FEDERAL COURT OF AUSTRALIA

Cable & Wireless Australia & Pacific Holding BV (in liquidatie) v Commissioner of Taxation [2017] FCAFC 71

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| Appeal from: | *Cable & Wireless Australia & Pacific Holding BV (in liquidation) v Commissioner of Taxation* [2016] FCA 78 |
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| File number: |  |
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| Judges: | **ALLSOP CJ, MIDDLETON AND BEACH JJ** |
|  |  |
| Date of judgment: | 1 May 2017 |
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| Catchwords: | **TAXATION** – share buy-back – dividend withholding tax payable by non-resident – part of off-market purchase price deemed to be dividend – part of purchase price debited against amounts standing to the credit of the share capital account of the company is not dividend – application for refund of withholding tax claimed to have been paid in error – share capital account – buy-back reserve account – whether record of transaction into which company had entered in relation to share capital – whether record of financial position of the company in relation to its share capital – substance and form of share buy-back transaction – appeal dismissed |
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| Legislation: | *Corporations Act 2001* (Cth) ss 256A-258F  *Income Tax Assessment Act 1936* (Cth) ss 6, 6D, 128B, 128C, 159GZZZP  *Taxation Administration Act 1953* (Cth) ss 12-210, 18-70 of Schedule 1 |
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| Cases cited: | *Archibald Howie Pty Ltd v Commissioner of Stamp Duties (NSW)* (1948) 77 CLR 143  *Commissioner of Taxation v Consolidated Media Holdings Limited* (2012) 250 CLR 503  *Re Westburgh Sugar Refineries Ltd* [1951] AC 625 |
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| Date of hearing: | 21 November 2016 |
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| Registry: | New South Wales |
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| Division: | General Division |
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| National Practice Area: | Taxation |
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| Category: | Catchwords |
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| Number of paragraphs: | 151 |
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| Counsel for the Appellant: | Mr B J Sullivan SC with Mr B L Jones and Mr T O Prince |
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| Solicitor for the Appellant: | Ernst & Young Law Pty Ltd |
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| Counsel for the Respondent: | Mr J O Hmelnitsky SC with Ms C A Burnett and Mr M A Cosgrove |
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| Solicitor for the Respondent: | Australian Government Solicitor |

ORDERS

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|  | | NSD 318 of 2016 |
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| BETWEEN: | CABLE & WIRELESS AUSTRALIA & PACIFIC HOLDING BV (IN LIQUIDATIE)  Appellant | |
| AND: | THE COMMISSIONER OF TAXATION OF THE COMMONWEALTH OF AUSTRALIA  Respondent | |

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| JUDGES: | ALLSOP CJ, MIDDLETON AND BEACH JJ |
| DATE OF ORDER: | 1 MAY 2017 |

THE COURT ORDERS THAT:

1. The appeal be dismissed with costs.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

REASONS FOR JUDGMENT

THE COURT:

1. The issue the subject of the present appeal relates to the correct characterisation for taxation purposes of an amount of $3,918,797,343.42 debited to a buy-back reserve account in the ledger of Cable & Wireless Optus Ltd, now known as Singtel Optus Australia Pty Ltd (Optus). The amount debited to the buy-back reserve account was part of the consideration paid by Optus to buy back approximately 43% of its shares on 6 and 28 September 2001; the buy-back was part of a takeover of Optus, with the acquirer putting Optus in funds to enable the consideration for the buy-back to be paid. Depending upon the correct characterisation of the amount debited to the buy-back reserve account, the appellant may be entitled to a refund from the Commissioner of Taxation of $452,452,013 in dividend withholding tax. Let us explain.
2. Prior to 6 September 2001, the appellant, a company incorporated in the Netherlands and not a resident of Australia, had been a shareholder in Optus and had held approximately 52% of shares in Optus. On 18 May 2001, Singapore Telecommunications Limited (SingTel) through its wholly owned subsidiary made a takeover offer for a majority of the shares in Optus. The takeover offer contained a number of transaction alternatives available to an accepting shareholder of Optus, including the appellant. An accepting shareholder could receive consideration by way of cash, bonds or SingTel shares. Further, an accepting shareholder could elect to accept either a purchase of its shares by the bidder *or* a buy-back by Optus of the accepting shareholder’s shares in Optus.
3. The takeover was successful. The appellant elected to accept a buy-back by Optus of most of its shares in Optus. On 30 August 2001, the appellant accepted the buy-back option in respect of 1,639,849,948 shares (it had a total holding of 1,981,382,291 shares) for a consideration of $6,216,762,899.29. In total, Optus agreed to buy back 1,642,101,319 shares from relevant accepting shareholders for a total consideration of $6,225,502,631.68. In the financial statements of Optus, the buy-back was accounted for in the following manner:

Dr Contributed Equity $2,306,705,228.16

Dr Buy-Back Reserve $3,918,797,403.52

Cr Debt due to Optus shareholders $6,225,502,631.68

1. The appellant contends that the buy-back reserve account was a “share capital account” within the meaning of s 6D of the *Income Tax Assessment Act 1936* (Cth) (ITAA). If that characterisation is correct, then the amount debited to that account referable to the payment to the appellant for the shares bought back by Optus is *not* taken to be a dividend paid by Optus as provided for by s 159GZZZP of the ITAA. And if that is correct, then the appellant was not obliged to pay dividend withholding tax of $452,452,013. That being the case, the appellant says that it is entitled to a refund of $452,452,013, which has been erroneously withheld as such tax, pursuant to s 18-70 of Schedule 1 to the *Taxation Administration Act 1953* (Cth) (TAA). It says that such an amount was withheld from the appellant and paid to the Commissioner in “error”. The appellant’s position is sought to be justified as a consequence of the High Court’s decision on 5 December 2012 in *Commissioner of Taxation v Consolidated Media Holdings Limited* (2012) 250 CLR 503.
2. Contrastingly, the Commissioner contends that no error has been made, that the buy-back reserve account is not a “share capital account” within the meaning of s 6D of the ITAA, and that *Consolidated Media* is distinguishable. Principally, it contends that *Consolidated Media* was concerned with a buy-back reserve account used to effect a reduction of capital, in contrast with the present case where the buy-back reserve account was not used to effect a reduction of capital.
3. The primary judge largely accepted the Commissioner’s submissions and accordingly dismissed the appellant’s proceeding, being in the form of an appeal by the appellant against an appealable objection decision under s 14ZZ of the TAA. The appealable objection decision made by the Commissioner under s 14ZY of the TAA was one which disallowed the appellant’s objection against the Commissioner’s decision to refuse a refund under s 18-70 of Schedule 1 to the TAA. The appellant has appealed the primary judge’s determination.
4. For the reasons that follow, we would dismiss the appeal.

# Background

1. Throughout 2001 and up to 6 September 2001, Optus had 3,786,766,521 shares on issue, which shares were listed for quotation on the Australian Stock Exchange.
2. Throughout 2001 and up to 6 September 2001, the appellant owned approximately 52% of those shares and was accordingly the majority shareholder in and effective controller of Optus. The balance of 48% of those shares was held by numerous other shareholders.
3. On 25 March 2001, SingTel entered into an Implementation Agreement with Optus with respect to implementing a transaction under which Optus shareholders would be invited by the bidder (a subsidiary of SingTel or SingTel itself) to dispose of their Optus shares.
4. On 18 May 2001, SingTel entered into an amending agreement to the Implementation Agreement; for convenience, we will refer to the Implementation Agreement (as so amended) as the “Implementation Agreement”.
5. Relevant provisions of the Implementation Agreement were the following:
   1. Clause 1.1 contained definitions of “Buy-Back”, “Buy-Back Agreement”, “Buy-Back Alternative”, “Buy-Back Consideration” and “Buy-Back Offer” in the following terms:

“**Buy-Back**” means a selective off market buy-back of Optus Shares to be implemented in compliance with Division 2 of Part 2J.1 of the Corporations Law.

“**Buy-Back Agreement**” means an agreement in the form set out in Schedule 4 between Optus and each Optus Shareholder who accepts the Offer and chooses the Buy-Back Alternative and which will be entered into and formed upon acceptance by Optus of that shareholder’s Buy-Back Offer.

“**Buy-Back Alternative**” is defined in clause 3.7(a)(ii).

“**Buy-Back Consideration**” is defined in clause 4.5(a).

“**Buy-Back Offer**” means an offer made by an Optus Shareholder to Optus to sell all or any of its Optus Shares to Optus on the terms of the Buy-Back Agreement which offer is constituted by that shareholder’s acceptance of the Offer and election of the Buy-Back Alternative.

* 1. Clause 1.1 also contained definitions of “Transaction” and “Withholding Tax” in the following terms:

“**Transaction**” means the implementation of the Takeover Bid, the Buy-Back and the Placement on the terms of this agreement.

“**Withholding Tax**” means, in respect of a payment to an Optus Shareholder or its agent, amounts required to be paid to the Australian Taxation Office pursuant to Part 2-5 of Schedule 1 of the Taxation Administration Act 1953 and other amounts required to be withheld from any payment in accordance with a provision of the Taxation Administration Act 1953, the Income Tax Assessment Act 1997 or the Income Tax Assessment Act 1936.

* 1. Clause 2.1 provided:

**2.1 Proposal of Transaction**

SingTel has proposed the Transaction to Optus. The Transaction has been formulated by SingTel to meet its commercial objectives.

* 1. Clauses 3.1, 3.2 and 3.7 to 3.9 provided:

**3.1 Offer by Bidder**

Bidder shall make Offers to all Optus Shareholders in respect of all of their Optus Shares on the terms set out in this agreement and in compliance with the Corporations Law (as modified or exempted).

**3.2 Consideration**

(a) Pursuant to the Offer, Optus Shareholders will be invited to dispose of their Optus Shares for one of the following forms of consideration (the “**Offer Consideration**”) as the shareholder elects from the following menu:

(i) 1.66 SingTel Shares for each Optus Share;

(ii) A$2.25 cash (or the US$ Cash Alternative) and 0.8 SingTel Shares for each Optus Share; or

(iii) A$2.00 cash (or the US$ Cash Alternative) and A$0.45 worth of Bonds (determined by reference to the Bond Issue Price) and 1 Unsecured Note for each Optus Share.

(b) If an Optus Shareholder does not make an election regarding the Offer Consideration it wishes to receive, or if it makes conflicting elections, the shareholder will be deemed to have elected the Offer Consideration described in clause 3.2(a)(ii).

(c) If the number of SingTel Shares to be issued to an Optus Shareholder as a result of acceptance of an Offer by that shareholder is not a whole number, the number of SingTel Shares issued to that shareholder will be rounded up to the nearest whole number.

