a tax offset equal to the partner or beneficiary’s share of the franking credit attached to the Special Dividend should be available to the partner or beneficiary, provided both the partner or beneficiary and the partnership or trust (as relevant) are each a “qualified person”. Shareholders who are partnerships or trusts should seek their own advice in relation to the application of these rules, including whether the Special Dividend will “flow indirectly” to partners or beneficiaries.

For a company, the franking credits attached to the Special Dividend will generally give rise to a franking credit in the company’s franking account. A company will not be entitled to a tax refund of the excess franking credits. Rather, the surplus franking credits may be converted to a tax loss which can be carried forward to future years (subject to satisfying certain loss carry forward rules).

4.1.1 Selective Capital Reduction Rules

Where a listed public company makes a distribution that is consideration for the cancellation of a membership interest in the company as part of a selective reduction of capital, that distribution is taken to be unfrankable. This means that no franking credits may be attached to the distribution and Shareholders should not be required to include any additional amount in their assessable income and should not be entitled to any tax offset in respect of the franking credits.

In our view, this rule should not apply to the Special Dividend because we do not consider that the Special Dividend is consideration for the cancellation of the membership interests in EAI. We consider that the fact that the Special Dividend was paid to all Shareholders, including those whose shares were not subject to the selective share capital reduction or cancellation, results in a conclusion that the Special Dividend is not received as consideration for the cancelation of the membership interest. This view is supported by the opinion provided by Michael O’Meara which is set out in an attachment to this letter.

4.2 Capital Reduction Distribution and cancellation of Shares

The Capital Reduction Distribution of EAGF Units to Shareholders and cancellation of Shares will give rise to a CGT event for the Shareholders who receive the Capital Reduction Distribution. Shareholders should accordingly be required to calculate a capital gain or capital loss. The amount of the capital gain or capital loss will be dependent on each Shareholder’s cost base (in the case of a capital gain) or reduced cost base (in the case of a capital loss).

A capital gain should arise for a Shareholder where the amount of the capital proceeds received by the Shareholder exceeds that Shareholder’s cost base for the shares. A capital loss should arise where the amount of the capital proceeds received by the Shareholder is less than the reduced cost base of the

shares. We consider that the capital proceeds for the share cancellation should include the Capital Reduction Distribution (being 74.2087 cents per share) only.

The time at which the CGT event should be recognised is at the time of the Capital Reduction Distribution and share cancellation on 5 June 2023. Resident individuals, trusts (where certain conditions are satisfied) and complying superannuation fund Shareholders who have held their shares for at least 12 months may be entitled to the CGT discount. The CGT discount may reduce capital gains by 50% for resident individuals and certain trusts or 33 1/3% for complying superannuation funds.

Returns of share capital may be re-characterised as unfranked dividends where the Commissioner makes a determination under section 45B of the Income Tax Assessment Act 1936. The ATO has not indicated that it is inclined to make such a determination. However, in the event that the Commissioner made such a determination with respect to the Capital Reduction Distribution, Shareholders would be required to include the amount of their entitlement to the Capital Reduction Distribution in their assessable income. The CGT discount should not apply in this case.

4.3 Cost base and date of acquisition of new EAGF Units

The first element of the cost base and reduced cost base for each new EAGF Unit that was acquired should equal the market value of the new EAGF Unit at the time of the transfer of the new EAGF Units, being $6.1435 per EAGF Unit.

For CGT purposes (including the CGT discount), the date of acquisition of the EAGF Units should be 5 June 2023.

5. ATO views

Shareholders may refer to the ATO's views contained in an attachment to this letter.

The ATO's view is that the Special Dividend is unfrankable because of the rule described in section 4.1.1 above.

The ATO's view is that the capital proceeds for the cancellation of EAI shares should include the Special Dividend of 8.0145 cents per share as well as the Capital Reduction Distribution of 74.2087 cents per share.

Where a Shareholder's cost base in a share is no greater than 74.2087 cents, the ATO's view should result in the same capital gain as if the consequences set out in section 4.2 applied. This is because the amount of the dividend should be reduced from the amount of the capital gain under the anti-overlap rule.

However, where a Shareholder's reduced cost base in a share is more than 74.2087 cents then the ATO's view should result in the Shareholder's capital loss in respect of the share cancellation being less than if the consequences set out in section 4.2 applied. There is no equivalent anti-overlap rule which applies to increase a capital loss.

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We consider that the ATO views are inconsistent with the fact that the Special Dividend was received by Shareholders who did not have their membership interests cancelled and that the ATO views inappropriately seek to disregard that fact.

6. Illustrative examples

Example 1 assumes the following facts:

- The Shareholder is an individual Australian resident taxpayer holding their shares on capital account and is a "qualified person" with respect to the Special Dividend.
- The Shareholder has a marginal tax rate of 47% including the Medicare Levy.
- The Shareholder acquired 10,000 EAI shares for $1 per share.

The tax implications set out below reflect the views expressed in Section 2.9 of the Shareholder Booklet and in sections 4.1 and 4.2 above. We note that this is contrary to the views expressed by the ATO.

Example 1

Special Dividend

The Shareholder will be required to include the following amounts in their assessable income:

Dividend:	10,000 x 8.0145 cents =	$801.45
Franking Credit:	10,000 x 2.6715 cents =	$267.15
Total		**$1,068.60**

The Shareholder will be entitled to a tax offset equal to the amount of the franking credit being $267.15.

The tax payable by the Shareholder in respect of the Special Dividend will be:

47% x $1,068.60	=	$502.24
Less: franking credit tax offset		($267.15)
Total		**$235.09**

Capital Reduction Distribution and cancellation of shares

Capital proceeds:	10,000 x 74.2087 cents =	$7,420.87	(Capital Reduction Distribution)
Cost base:	10,000 x $1.00 =	($10,000.00)	
Capital loss		**($2,579.13)**	

The capital loss may be applied to the Shareholder's current or future capital gains.

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Example 2 assumes the same facts as Example 1. The tax implications below reflect the ATO's views:

Example 2

Special Dividend

The Shareholder will be required to include the following amounts in their assessable income:

Dividend:	10,000 x 8.0145 cents =	$801.45	
Franking Credit:		Nil	
Total		**$801.45**	

The Shareholder will not be entitled to any tax offset.

The tax payable by the Shareholder in respect of the Special Dividend will be:

47% x $1,068.60	=	$502.24	
Less: franking credit tax offset		Nil	
Total		**$502.24**	

Capital Reduction Distribution and cancellation of shares

Capital proceeds:	10,000 x 74.2087 cents =	$7,420.87	(Capital Reduction Distribution)
	10,000 x 8.0145 cents =	$801.45	(Special Dividend)
Cost base:	10,000 x $1.00 =	($10,000.00)	
Capital loss		**($1,777.68)**	

The capital loss may be applied to the Shareholder's current or future capital gains.