**3.7 Alternative disposal mechanisms**

(a) Subject to clause 3.11(b), Bidder must ensure that, pursuant to the Offer, each Optus Shareholder will be given the choice to dispose of all or any of its Optus Shares by either:

(i) selling and transferring all or any of its Optus Shares to Bidder under the Takeover Bid (the “**Transfer Alternative**”); or

(ii) having all or any of its Optus Shares bought back by Optus under the Buy-Back (the “**Buy-Back Alternative**”),

and an Optus Shareholder may elect the Transfer Alternative for some of its Optus Shares and the Buy-Back Alternative for others.

(b) If an Optus Shareholder fails to make an election regarding the disposal mechanism, or if it makes conflicting elections, the shareholder will be deemed to have elected the Transfer Alternative.

**3.8 Appointment of Bidder as Optus Shareholders’ agent**

Bidder must ensure that each Optus Shareholder who accepts the Offer and chooses the Buy-Back Alternative will irrevocably appoint Bidder as the shareholder’s exclusive agent, with irrevocable instructions:

(a) to enter into a Buy-Back Agreement on behalf of that shareholder; and

(b) to present the Cheque which the Optus Shareholder has received pursuant to clause 4.5(b)(ii) to Optus for purchase accordance with clause 4.7; and

(c) to perform all other actions on behalf of that shareholder necessary to give effect to the terms of the Buy-Back Agreement, and that redemption,

and Bidder accepts that appointment and will do all things necessary to fulfil those instructions. Bidder must ensure that the terms of Bidder’s appointment as agent include terms stating that Bidder, in its role as agent, is permitted to perform actions which will give a commercial benefit to Bidder.

**3.9 Bidder to receive Buy-Back Offers**

Optus agrees that receipt by Bidder of an acceptance form from an Optus Shareholder who has elected the Buy-Back Alternative will constitute receipt by Optus of a Buy-Back Offer made by that shareholder.

* 1. Clauses 4.2 to 4.6 provided:

**4.2 Settlement Dates**

SingTel and Bidder must ensure that each Optus Shareholder who accepts the Offer, whether the Optus Shareholder chooses the Transfer Alternative or the Buy-Back Alternative, will receive the Offer Consideration due to be paid to that shareholder (in the latter case, net of Withholding Tax pursuant to the mechanism described in clause 4.5), as follows:

(a) for each Optus Shareholder who accepts the Offer prior to the Unconditional Date, on the day which is 7 days after the Unconditional Date (the “**First Settlement Date**”);

(b) for each Optus Shareholder who accepts the Offer after the Unconditional Date, on a date nominated by Bidder to Optus (“**Second Settlement Date**”) which is no later than the earlier of:

(i) one month after the later of acceptance of the Offer by the Optus Shareholder and the Unconditional Date; and

(ii) 21 days after the end of the Offer Period.

Bidder may nominate more than one Second Settlement Date under this clause 4.2(b). The Settlement Date for a particular acceptance by an Optus Shareholder must not occur until at least 5 Business Days after the date of acceptance by that shareholder.

**4.3 The Buy-Back Alternative**

(a) Bidder, as agent for each Optus Shareholder, must prepare a Buy-Back Agreement for each Optus Shareholder who elects the Buy-Back Alternative in respect of each Settlement Date on which Optus is required to accept Buy-Back Offers, completing all relevant details of those agreements in accordance with this agreement and in a form suitable for execution by Optus.

(b) In relation to each Optus Shareholder who accepts the Offer and elects the Buy-Back Alternative, and who therefore makes a Buy-Back Offer, Optus must, on the first applicable Settlement Date following the later of the day on which an Optus Shareholder makes a Buy-Back Offer and the Unconditional Date:

(i) enter into a Buy-Back Agreement with that Optus Shareholder in respect of all Optus Shares in respect of which the Buy-Back Alternative has been chosen by the Optus Shareholder (and, as contemplated by clause 3.8, Bidder will act as agent for the Optus Shareholder) by executing the draft agreements referred to in paragraph (a); and

(ii) pay the Buy-Back Consideration payable to each Optus Shareholder who enters into a Buy-Back Agreement in accordance with clause 4.5; and

(iii) accept a transfer of the relevant Optus Shares.

(c) Optus must use all reasonable endeavours to register the transfer of the relevant Optus Shares to Optus on the relevant Settlement Date or, if that is not reasonably practicable, as soon as reasonably possible after the relevant Settlement Date. In accordance with section 257H(3) of the Corporations Law, the Optus Shares are cancelled immediately after registration of the transfer to Optus.

**4.4 Withholding Tax**

On each Settlement Date, before Optus draws a Cheque, Lender must lend to Optus an amount equal to the sum of:

(a) amounts which are required to discharge Optus’ obligation to pay Withholding Tax (if any) in relation to the completion of any Buy-Back Agreement which Optus enters into as part of the Transaction; and

(b) any fees, duties, levies, taxes or charges which are or will be incurred by Optus in connection with the existence or operation of the bank account described below as it relates to the Transaction,

by crediting a bank account of Optus at the Nominated Bank on that date in immediately available funds.

**4.5 Buy-Back Consideration**

(a) The consideration payable by Optus to each Optus Shareholder who enters into a Buy-Back Agreement will be an amount equal to the sum of the following (the “**Buy-Back Consideration**”):

(i) the cash component of the Offer Consideration due to be paid to the Optus Shareholder (if any) calculated as:

(A) the A$ amount; or

(B) the A$ Equivalent of the US$ Cash Alternative; and

(ii) the A$ Equivalent of the aggregate US$ amount of the Bond Issue Prices (calculated by applying the Announcement Exchange Rate) of the Bond component of the Offer Consideration due to be issued to the Optus Shareholder (if any);

(iii) the A$ Equivalent of the Market Value of the SingTel Shares component of the Offer Consideration due to be issued to the Optus Shareholder (if any); and

(iv) the Initial Redemption Amount of the Unsecured Notes component of the Offer Consideration due to be issued to the Optus Shareholders (if any).

(b) Optus will pay the Buy-Back Consideration to each Optus Shareholder who enters into a Buy-Back Agreement by:

(i) firstly, paying the amount of any Withholding Tax to the Australian Tax Office; and

(ii) secondly, delivering a Cheque in favour of the Optus Shareholder or order for an A$ face amount equal to the Buy-Back Consideration less the amount of any Withholding Tax to the Optus Shareholder’s agent, Bidder.

**4.6 Lender to advance monies to Optus**

(a) On each Settlement Date, before Optus draws a Cheque, Lender must lend to Optus an amount equal to the sum of:

(i) the amounts which are required by Optus to pay in full the Cheques to be issued in accordance with clause 4.5(b)(ii); and

(ii) any fees, duties, levies, taxes or charges which are or will be incurred by Optus in connection with the existence or operation of Optus’ Account as it relates to the Transaction,

by crediting Optus’ Account on that date in immediately available funds.

(b) In its role as agent, Lender agrees it will not take any action which is not contemplated by this agreement and its role as agent is limited accordingly.

* 1. Clauses 4.9, 4.12 and 4.13 provided:

**4.9 Subordination of debt due to Lender**

The amounts lent to Optus under clauses 4.4 and 4.6 together with any interest on that amount (the “**Subordinated Debt**”) shall be:

(a) subordinated to all other indebtedness of Optus on the terms set out in the Subordination Deed; and

(b) denominated in Australian dollars.

**4.12 Withholding Tax calculation**

Following an acceptance of an Offer by an Optus Shareholder who chooses the Buy-Back Alternative, the parties must consult with the Australian Taxation Office and use all reasonable endeavours to obtain confirmation from the Australian Taxation Office of the basis of the calculation of Withholding Tax for that shareholder.

**4.13 Buy-Back Agreement Undertakings**

Bidder undertakes to Optus to ensure that, in respect of each Optus Shareholder (“**Relevant Shareholder**”) for whom Bidder has prepared a Buy-Back Agreement under clause 4.3(a):

(a) Bidder will have been duly authorised by the Relevant Shareholder to enter into the Buy-Back Agreement on behalf of the Relevant Shareholder and to endorse any Cheque drawn in favour of the Relevant Shareholder in favour of Optus; and

(b) the consideration set out in Schedule A to the Buy-Back Agreement in respect of each parcel of Optus Shares:

(i) will conform with the terms of clause 4.5 of this agreement; and

(ii) will be in accordance with the election made by the Relevant Shareholder when the Relevant Shareholder accepted the Offer;

(c) the Relevant Shareholder will have applied to SingTel (or other issuer) to subscribe for SingTel Shares, Bonds and Unsecured Notes in accordance with the Relevant Shareholder’s election and this agreement; and

(d) SingTel (or other issuer) will have agreed to issue SingTel Shares, Bonds and Unsecured Notes to the Relevant Shareholder in accordance with this agreement.

* 1. Clauses 5.1 to 5.5 provided:

**5.1 Compulsory placement**

If:

(a) at the end of the Offer Period Bidder is not entitled to proceed with Compulsory Acquisition; or

(b) a Section 661E order is made disallowing Compulsory Acquisition and that order is not capable of further legal challenge; and

(c) no Insolvency Event subsists in relation to Optus,

Bidder may, and must if required by Optus, subscribe for one Optus Share for each Optus Share bought back under a Buy-Back Agreement. The Placement made under this clause must take place on the final Settlement Date.

**5.2 Optional placement**

If at the end of the Offer Period Bidder is entitled to proceed with Compulsory Acquisition, Bidder may at its option subscribe for Optus Shares pursuant to a Placement. The Placement must take place no earlier than 7 days after the final Settlement Date.

**5.3 Subscription for Optus Shares**

To effect the subscription for Optus Shares under a Placement:

(a) any Optus Shares issued will be issued at a subscription price per share equal to the total Buy-Back Consideration divided by the total number of Optus Shares bought back; and

(b) for any Optus Shares issued, Bidder will draw a cheque guaranteed by SingTel, by endorsement, in favour of Optus for an amount equal to the subscription price for the Optus Shares.

**5.4 Repayment of Subordinated Debt**

Optus will use the funds subscribed for Optus Shares under the Placement to repay an equal amount of Subordinated Debt. It will do this by endorsing the cheque referred to in clause 5.3(b) to Lender in satisfaction (or partial satisfaction to the extent of the subscription price) of the Subordinated Debt.

**5.5 Balance of Subordinated Debt**

The Subordinated Debt must not be charged and will not bear any interest during any period when the Bidder holds less than 100% of the Optus Shares. If and when Bidder holds 100% of Optus Shares, any remaining Subordinated Debt shall bear interest at commercial rates of interest to be agreed between SingTel and Optus from time to time.