Example 3 assumes the following facts:

- The Shareholder is an individual Australian resident taxpayer holding their shares on capital account and is a "qualified person" with respect to the Special Dividend.
- The Shareholder has a marginal tax rate of 47% including the Medicare Levy.
- The Shareholder acquired 10,000 EAI shares for $0.65 per share.
- The Shareholder had held their shares for less than 12 months at the time of the Transaction.

The tax implications set out below reflect the views expressed in Section 2.9 of the Shareholder Booklet and in sections 4.1 and 4.2 above. We note that this is contrary to the views expressed by the ATO.

Example 3

Special Dividend

The Shareholder will be required to include the following amounts in their assessable income:

Dividend:	10,000 x 8.0145 cents =	$801.45	
Franking Credit:	10,000 x 2.6715 cents =	$267.15	
Total		**$1,068.60**	

The Shareholder will be entitled to a tax offset equal to the amount of the franking credit being $267.15.

The tax payable by the Shareholder in respect of the Special Dividend will be:

47% x $1,068.60	=	$502.24
Less: franking credit tax offset		($267.15)
Total		**$235.09**

Capital Reduction Distribution and cancellation of shares

Capital proceeds:	10,000 x 74.2087 cents =	$7,420.87	(Capital Reduction Distribution)
Cost base:	10,000 x $0.65 =	($6,500.00)	
Capital gain		**$920.87**	

The tax payable by the Shareholder in respect of the Capital Reduction Distribution and cancellation of shares will be:

47% x $920.87	=	$432.81

The total tax payable by the Shareholder in respect of the Transaction will be $667.90.

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Example 4 assumes the same facts as Example 3. The tax implications below reflect the ATO's views:

Example 4

Special Dividend

The Shareholder will be required to include the following amounts in their assessable income:

Dividend:	10,000 x 8.0145 cents =	$801.45	
Franking Credit:		Nil	
Total		**$801.45**	

The Shareholder will not be entitled to any tax offset.

The tax payable by the Shareholder in respect of the Special Dividend will be:

47% x $1,068.60 =	$502.24	
Less: franking credit tax offset	Nil	
Total	**$502.24**	

Capital Reduction Distribution and cancellation of shares

Capital proceeds:	10,000 x 74.2087 cents =	$7,420.87	(Capital Reduction Distribution)
	10,000 x 8.0145 cents =	$801.45	(Special Dividend)
Cost base:	10,000 x $0.65 =	($6,500.00)	
Sub-total		$1,722.32	
Less: reduction under anti-overlap rule		($801.45)	
Capital gain		**$920.87**	

The tax payable by the Shareholder in respect of the Capital Reduction Distribution and cancellation of shares will be:

47% x $920.87 =	$432.81	

The total tax payable by the Shareholder in respect of the Transaction will be $935.05.

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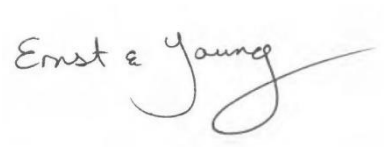
7. Disclaimer

The summary of tax implications contained in this letter does not constitute financial product advice as defined in the *Corporations Act 2001*. The summary is confined to taxation issues and is only one of the matters you need to consider when making a decision about your investments. You should consider taking advice from a licensed adviser, before making a decision about your investments. The partnership of Ernst & Young is not required to hold an Australian Financial Services Licence under the *Corporations Act 2001* to provide this taxation advice.

We disclaim all liability to any Shareholder or other party for all costs, loss, damage and liability that the Shareholder or other party may suffer or incur arising from or relating to or in any way connected with the contents of this letter or the provision of this letter to the Shareholder or other party.

* * * * *

Yours sincerely,



Ernst & Young

Appendix C

In re Ellerston Asian Investments Limited and the *Income Tax Assessment Act 1997* (Cth)

OPINION

Certain tax consequences of the payment of in-specie distribution

For: Ernst & Young
Attention: Mr George Stamoulos / Mr Daryn Moore

Introduction and background:

1. On and from 10 September 2015 Ellerston Asian Investments Limited (**EAI**) was a listed investment company admitted to the official list of the Australian Stock Exchange (**ASX**). EAI's investment objective was to establish and maintain a concentrated portfolio of Asian equity securities with a focus on capital growth. EAI appointed Ellerston Capital Limited as manager of its portfolio. A majority of its investments have been in listed Asian securities with other investments in cash, interest products, foreign currencies, derivatives and unlisted Asian equity securities.

2. From the time of its listing, EAI's shares consistently traded at a price which reflected a discount to the value of EAI's net tangible assets per share. To address this, from November 2022 to June 2023 EAI proposed and undertook a transaction the effect of which was to merge EAI with the Ellerston Asia Growth Fund, which was to be renamed Ellerston Asia Growth Fund (Hedge Fund) (**EAGF**), and convert it to a dual-structure exchange traded managed fund (**the Transaction**). EAGF units would then trade on the ASX with AQUA Trading Status. AQUA Trading Status applies modified listing rules to the products listed under that status. The AQUA Trading Status is appropriate for products the capital value of which is linked to underlying instruments with a robust and transparent pricing mechanism, eg., securities traded on a public stock exchange or commodities traded on a public commodities market. EAI's Board anticipated that, following the Transaction, units in EAGF would trade at a price that would more closely reflect the underlying value of the investments.

3. My opinion has been sought on two questions relating to the treatment of aspects of the Transaction under the *Income Tax Assessment Act 1997* (Cth) (**1997 Act**), including as amended

by the *Treasury Laws Amendment (2023 Measures No 1) Bill 2023* (Cth) (**2023 Bill**) which is currently before Parliament. To understand those questions and how they arise, it is necessary to explain some further aspects of the Transaction.

4. The essential elements of the Transaction were as follows:

   (a) EAI transferred to EAGF all of its assets aside from a cash reserve to meet transaction costs and estimated tax liabilities.

   (b) In consideration for the transfer of its assets, EAGF issued to EAI fully paid ordinary units (**EAGF units**).

   (c) EAI then made an in-specie distribution of EAGF units to its shareholders (**in-specie distribution**). The in-specie distribution consisted of two parts:

      (i) a fully franked special dividend debited to EAI's dividend profits reserve which would be paid to all shareholders (**special dividend**). The dividend profits reserve was constituted by amounts transferred from current period earnings and retained profits; and

      (ii) a capital reduction distribution made as part of a selective capital reduction and cancellation of the EAI shares pursuant to Part 2J.1 of the *Corporations Act 2001* (Cth) (**Corps Act**) which would be paid to all shareholders other than ENSZ Nominees Pty Limited (**Ellerston shareholder**). The shareholders receiving the capital reduction distribution were referred to as the **exiting shareholders**. The Ellerston shareholder was maintained to ensure EAI had a shareholder to attend to administrative matters and to enable the ultimate deregistration of EAI.

   (d) The number of EAGF units distributed as part of the in-specie distribution was determined according to a formula the intended effect of which was that the EAGF units distributed to exiting shareholders would give them equivalent value to the value of their EAI shares immediately before the Transaction. In the events which happened, the application of the formula resulted in EAI shareholders receiving 0.13384 EAGF units per EAI share.

(e) The in-specie distribution was divided between the special dividend and the capital reduction distribution by reference to the available balance in EAI's dividend profits reserve. In the event, the special dividend was 8.0145c per EAI share satisfied through EAGF units. It was debited to and exhausted EAI's dividend profits reserve.

(f) The balance of the in-specie distribution, which was the capital reduction distribution, was debited to EAI's share capital account.

(g) In the case of overseas shareholders of EAI, the EAGF units to which the shareholders were entitled were sold by EAI to a nominee and then sold on the market with the proceeds (less costs and expenses) remitted to the overseas shareholders. This was a result of the compliance burden associated with making an in-specie distribution to shareholders in overseas jurisdictions.

(h) EAI delisted from the ASX, converted to a proprietary limited company and will ultimately be deregistered. In the events which happened, the in-specie distribution was effected on the same day that EAI was delisted from the ASX, being 4pm on 5 June 2023.

Questions on which my opinion is sought and short answers to those questions:

5. Against that background, it is possible to identify and provide my short answers to the questions on which my opinion has been sought:

(a) **Question 1:** Does the special dividend which was paid as part of the Transaction comprise capital proceeds for the CGT event which occurred upon the cancellation of the shareholders' shares in EAI?

Answer: No.

(b) **Question 2**: Does the special dividend which was paid as part of the Transaction comprise "consideration for the cancellation of a membership interest in the company as part of a selective reduction of capital" for the purposes of the proposed par. 202-45(k) of the 1997 Act as contained in Item 19 of Part 2 of Schedule 4 of the 2023 Bill?

Answer: No.

6. I develop my answers to each of these questions below. Before doing so, however, it is necessary to set out some further background. I commence that background by discussion of some of the provisions in EAI's Constitution at the time of the Transaction, particularly those dealing with the payment of dividends and those dealing with capital reductions.

Further background:

EAI's Constitution:

7. Rule 3 of EAI's Constitution provides to the effect that the replaceable rules in Part 2B.4 of the Corps Act do not apply to EAI.

8. Rules 30 to 33 of EAI's Constitution appear under the heading "Changes to Share Capital". Rule 30 provides to the effect that the directors may do anything to give effect to any resolution altering or approving the reduction of EAI's share capital, with some inclusive references which are not presently relevant. Rule 31 is entitled "Reductions of capital" and r. 31.1 provides that, subject to the Corps Act and the ASX Listing Rules, EAI may reduce its share capital in any manner. Rule 31.2 provides that:

> Without limiting the generality of clause 31.1, the Company [EAI] when reducing its share capital may resolve that such reduction be effected wholly or in part by the distribution of specific assets … and in particular fully paid shares, debentures, debenture stock or other securities of any other corporation or in any one or more of such ways. The Directors may fix the value for distribution of any specific assets.

9. Rule 31.3 deals with a circumstance in which EAI, pursuant to a reduction of its share capital, distributes shares in another corporation and provides, in effect, that in those circumstances EAI's members will be deemed to have agreed to become members of the other corporation. The member appoints EAI or its directors their agent to execute any transfer of shares or other document necessary to effect the distribution of shares to them.

10. Rules 88 to 99 of EAI's Constitution appear under the heading "Dividends and reserves". Rule 88 provides, in effect, that EAI's directors may, by resolution, declare, and fix the amount, the time and the method for payment of a dividend (par. (a)); or determine a dividend or interim dividend is payable, and fix its amount, the time and method of payment (par. (b)). The

distinction between the power of the directors of EAI to "declare" a dividend in r. 88(a) and to "determine" a dividend in r. 88(b) reflects the distinction drawn in s 254U and s 254V of the Corps Act and affects the time at which the dividend becomes a debt due by EAI to a shareholder: cf., ***Bluebottle*** *UK Limited v Deputy Commissioner of Taxation* (2007) 232 CLR 598 at [26]-[36]. This is supported by r. 89 which provides, in effect, that if the directors determine a dividend or interim dividend is payable, they may amend or revoke that determination before the record date notified to the ASX.

11. Rule 91 is entitled "Reserves" and provided as follows:

> The Directors may set aside out of any amount available for distribution as a dividend such amounts by way of reserves as they think appropriate before declaring a dividend or determining a dividend.

12. Rule 91.2 provides in effect that where the directors resolve to declare or determine a dividend or state their intention to do so, the directors will have been taken to set aside the amount available for distribution as a dividend as a reserve and such amount will not be appropriated against losses or appropriated or used for any other purpose, expect pursuant to a resolution of the directors.

13. Rule 92.1(a) provides, in effect, that, subject to shares with any special rights to dividends (of which there was none), all fully paid shares were entitled to participate equally in a dividend. Rule 92.1(b) is concerned with partly paid shares and can be passed over. Rule 92.4 provides that, subject to the ASX Settlement Operating Rules, the directors may fix a record date for a dividend and r 92.5(a) provides to the effect that where the directors have fixed a record date the dividend must be paid to the person registered or entitled to be registered as a holder of shares in EAI on the record date. Where no record date is fixed, the dividend must be paid to the persons who are registered, or are entitled to be registered, as holders of shares on the date fixed for payment of the dividend (r. 95.2(b)). Transfers of shares which are not registered before the record date or the date fixed for payment are not effective to transfer the right to the dividend (r 92.5 and r. 92.6).

14. Rule 95 is entitled "Distribution of assets" and r. 95.1 provides as follows:

> The Directors may resolve that a dividend will be paid wholly or partly by the transfer or distribution of specific assets, including fully paid shares in, or debentures of, any other corporation.

15. Rule 95.2 provides to the effect that the directors can deal with difficulties in making a transfer or distribution of specific assets as they consider expedient, including fixing the value of all or any part of the specific assets for the purposes of the distribution. Rule 95.3 provides that if a distribution of specific assets was illegal or impracticable, the directors could make a cash payment to member(s) on the basis of the cash amount of the dividend. Rule 95.4 addresses a dividend consisting of shares in another entity in a manner similar to r. 31.3 referred to in par. 9 above.

EAI General Meeting and Special Meeting of 18 May 2023:

16. On 18 May 2023 a General Meeting of EAI shareholders and a Special Meeting of exiting shareholders (together, **the Meetings**) occurred at which the shareholders considered and passed a series of resolutions directed at facilitating and approving the Transaction. The Meetings were preceded by provision of a **Shareholders Booklet** dated 19 April 2023 containing (inter alia) an Explanatory Memorandum (**EM**).