* 1. Clause 6 provided:

**6 ACCOUNTING FOR THE BUY-BACK**

Subject to the Corporations Law, Optus must account for the Buy-Back, including all the transactions referred to in clauses 4 and 5 required to be undertaken by Optus, in accordance with the pro-forma accounting entries set out in Schedule B of the Buy-Back Agreement.

1. Schedule 4 to the Implementation Agreement set out the Terms of Buy-Back Agreement. As to the content thereof:

(a) The Recitals were as follows:

**RECITALS**

A. Each Relevant Shareholder has accepted the Offer and has chosen the Buy-Back Alternative in respect of the parcel of Optus Shares set out beside that shareholder’s name in Schedule A (the “Relevant Shares”).

B. Pursuant to the terms of the Offer, each Relevant Shareholder has appointed Bidder as its agent to enter into this agreement and to perform all other actions necessary to give effect to this agreement.

C. By choosing the Buy-Back Alternative, each Relevant Shareholder has made a Buy-Back Offer to Optus whereby that Relevant Shareholder has offered to sell to Optus its Relevant Shares on the terms of this agreement.

D. Optus accepts the Buy-Back Offer from each Relevant Shareholder and agrees to Buy-Back the Relevant Shares on the terms of this agreement.

(b) Clauses 2, 3, 4, 5 and 6 provided:

**2. Sale and purchase**

Each Relevant Shareholder hereby sells to Optus, and Optus hereby purchases from that Relevant Shareholder, its Relevant Shares for the consideration set out in Clause 3.

**3. Buy-Back Consideration**

(a) The consideration payable by Optus to each Relevant Shareholder is an amount equal to the A$ Buy-Back Consideration for that Relevant Shareholder determined under clause 4.5(a) of the Implementation Agreement.

(b) Optus will pay the Buy-Back Consideration to each Relevant Shareholder by:

(i) firstly, paying the amount of any Withholding Tax to the Australian Taxation Office; and

(ii) secondly, delivering a Cheque in A$ equal to the Buy-Back Consideration less the amount of any Withholding Tax.

**4. Cheques**

Each Relevant Shareholder directs Optus to deliver the Cheque to which it is entitled pursuant to clause 3 to Bidder, as agent for that Relevant Shareholder. Each Relevant Shareholder acknowledges that this will discharge Optus’ obligation to that shareholder to provide the Buy-Back Consideration.