17. The EM explained the Transaction and its rationale and at section 2.3, p11 under the heading "What will you receive?" read as follows (emphasis added):

> If the Transaction is implemented, it is expected that Shareholders will receive the following distributions:
>
> (a) for all Shareholders, the Special Dividend, to be franked to the maximum extent possible; and
>
> (b) for the Exiting Shareholders, the Capital Reduction Distribution (**in consideration for which the Shares held by the Exiting Shareholders will be cancelled**).
>
> Payment of the Special Dividend and Capital Reduction Distribution will be satisfied by the In Specie Distribution, being the distribution in-specie of EAGF Units. Certain Overseas Shareholders will, instead of receiving EAGF Units, receive Cash Proceeds (see further details below).

18. Under the heading "What is the impact on your shareholding in the Company?", p13, the EM stated as follows:

> If you are an Exiting Shareholder, your Shares will be cancelled if the Transaction is implemented. As a result, you will no longer hold any Shares in the Company.

> If you are not an Exiting Shareholder (ie you are the Ellerston Shareholder), the number of Shares you hold will not change however the value of your Shares in the Company will be less than the value held prior to the Transaction being implemented due to the removal of the EAI Assets from the Company's asset portfolio. The size of any decrease will be dependent on the value ascribed to the EAI Assets.
>
> In addition, if you are the Ellerston Shareholder, you will be the sole Shareholder if the Transaction is implemented.

19. Six resolutions were put before and passed by the Meetings on 18 May 2023. The first resolution put before the General Meeting was a special resolution to amend EAI's Constitution pursuant to s 136(2) of the Corps Act to include cl. 31 and cl. 95 of the Constitution referred to in pars. 7 - 9 and 13 - 15 above.

20. The second resolution sought approval for the capital reduction distribution and was put before the General Meeting and Special Meeting in similar terms. The terms of the resolution put before the General Meeting were as follows:

> That, subject to and conditional on all other Resolutions and the Special Meeting Resolution being passed, for the purposes of sections 256B and 256C of the Corporations Act and for all other purposes, approval is given for the Company to reduce its share capital, with the reduction to be effected against each Share held by each Exiting Shareholder at the Record Date by cancelling all such Shares in consideration for potentially some cash and the Company making a pro rata distribution in-specie of EAGF Units to each Exiting Shareholder at the Record Date on the terms and conditions set out in the Explanatory Memorandum which accompanied the Notice of General Meeting.

21. The EM at section 6.2 and at section 10.2 noted that the proposed reduction of capital by way of the capital reduction distribution was a selective capital reduction pursuant to s 256C of the Corps Act and the elements of s 256C were addressed, ie., that the reduction was fair and reasonable to shareholders as a whole; it did not materially prejudice the company's ability to pay its creditors; and, was approved by shareholders. Reference was made to the independent expert report provided by KPMG dated 19 April 2023 which concluded that the Transaction was fair and reasonable and in the best interests of exiting shareholders, subject to a superior proposal (**KPMG report**). The KPMG report is discussed further below.

22. On p43 in section 10.2 the EM stated as follows:

> Under the Capital Reduction Distribution, the Shares held by the Exiting Shareholders will be cancelled and as consideration they will receive EAGF Units. It is anticipated that as a result

of the Special Dividend and the Capital Reduction Distribution, Exiting Shareholders will have substantially the same percentage holding in EAGF as they used to have in the Company (adjusted for the EAGF Units which are currently on issue).

23. The third resolution put before the General Meeting sought approval for the removal of EAI from the Official List of the ASX. The fourth resolution put before the General Meeting sought approval for the admission of EAGF units to AQUA Trading Status on the ASX. The fifth resolution put before the General Meeting sought approval for the Transaction.

24. As noted above, the KPMG report accompanied the Shareholders Booklet. KPMG concluded that the Transaction was fair because the value of the proposed consideration to be issued to exiting shareholders (128,092,270 EAGF units) per EAI share largely overlapped with the value of an EAI share, the difference being attributable to transaction costs. As the Transaction was fair, KPMG considered it was also reasonable.

Resolutions of EAI Board of 23 May 2023:

25. On 23 May 2023 the EAI Board passed the following resolutions, by way of a circular resolution:

    1. the Company seek formal approval under ASX Listing Rule 17.11 to remove EAI from the Official List of ASX on or about 5 June 2023;

    2. subject to and after the removal of EAI from the Official List of ASX taking effect, EAI pay the Special Dividend to all Shareholders (franked to the maximum extent possible) and undertake a selective capital reduction to all Shareholders apart from the Ellerston Shareholder, payment of which will be satisfied by the distribution in-specie of EAGF Units pursuant to a ratio of EAGF Units per EAI share to be determined on or about (or before) 5 June 2023.

Implementation of the Transaction:

26. On 25 May 2023 trading in EAI shares on the ASX was suspended. The "record date" for the in-specie distribution, including the special dividend, was 29 May 2023. On 31 May 2023 EAI transferred its assets to EAGF and the EAGF units were issued to EAI. Also on that day, the number of EAGF units to be distributed to each EAI shareholder was calculated. On 5 June 2023 EAI made the in-specie distribution to EAI shareholders, including the special dividend and the capital reduction distribution. On the same day, EAGF units were given the AQUA

Trading Status on the ASX. At the close of trading on 5 June 2023, EAI shares were delisted from the ASX. On 8 June 2023 EAGF units commenced trading on the ASX.

Legal character of the capital reduction distribution and special dividend:

27. Before addressing the specific questions on which my opinion has been sought, it is necessary to briefly examine the legal character of, and distinction between, a payment to a shareholder pursuant to a reduction of capital and payment of a dividend.

28. The traditional distinction between a return of capital by a company and other payments made by a company to shareholders, including dividends, was expressed by Lord Russell of Killowen in *Hill v Permanent Trustee Co of New South Wales Ltd* [1930] AC 720 (PC) at 731:

> A limited company not in liquidation can make no payment by way of return of capital to its shareholders except as a step in an authorised reduction of capital. Any other payment made by it by means of which it parts with money to its shareholders must and can only be made by dividing profits. Whether the payment is called "dividend" or "bonus" or any other name, it still must remain a division of profits.

29. This statement requires qualification following the amendment of s 254T of the Corps Act in 2010 to remove the requirement that a dividend not be paid other than out of profits. Following those amendments, s 254T provides to the effect that a company must not pay a dividend unless: the company's assets exceed its liabilities immediately before the dividend is declared and that excess is sufficient for the payment of the dividend (par (a)); the payment of the dividend is fair and reasonable to the company's shareholders as a whole (par (b)); and the payment of the dividend does not materially prejudice the company's ability to pay its creditors (par. (c)): see further, *DSHE Holdings Ltd v Potts* [2022] NSWCA 165; (2022) 371 FLR 349 at [89].

30. However, it remains true that a reduction of capital can only occur in a manner authorised by Part 2J.1 of the Corps Act with the result that a distinction is to be drawn between a payment which is a reduction of capital (which must be authorised under Part 2J.1) and other payments made by a company (whether called "dividends", "bonuses" or otherwise) which must comply with s 254T: see RP Austin and IM Ramsey (eds), *Ford's Principles of Corporations Law* (17th Ed, 2018) at [18.090], p1195-1196. Perhaps for related reasons, it has been suggested that notwithstanding the amendments to s 254T of the Corps Act in 2010, there remains a general law principle that dividends can only be paid out of profits, given the essential nature of a

dividend as a "share of profits": *Wambo Coal Pty Limited v Sumiseki Materials Co Ltd* (2014) 88 NSWLR 689 at [57] (Barrett JA; Bathurst CJ and Beazley P agreeing).

31. Traditionally, a final dividend was a debt due by the company to the shareholder from the date of declaration or other date stipulated for payment. In contrast, interim dividends were revocable until paid: *Bluebottle* at [19]-[20]. Section 254V(1) of the Corps Act now provides that a company does not incur a debt merely by fixing the amount or time for payment of a dividend, but a debt only arises when the time fixed for payment arrives, and the decision to pay a dividend can be revoked at any time before then. Section 254V(2) provides that where a company's constitution provides for the declaration of dividends, the company incurs a debt when a dividend is declared. The liability to pay a dividend will be complete when the shareholders to whom it is to be paid have been identified, which will usually be on the "record date:" *Bluebottle* at [41].

32. In ***Cable & Wireless*** *Australia & Pacific Holdings BV (in liq) v Federal Commissioner of Taxation* (2017) 251 FCR 483 at [94] Allsop CJ, Middleton and Beach JJ pointed out that a reference to capital in the context of a return of capital is a reference to the value of shareholders' capital or to contributed capital. The assets constituting that capital may change from time to time, but that does not constitute a reduction of capital. A reduction of capital is a payment (including by way of an in-specie distribution) which diminishes the *value* of that contributed capital.

33. The relevant means for an authorised reduction of capital appear in Division 1 of Part 2J.1 of the Corps Act and are to the following effect. Section 256B(1) of the Corps Act provides that a company may reduce its share capital in a way not otherwise authorised by law if: the reduction is fair and reasonable to the company's shareholders as a whole (par. (a)); it does not materially prejudice the company's ability to pay its creditors (par (b)); and it is approved by shareholders under s 256C. Sections 256B(2) and (3) distinguish between equal reductions of capital and selective reductions, the former being reductions which applied only to all holders of ordinary shares in the same proportions and on the same terms and the latter being all other reductions. The approval requirements for equal and selective reductions are set out in s 256C and need not be described, except to note that where the reduction involves a cancellation of shares, the reduction must be approved by a special resolution at a meeting of the shareholders whose shares are to be cancelled. A company must not make a reduction of its share capital unless authorised by s 256B (s 256D).

34. In ***Archibald Howie*** *Pty Limited v Commissioner of Stamp Duties (NSW)* (1944) 77 CLR 143 the appellant company made a reduction of capital to the holders of paid up shares to the extent of 19s 6d per £1 share by way of an in-specie distribution of shares in other companies. Both Dixon J and Williams J examined the legal character of a payment made on a reduction of capital. Dixon J observed (152-153):

> A reduction of capital involving the payment off of any paid up share capital, or what is in essence the same thing, the distribution of assets *in specie* in satisfaction of paid up share capital, is a transaction which must be provided for by the articles of association. ... While a shareholder has not a proprietary right or interest in the assets of an incorporated company, his "share" is after all an aliquot proportion of the company's share capital with reference to which he has certain rights. He is entitled among other things to have share capital applied in pursuance of the memorandum and articles of association and, so far as assets are available for the purpose, to have his paid up capital returned in liquidation or **upon a reduction of capital if that method of returning it is decided upon pursuant to the articles of association.** These rights all arise out of the contract *inter socios*. ...
>
> The reduction involving the payment off of part of the paid up share capital must therefore be considered an effectuation of a provision of the contract of membership. The allotment of the share and the payment up of the liability thereon conferred upon the holder for the time being of the share a right to have the assets of the company used and applied in the various ways in which the articles expressly or impliedly require or authorize **and this is one of them. It is an effectuation or realization of the rights obtained by the acquisition of the share in the same way as is the distribution of a dividend**. The consideration given is the payment up of the share capital in satisfaction of the liability for the amount of the share incurred on allotment.

35. Dixon J went on to observe to the effect that a paid up share represented the proportion in which a shareholder shares with other shareholders in a distribution of excess assets (at 153). He then observed that "the return of 19s. 6d. of the amount paid up is the discharge *pro tanto* of a claim of the shareholder upon the assets of the company." Where that claim was discharged by an allocation of assets, Dixon J went on to observe, "that means that the shareholder in satisfaction of his proportionate 'interest' in the assets, an interest consisting of congeries of rights *in personam*, takes an aliquot part of the assets" (at 154).

36. Dixon J's observation in *Archibald Howie* to the effect that a reduction of capital can occur by way of an in-specie distribution in an amount or value measured by reference to the shareholder's right to a return of capital was taken up by Allsop CJ, Middleton and Beach JJ in *Cable & Wireless* at [96] in the following passage (emphasis added):

> Subject to satisfying legislative requirements and a company's constitution, such a reduction can occur out of any assets of a company or any source and may involve a distribution in specie … . But a reduction of capital does not arise simply from or by negative equity or a wasting or deficiency in assets. The amount or value of capital contributed does not itself change as such, although the money originally provided may have been transformed, consumed or lost. **Moreover, that amount or value can also be seen as a standard to measure the right to any return of capital which a company may make either as a going concern or in a winding up** … whatever may have happened to the money originally contributed.