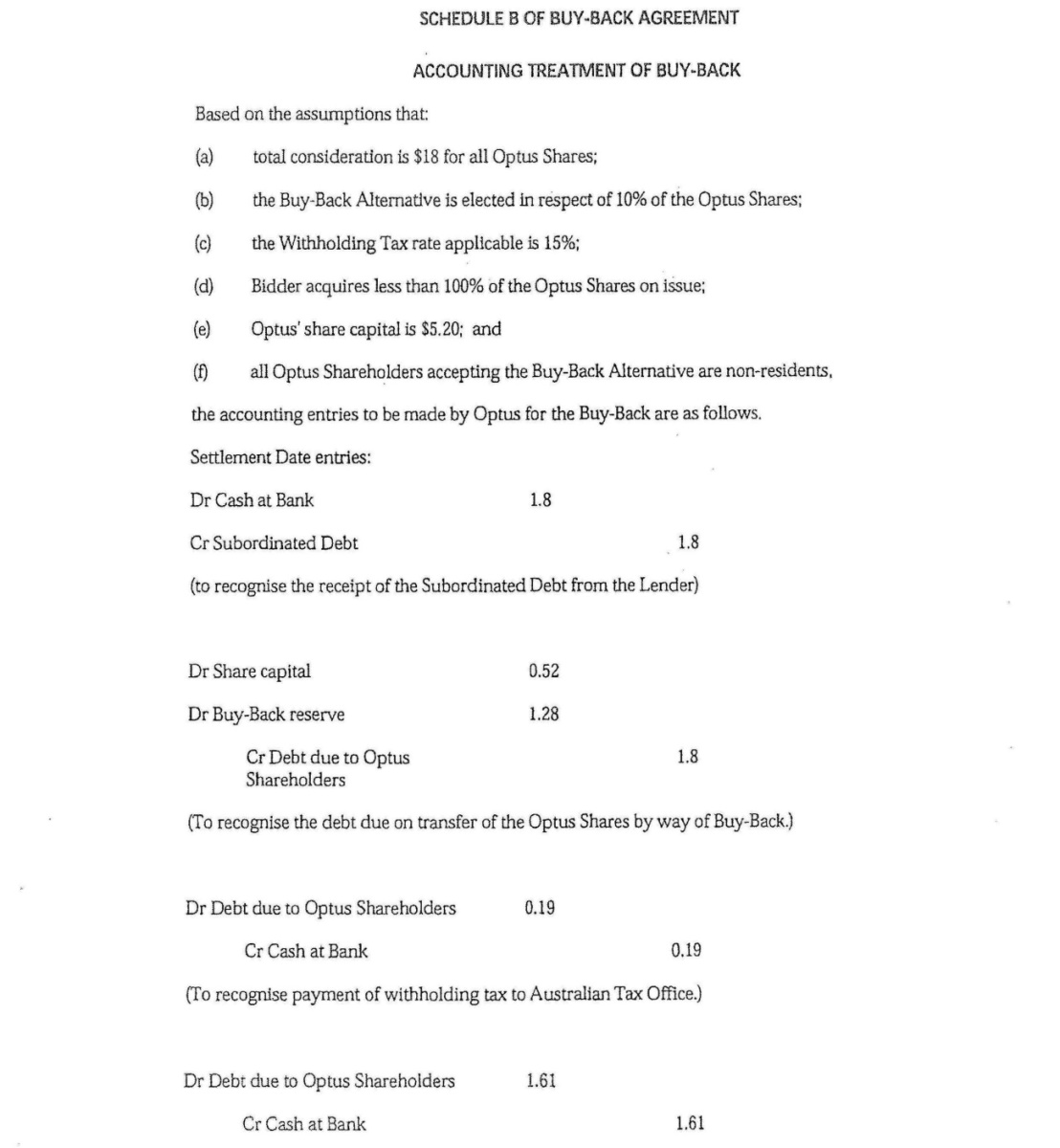
**5. Withholding Tax**

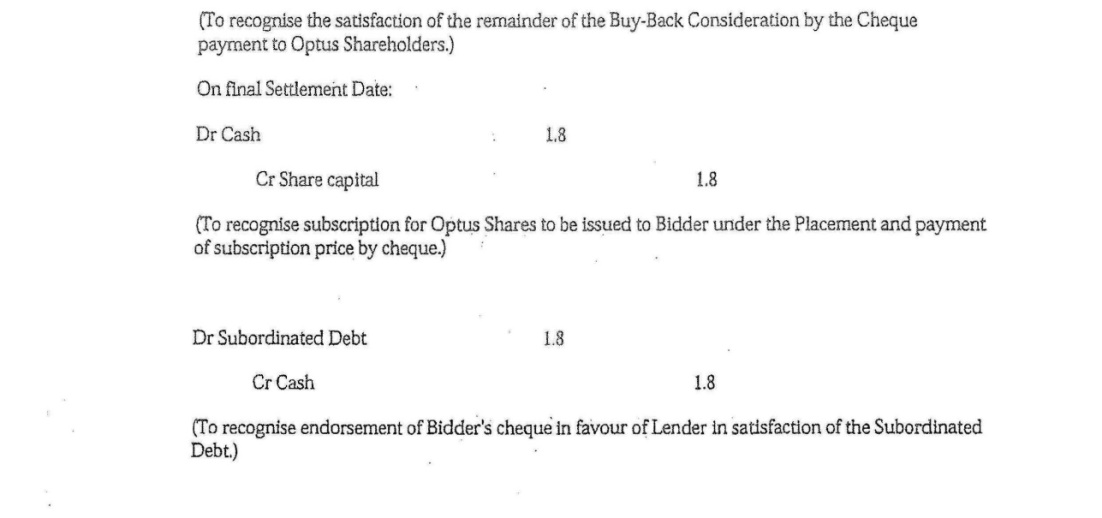
Each Relevant Shareholder acknowledges and agrees that Optus may withhold from the Buy-Back Consideration due to be paid to that shareholder the amount of any Withholding Tax.

**6. Accounting**

Subject to the Corporations Law, Optus must account for the Buy-Back in accordance with the pro-forma accounting entries set out in Schedule B.

(c) Schedule B of the Buy-Back Agreement was in the following terms:





1. Schedule 6 to the Implementation Agreement set out the form of the Buy-Back Deed Poll. Clauses 2 and 3 thereof were in the following terms:

**2. Undertaking to buy-back**

Subject to the Corporations Law and to the conditions in clause 3, Optus unconditionally and irrevocably undertakes to each Optus Shareholder who accepts the Offer and chooses the Buy-Back Alternative that Optus will (as and when required by the Implementation Agreement) enter into and complete a Buy-Back Agreement with each such Optus Shareholder under which Optus will purchase from that Optus Shareholder the Optus Shares in respect of which that Optus Shareholder chooses the Buy-Back Alternative.

**3. Condition**

The conditions referred to in clause 2 are that:

(a) at any time during or at the end of the Offer Period, Bidder receives acceptances in respect of more than 50% (by number) of the Optus Shares; and

(b) all other defeating conditions of the Offer (being those to be set out in the Offer) are fulfilled, or Bidder declares the Offer to be free of all such conditions which have not been fulfilled.