37. In *Archibald Howie* Williams J (at 156) noted the nature of property in a share as "composed of rights and obligations which are defined by the Companies Act and by the memorandum and articles of association". Williams J continued (at 156 – 157, emphasis added):

> Such rights include the right to participate in dividends whilst the company is a going concern and the right to participate in the distribution of assets available for the shareholders upon a winding up. **They also include the right to receive capital in excess of the wants of the company which the company resolves to distribute upon a reduction of capital**. Such a reduction requires to be confirmed by the court mainly to ensure that the creditors will not be prejudiced but also to ensure that the reduction will not operate unfairly between the shareholders. Distributions of profits to shareholders by way of dividend or of capital upon a winding up or upon a reduction of capital are usually made in money. But where the articles so provide in the case of dividends or upon a winding up, and where the special resolution so provides in the case of a reduction of capital, the distribution may be made *in specie*.
>
> Except in the case of a compulsory liquidation, all these distributions originate in a voluntary act on the part of the company. But when the company voluntarily declares a dividend it becomes indebted to the shareholders for the sums they are entitled to be paid. ... When the company goes into voluntary liquidation s.282 of the *Companies Act* provides that the property of the company shall be applied in satisfaction of its liabilities, and subject to that application shall, unless the articles otherwise provide, be distributed among the members according to their rights and interests in the company. **When the company voluntarily passes a special resolution to pay off capital in excess of the wants of the company and the special resolution takes effect, the company becomes indebted to the shareholders to whom the money is payable in the same manner as it becomes indebted upon a declaration of dividend**. ...
>
> A company obtains capital by the issue of shares. … When the person to whom the shares are allotted pays or assumes the liability to pay for the shares in money or money's worth, full consideration in money or money's worth moves from him to the company for all the rights which he acquires under the memorandum or articles of association. Amongst the most valuable of these rights are the rights to share in the distributions of money and assets already mentioned. The declaration of a dividend and the taking effect of a special resolution to return capital create debts because the shareholders have acquired the legal right to be paid these moneys for valuable

> consideration. If the moneys were not payable as debts but as gifts the shareholders would have no legal rights to sue for them. The authorities already cited show that the shareholders have these legal rights. They are legal rights which flow from the original issue of the shares. They are ingredients in the chose in action which each original shareholder purchased from the company.

38. The statutory context provided by the Corps Act is, of course, different from that within which Dixon J and Williams J made their observations in *Archibald Howie*. It remains true, however, that payments made (including by way of in-specie distribution) by a company both by way of dividend and by way of capital reduction represent the satisfaction of rights which are among the congeries of rights which a shareholder has under the statutory contract the terms of which are in the company's constitution (s 140, Corps Act). However, they are rights which have a distinct source and a distinct character. The payment of a dividend represents the satisfaction of shareholders' rights at the "record date", or date fixed for payment, to a distribution of amounts of a non-capital nature determined by the directors in circumstances where the directors have resolved to make that distribution (r. 88) and the distribution complies with the requirements of s 254T of the Corps Act. Sometimes, and in this case, a company's constitution will make provision for the reservation of specific amounts to disclose those amounts as available for dividends and to which the dividend is then debited: cl. 91, EAI Constitution; see further, *Heesh v Baker* (2008) 67 ACSR 192 at [38]-[45] (Barrett J). In contrast, a capital reduction distribution reflects the discharge of the shareholders' claim to the application of the contributed capital of the company where the company has, by the relevant corporate organs (being, in this case, the company in general meeting: EAI Constitution, rr. 30 and 31) and in compliance with the requirements of Part 2J.1 of the Corps Act, decided that its capital is excess to its requirements. This includes cases where the company cancels the shares corresponding to the reduced capital. In such cases, at least in the ordinary course, the capital reduction distribution will be debited to a share capital account: *Cable & Wireless* at [78], [79], [81], [117]. That is what occurred in the present case (see par. 4(f) above).

39. I turn now to address the specific questions on which my opinion has been sought.

Question 1: Was the special dividend part of the capital proceeds for CGT event C2?

40. The first question on which my opinion is sought is whether the special dividend comprises capital proceeds for the CGT event which occurred upon the cancellation of the exiting shareholders' shares in EAI.

41. The cancellation of the EAI shares of exiting shareholders as part of the capital reduction under Part 2J.1 of the Corps Act caused CGT C2 to occur. This is because the exiting shareholders' ownership of a CGT asset, being the EAI shares, ended because those shares were cancelled (s 104-25(1)(a) of the 1997 Act). The capital gain from CGT event C2 is the amount by which the capital proceeds from the ending of the ownership of the asset are more than its cost base; and, the capital loss from CGT event C2 is the amount by which those capital proceeds are less than the reduced cost base (s 104-25(3)).

42. The general rule about capital proceeds is contained in s 116-20(1) which provides as follows:

> **General rules about capital proceeds**
>
> (1) The ***capital proceeds*** from a *CGT event are the total of:
>
> (a) the money you have received, or are entitled to receive, in respect of the event happening; and
>
> (b) the *market value of any other property you have received, or are entitled to receive, in respect of the event happening (worked out as at the time of the event).

43. As the special dividend involved an in-specie distribution of EAGF units, whether those units were part of the capital proceeds from CGT event C2 happening by the cancellation of the EAI shares depends on the application of s 116-20(1)(b) and, in particular, on whether the EAGF units which made up the special dividend are property which the exiting shareholders received "in respect of the event [that is, CGT event C2] happening".

44. In ***South Western Helicopters*** *Pty Limited v Stephenson* (2017) 98 NSWLR 1 at [274] – [279] Leeming JA collected and analysed the authorities concerning the construction of the statutory phrase "in respect of" as follows:

> [274] The meaning of any legal expression which uses the words "in respect of" to specify the terms of a relationship is inevitably contextual. In *Workers' Compensation Board (Q) v Technical Products Pty Ltd* (1988) 165 CLR 642 at 653-654 it was said of the words "in respect of" that "the phrase gathers meaning from the context in which it appears and it is that context which will determine the matters to which it extends". A majority of the High Court approved that passage in *Commissioner of Taxation of the Commonwealth of Australia v Scully* (2000) 201 CLR 148 at [39]. The same point was made in *R v Khazaal* (2012) 246 CLR 601 by French

CJ, who described "in respect of" and other "relational terms" such as "connected with", "in relation to" and "in connection with" at [31]:

> "They may refer to a relationship between two subjects which may be the same or different and may encompass activities, events, persons or things. They may denote relationships which are causal or temporal or relationships of similarity or difference. The task of construing such terms does not involve the resolution of ambiguity. They are ambulatory words and may be designed to cover a variety of subjects and a variety of relationships between those subjects. The nature and breadth of the relationships they cover will depend upon their statutory context and purpose."

[275] French CJ had made the same point in *Kostas v HIA Insurance Services Pty Ltd* (2010) 241 CLR 390 at [24] (citations omitted):

> "The extent of the term 'a question with respect to a matter of law' is controlled by the words 'with respect to'. They are to be read and applied having regard to their legislative context. Like the terms 'in relation to' or 'in connection with', they constitute a 'prepositional phrase' of indefinite content."

[276] … It matters not whether such words are labelled "relational terms" or "prepositional phrases". The point is that the statutory context and purpose will determine the legal meaning of the words "in respect of", and thus the closeness of the relationship required by them. …

[279] … when faced with the task of construing a statute which turns upon a relational term such as "in respect of", its legal meaning is not determined by reference to the broadest meaning which those words may reasonably bear. The legal meaning of a term such as "in respect of" may be, and often will be, when considered in its context and by reference to its purpose, narrower than its maximal meaning considered in isolation.