1. Before proceeding further, we note at this point that the Implementation Agreement reflected a number of salient features:
   1. First, the buy-back option element appears to have been suggested by SingTel and formulated to meet its objectives (see cl 2.1; “Transaction” includes the “Buy-Back”).
   2. Secondly, any shareholder who chose the buy-back option appointed the bidder as that shareholder’s agent to enter into the Buy-Back Agreement with Optus and to carry out any necessary steps on the part of the shareholder to effect or perform the buy-back (cl 3.8). In other words, the bidder, albeit as agent of the relevant shareholder, was in control of the buy-back mechanism process from the shareholder’s perspective. Further, and by way of reinforcement, receipt by the bidder of an acceptance form from a shareholder who had elected the buy-back option was taken to be receipt by Optus of a buy-back offer (cl 3.9). It is apparent from provisions such as these that the buy-back mechanism was an intricate part of the takeover mechanism which the bidder controlled. This is also reinforced by other provisions such as, for example, cll 4.3 and 4.13 and Schedule 4 generally.
   3. Thirdly, it is apparent that the consideration to be paid under any Buy-Back Agreement was to be sourced from debt finance provided by the “Lender” (defined to be SingTel or its subsidiary); see cll 4.5(b) and 4.6(a). This was to occur by the necessary crediting of Optus’ Account on each relevant settlement date in immediately available funds. The expression “Optus’ Account” was defined as an A$ denominated account in the name of Optus styled “Buy Back Account”. The amount lent by the Lender to Optus was unsecured and subordinated (cl 4.9). Moreover, it was interest free until such time as the bidder held 100% of the Optus shares.
   4. Fourthly, as to this subordinated debt owed to the Lender, cll 5.1 to 5.4 provided a mechanism under which the debt could be repaid from a subsequent equity placement made to the bidder. Now if the bidder was not entitled to proceed to compulsory acquisition (and then 100%), the bidder could at its option (or if required by Optus) subscribe for one Optus share for each Optus share bought back (cl 5.1), with the proceeds used to repay the subordinated debt (cl 5.4). It was anticipated that this may occur, the alternative being the unpalatable consequence of an interest free loan; see the Target Statement at section 3.18(e), an extract of which is set out later in our reasons. But if the bidder could proceed to compulsory acquisition (and hence 100%) it had the option of subscribing for equity to repay the subordinated debt (cl 5.2) or leaving that debt in place, which would then become interest bearing (a palatable commercial option). We have discussed these provisions to demonstrate that it was not necessarily enshrined that the shares bought back would be replaced with equivalent shares under these placement provisions, but this was the likely scenario in the contemplation of the bidder and Optus (see also the worked example in Schedule B to the Buy-Back Agreement), particularly if *less* than 100% of the shares were to be acquired.
   5. Fifthly, cl 6 mandated that Optus had to account for the buy-back in accordance with the pro forma accounting entries set out in Schedule B of the Buy-Back Agreement (see also cl 6 of Schedule 4). This was an unusual provision, but no doubt was designed to ensure in part that the accounting entries accorded with how the proposed transactions had been presented to the Commissioner and upon which rulings had been sought. As we will explain in a moment, the buy-back reserve was presented to the Commissioner as *not* being a “share capital account” within the meaning of s 6D. Further, Schedule B made it apparent that both the bidder and Optus were making a clear distinction between the share capital account and the buy-back reserve account and that the former was to be debited on a pro rata basis. Undoubtedly, how the parties described the accounts and the entries (and their purpose) is not definitive of the issues that we have to decide. Nevertheless, the transactions and the accounts need to be considered and analysed in their commercial setting in order to address the principal question before us.
2. Prior to the execution of the Implementation Agreement on 18 May 2001, on 12 April 2001 Optus had applied (presumably on behalf of all shareholders who accepted the takeover offer and elected for the buy-back mechanism) through PricewaterhouseCoopers (PWC) for a buy-back class ruling from the Deputy Commissioner of Taxation to confirm that the proposed accounting treatment for the buy-back provided for an appropriate allocation of the buy-back consideration into dividend and capital components; it would appear that another class ruling was also sought dealing with capital gains tax aspects of the “scrip for scrip” option(s), but this can be put to one side for present purposes.
3. The class ruling application maintained that the amount of the buy-back consideration which was not taken to be a dividend was the amount to be debited to the account labelled “share capital”, which was to be calculated by the percentage of shares bought back over the total number of Optus shares on issue. The class ruling application also expressly stated that the buy-back reserve account was *not* an account of share capital. It also stated at page 13 the following:

Pursuant to sections 159GZZZQ(3)-(5), the amount of the consideration determined under section 159GZZZQ(l) will be reduced by the amount of the buy-back consideration that is taken to be a dividend by section 159GZZZP, provided:

(a) the dividend is included in the seller’s assessable income (disregarding section 128D); and

(b) the amount of the dividend is not debited by the company against a share capital account or asset revaluation reserve and is not attributable to amounts that were transferred from such an account or reserve of the company.

As noted above, the dividend component of the Buy-Back Consideration is effectively the amount debited to the buy-back reserve. This dividend is deemed by section 159GZZZP to be paid from profits of the company. Accordingly, it will be included in the assessable income of resident Optus shareholders (pursuant to section 44(1)) and would be similarly included in the assessable income of non-resident shareholders if it were not for the application of section 128D. Further, the buy-back reserve is neither a share capital account or an asset revaluation reserve (or an amount transferred from such an account).

1. Optus created a new ledger account called a “share buy‑back reserve” account to reflect the buy-back in accordance with the terms of the Implementation Agreement.
2. On 1 May 2001, the Deputy Commissioner sought further information in relation to the accounting proposed for the buy-back. The Deputy Commissioner’s enquiry related primarily to the debiting of part of the buy-back consideration to a share buy-back reserve, rather than to some other account, such as retained profits.
3. On 2 May 2001, PWC wrote to the Deputy Commissioner and, inter alia, stated the following:

(a) At the outset, PWC stated:

It seems to us the key issue is whether the amount debited to share capital in respect of the Buy-Back Consideration is an appropriate amount. Once the amount to be debited to share capital is determined, any excess will be a dividend, notwithstanding the choice of other account, the availability of retained profits or the future treatment of such accounts.

Under Division 16K, any part of the Buy-Back consideration which is not debited to amounts standing to the credit of a share capital account is deemed to be a dividend: section 159GZZZP(1). It does not matter whether this excess is debited to a share buyback reserve, retained profits or asset revaluation reserve. Similarly, it does not matter how that reserve is treated or adjusted in the future.