45. The present context in which the phrase "in respect of" in s 116-20 falls to be applied is for the purposes of a provision (s 104-25) which is directed at identifying gains a taxpayer has made so as to bring them to tax, or identifying losses a taxpayer has suffered so as to enable them to be recognised, from the ending of the ownership of an asset by the cancellation of the asset. In this context, the phrase "in respect of" in s 116-20 is not, in my opinion, to be given what Leeming JA in *South Western Helicopters* referred to as its "maximal meaning" such that any connection between the cancellation of the asset and the receipt of money or property is sufficient to characterise the money or property as "capital proceeds" from the CGT event.

46. Rather, in my opinion, the words "in respect of" in s 116-20 in the present context are directed to identifying money or property which the taxpayer has received *in return for*, or in satisfaction of, the asset the taxpayer's ownership of which has been ended by its cancellation.

This construction of the phrase "in respect of" in s 116-20 in the context of an application of CGT event C2 is consistent with the approach the Commissioner has adopted, albeit in the context of CGT event A1, in **TR 2010/4** "Income Tax: capital gains: when a dividend will be included in the capital proceeds from a disposal of shares that happens under a contract or scheme of arrangement" at [9], [55] and [72].

47. The cancellation of the EAI shares which constituted CGT event C2 occurred pursuant to a decision by EAI in general meeting on 18 May 2023 to reduce its share capital in a manner that was provided for in its Constitution (rr. 30 and 31) and which complied with the requirements of Part 2J.1 of the Corps Act. As Dixon J and Williams J pointed out in *Archibald Howie,* in the passages quoted in par. 34 to 35 and 37 above, that decision gave rise to claims in EAI's shareholders the subject of the capital reduction (ie., the exiting shareholders) to the re-application of EAI's share capital by returning it to them: see also, *Cable & Wireless* at [96], quoted in par. 36 above. Those claims were discharged by the capital reduction distribution. The capital reduction distribution was, in my opinion, that which EAI shareholders received in return for, or in satisfaction of, the ending of their ownership of EAI shares by the cancellation of those shares. This was reflected in the terms of the EM (see par. 17 above) and in the fact that the capital reduction distribution was debited to EAI's share capital account (see par. 4(f) above). The capital reduction distribution, therefore, was property received "in respect of" the happening of CGT event C2 by the cancellation of the EAI share and, accordingly, formed the capital proceeds for that CGT event.

48. In contrast, in my opinion, the special dividend was not something the exiting shareholders received in return for, or in satisfaction of, the ending of their ownership of EAI shares by the cancellation of those shares. It was not, therefore, property received "in respect of" the happening of CGT event C2 by the cancellation of the EAI shares and, thus, did not form part of the capital proceeds from that CGT event. The special dividend represented non-share capital amounts which EAI could distribute consistently with s 254T of the Corps Act. It was a return *on* capital, not *of* capital: *Cable & Wireless* at [51]. The right of EAI shareholders to the special dividend arose as a consequence of the exercise of the powers of the directors of EAI to declare or determine that a dividend be payable (r. 88, EAI Constitution), including by way of a distribution of specific assets (r. 95.1), and EAI shareholders being registered, or entitled to be registered, as the holders of shares at the record date (rr. 92.1 and 92.5). In this case, the "record date" was 29 May 2023 (see par. 31 above). For these reasons, in my opinion, the right to the special dividend, and the receipt of the EAGF units constituting it, were

incidents of the *holding* of EAI shares by EAI shareholders. They were not incidents of the cancellation of the EAI shares following the capital reduction (cf., TR 2010/4 at [55]). It is of significance that, consistently with this characterisation, the special dividend was paid to all EAI shareholders, not only the exiting shareholders (see par. 4(c) above). It is difficult to see how a distribution of property which was made to all EAI shareholders, not only those whose shares were cancelled, can be said to be capital proceeds from the happening of CGT event C2 by the cancellation of those shares.

49. The following factors further support the conclusion that the special dividend was not something the exiting shareholders received in return for, or in satisfaction of, the ending of their ownership of EAI shares by the cancellation of those shares and, therefore, was not property received "in respect of" the happening of CGT event C2 by the cancellation of the EAI shares:

    (a) The special dividend was debited to a dividend profits reserve which the directors had established under r. 91 of EAI's Constitution (see par. 11 above). That was, therefore, an amount which it would be expected would have been distributed to EAI's shareholders in any event: cf., TR 2010/4 at [35] and [59]. In this connection, it may also be noted that EAI has since 2021 paid half-yearly dividends of 3c a share. The value of the special dividend was around 8c per share (see par. 4(e) above) and was, therefore, in line with EAI's historical dividend policy.

    (b) Further to the first point, there is nothing in the present circumstances analogous to the facts the subject of *Chief Commissioner of Stamp Duties (NSW) v* ***Dick Smith*** *Electronics Holding Pty Limited* (2005) 221 CLR 496 in which a purchaser of shares in a company, as an aspect of the agreement for purchase, put the company in funds to pay a dividend to the vendor of the shares in the company: cf., TR 2010/4 at [61]-[72].

    (c) While the special dividend and the capital reduction distribution together formed the in-specie distribution and were both aspects of a single Transaction which were contemplated to occur, and did occur, at the same time, the resolutions approving the capital reduction distribution and consequent cancelling of the shares of the exiting shareholders were not expressed to be conditional on the payment of the special dividend (see par. 20 above): cf., TR 2010/4 at [10]-[11], [24] and [56]-[57].

50. For these reasons, the answer to the first question on which my opinion has been sought is "No".

Question 2: Was the special dividend consideration for the cancellation of the EAI shares?

51. The second question on which my opinion is sought directs attention to the proposed s 202-45(k) of the 1997 Act which appears in Item 19 of Part 2 of Schedule 4 of the 2023 Bill. That proposed provision will add the following to the list of unfrankable distributions in s 202-45:

> a distribution by a listed public company that is consideration for the cancellation of a membership interest in the company as part of a selective reduction of capital, including a selective reduction of capital within the meaning of section 256B of the *Corporations Act 2001*.

52. My opinion is sought on whether the special dividend was a distribution that was consideration for the cancellation of the EAI shares as part of the selective reduction of capital under s 256B of the Corps Act within the meaning of the proposed s 202-45(k) of the 1997 Act.

53. The Explanatory Memorandum to the 2023 Bill (**2023 Bill EM**) describes the proposed s 202-45(k) of the 1997 Act in the following terms (at [4.25] and [4.27]):

> … This is an integrity measure designed to prevent companies using selective reductions of capital as an alternative way to take advantage of the concessional tax status of shareholders as part of their capital management activities …
>
> The reference to a 'selective reduction of capital' is intended to be broad and to take its ordinary meaning, so as to include reductions of capital effected through selective cancellations of non-share equity interests and other reductions of capital that in substance result in a disproportionate cancellation of membership interests.

54. In my opinion, the phrase "consideration for" in the proposed s 202-45(k) of the 1997 Act should be construed consistently with the observations of Gummow, Kirby and Hayne JJ at [71] – [72] of *Dick Smith*. Those observations were made in the context of the phrase "consideration for" in s 21(1) of the *Duties Act 1997* (NSW) and were as follows (emphasis added):

> [71] It was accepted by both parties that, consistent with this Court's decisions in *Archibald Howie Pty Ltd v Commissioner of Stamp Duties (NSW)* and *Davis Investments Pty Ltd v Commissioner of Stamp Duties (NSW)* on earlier stamp duty legislation of New South

> Wales, "consideration" in s21 of the Act is not to be read as requiring identification of the consideration sufficient to support a contract. So much follows inevitably from the recognition of the fact that s21(1)(a) (and the expression "the consideration ... for the dutiable transaction") will find application in cases in which a transfer of dutiable property is not made pursuant to contract. So, as Dixon J pointed out in *Archibald Howie*:
>
> > "the word 'consideration' should receive the wider meaning or operation that belongs to it in conveyancing rather than the more precise meaning of the law of simple contracts".
>
> That is, as his Honour went on to say, "the consideration is rather the money or value passing **which moves the conveyance or transfer**".
>
> [72] To adapt what was said by Lord Wilberforce of other stamp duty legislation [***Shop and Store Developments*** *Ltd v Commissioners of Inland Revenue* [1967] 1 AC 472 at 503]:
>
> > "In the first place, the phrase 'consideration for the transfer or conveyance' seems to me to refer clearly and naturally to that which passed to the transferor company 'for' the transferred properties."
>
> The criterion in the Act of consideration "for" the transaction, being the Agreement for the sale and transfer of the Shares to the Purchaser, upon whom s 13 imposes the liability to pay the duty, looks to what was received by the Vendors **so as to move the transfers** to the Purchaser as stipulated in the Agreement.

55. At footnote 37 of [72] of their judgment in *Dick Smith*, Gummow, Kirby and Hayne JJ referred with approval to the observation of Lord Hodson at 498 of *Shop and Store Developments* where his Lordship observed that "[w]hatever extended meaning is given to 'consideration' it must represent a quid pro quo for that which passed by the transfer or conveyance".

56. Consistently with the approach of the majority in *Dick Smith,* in my opinion, when the proposed s 202-45(k) of the 1997 Act refers to "consideration for the cancellation of the membership interest in a company" it is referring to that which moves the cancellation of the membership interest; or, to put it another way, that which was the quid pro quo for the cancellation of the membership interest.

57. For much the same reasons as appear at pars. 47 to 49 above, in my opinion, the special dividend was not consideration for the cancellation of the EAI shares which occurred by reason of the capital reduction under Part 2J.1 of the Corps Act. That which moved, or the quid pro

quo for, the cancellation of the EAI shares was the satisfaction of the claims of the exiting shareholders to the reapplication of their contributed capital which arose on the decision to reduce the share capital of EAI. Those claims were discharged by the capital reduction distribution made to the exiting shareholders which was debited to the share capital account. Moreover, that is how the matter was expressed to shareholders in the EM (see par. 17 above). In contrast, the special dividend was paid to all EAI shareholders (not just those whose shares were being cancelled) to discharge the entitlements which had arisen under EAI's Constitution arising from the resolution of the directors of EAI to pay the dividend to EAI's shareholders on the "record date" of 29 May 2023 and was debited to an account reserved for dividend distributions.

58. While the special dividend occurred at the time of, and as part of, a single transaction (the Transaction), which also involved the cancellation of the EAI shares, that is insufficient, in my opinion, to support the conclusion that the special dividend was part of that which moved the cancellation of the EAI shares, or was part of the quid pro quo for it, so as to constitute the "consideration for" the cancellation. The additional factors which may support a conclusion to that effect (such as those present in *Dick Smith:* see par. 49(a) above) are absent in this case.

59. For these reasons, in my opinion, the answer to the second question on which my opinion has been sought is "No".

60. In *Commissioner of Taxation v* ***Scully*** (2000) 201 CLR 148 the majority (Gaudron A-CJ, McHugh, Gummow and Callinan JJ) construed the phrase "consideration of a capital nature for, or in respect, of personal injury to the taxpayer" in par. (n) of the definition of "eligible termination payment" in s 27A(1) of the *Income Tax Assessment Act 1936* (Cth) as involving a "notion of recompense" or "compensation" (at [29]). The context in which the phrase "consideration for, or in respect of" appeared in *Scully* is, of course, significantly different to the context in which the phrase "consideration for" appears in the proposed s 202-45(k) of the 1997 Act. In my opinion, the notions of "recompense" or "compensation" referred to in *Scully* fit the latter context less well than the notions of consideration which are reflected in the passages in *Dick Smith* extracted in par. 54 above. The notion of "re-imbursement", which is also referred to at [25] of *Scully* as among the standard meanings of "consideration", may be more apt for context of s 202-45(k) than the notions of "recompense" or "compensation", but has no different effect, in my opinion, to the construction of the phrase "consideration for" arrived at in *Dick Smith*.

61. At all events, even if the phrase "consideration for" in the proposed s 202-45(k) is construed, in accordance with *Scully*, as involving a "notion of recompense", or "compensation" or "re-imbursement", for the same reasons as are given in par. 57 to 58 above, in my opinion, the recompense, compensation or re-imbursement received by exiting shareholders for the cancellation of their EAI shares was the capital reduction distribution and was not the special dividend (which was paid to all EAI shareholders and debited to an account reserved for that purpose).

62. Moreover, it is difficult to see how the special dividend engages the tax mischief to which the passages from the 2023 Bill EM quoted in par. 53 above indicate the proposed s 202-45(k) of the 1997 Act is directed. Those passages indicate that s 202-45(k) is directed to circumstances in which the distribution which is consideration for the selective capital reduction is received disproportionately to take advantage of the concessional tax status of some shareholders. That is, the paragraph contemplates an alignment between the selectivity of the capital reduction and the selectivity which attends the distribution. However, in the present case, the special dividend was received by all EAI shareholders. No question of disproportionate receipt of the special dividend arises. This re-inforces the conclusion that the special dividend was not consideration for the cancellation of the shares of exiting shareholders which occurred as a result of the selective reduction of capital under Part 2J.1 of the Corps Act.

Conclusion:

63. The questions on which my opinion has been sought and my short answers to them appear at par. 5 above.

I so advise.

Michael O'Meara SC
Sixth Floor, Selborne / Wentworth Chambers
28 August 2023