(b) Under the heading, “Why is the share buy-back debited to the buy-back reserve?”, PWC stated the following:

Essentially, [Urgent Issues Group Consensus View UIG 22, *Accounting for the Buy-Back of No Par Value Shares* (November 1998)] provides guidance on the appropriate approach to account for the Buy-Back of no par value shares under Australian Generally Accepted Accounting Principles (GAAP).

The key requirement is that the “equity” of an entity is reduced by the cost of acquisition of the shares bought back. However, UIG 22 does not prescribe which equity accounts should be reduced, merely that the accounting should reflect the “substance” of the transaction.

CWO currently only has two equity accounts: viz share capital and retained losses as at 31 March 2000, the last audited statutory accounts.

CWO could thus debit the Buy-Back Consideration to share capital; retained profits/losses and/or a new equity account specifically raised for the purpose: a buy-back reserve.

The accounting advice received strongly recommended that the most appropriate amount of the Buy-Back Consideration to debit to CWO’s share capital account is an amount pro-rata to the number of shares bought back [all CWO shareholders would then receive an equal return of share capital if all CWO shareholders accepted the bid by way of the Buy-Back Alternative].

The balance of the Buy-Back Consideration would then be debited either to the retained profits / losses account or a buy-back reserve. The buy-back reserve was chosen because it was considered that the accounts would better reflect the substance of the transaction ie the transaction should not create accumulated losses. Rather, the Buy-Back accounting should reflect a matter of equity and be carried as a negative reserve in the same way as foreign currency translation and other reserves.

An alternative was considered: namely, CWO to revalue investments in subsidiaries to create an asset revaluation reserve in CWO’s equity accounts which could be debited with the balance of the Buy-Back Consideration. However, this alternative was dismissed by CWO as it would, under Australian accounting standards, require the costly regular revaluation of subsidiaries and the potential write-down of those investments in the future through CWO’s profit and loss account. In addition, the revaluation of assets would potentially not, in any event, eliminate the requirement to debit a buy-back reserve in CWO’s consolidated accounts as internally generated goodwill could not be revalued in those accounts. The use of a buy-back reserve would thus also keep CWO’s company only and consolidated accounts consistent.

Whether the accounting treatment adopted is to debit the “balance” of the Buy-Back Consideration to CWO’s retained profits / losses, a buy-back reserve or an asset revaluation reserve, the treatment under Division 16K is the same ie a deemed dividend.

Even if the balance is debited to CWO’s share capital account, the amount which does not reduce an amount standing to the credit of the share capital account - reflecting CWO shareholders who do not accept the Buy-Back - would be a deemed dividend ie the amount of any negative share capital account. It was, however, considered inappropriate to return more than a pro-rata amount of share capital to the shareholders accepting the Buy-Back ie by “delivering” share capital “belonging” to ongoing shareholders to exiting shareholders.

CWO has negligible franking credits ($286,000) in the context of the value of the takeover offer [A$14.9 billion to A$16.0 billion using the implied purchase price per SingTel media release of 26 March 2001 announcing the takeover offer].

It is thus anticipated that any deemed dividend will be unfranked [due to the de minimus franking requirements in section 160APX(1B)] and non-rebateable.

(c) Under the heading, “Does, or could, Optus have sufficient profits against which to debit the share buy-back?”, it was concluded by PWC that:

Overall, it is anticipated that any retained profits at the time of the Buy-Back would be insubstantial when compared to the Buy-Back Consideration and the amount debited to the buy-back reserve.

(d) Under the heading, “Will the debit balance of the buy-back reserve be debited, ultimately, to profits or share capital?”, it was stated:

Australian GAAP neither mandates nor prohibits the maintenance of the buy-back reserve indefinitely.

We are not able to confirm what might, ultimately, happen to the buy-back reserve.

SingTel has indicated that the most likely event, if the buy-back reserve is not maintained indefinitely, would be that a portion of future accounting profits is credited to the reserve to reduce its negative balance.

The offset of some or all of the buy-back reserve against share capital might be possible in the future (we have not sought a legal opinion on the Corporations Law). The offset of the buy-back reserve against share capital has not been considered in any detail by CWO eg could such an offset be considered to “taint” the share capital account for income tax purposes, [Section 160ARDM] even though an amount would be debited not credited to the share capital account?

1. We have set this out at some length as it is apparent that all relevant participants were proceeding on the basis that the buy-back reserve account was not a “share capital account” within the meaning of s 6D. Equally importantly, it would seem that the parties were proceeding on the basis that the return of share capital was only recognised with respect to the debit of the requisite pro rata amount to the share capital account, but not the buy-back reserve.
2. On 10 May 2001, the appellant (through Arthur Andersen) applied for a private ruling on the buy-back question.
3. The private ruling application stated in part at pages 7 and 8:

The taxation consequences of a share buy-back are codified in Division 16K of Part III of the Income Tax Assessment Act 1936 (“the Act”). The SingTel takeover proposal would be considered an “off market” buy-back pursuant to section 159GZZZK, resulting in the tax consequences for CWAP being calculated in accordance with Subdivision C.

Pursuant to section 159GZZZP(1), for all purposes of the Act, the difference between the purchase price (ie. the buy-back price) and the amount debited against the company’s share capital account istaken to be a dividend paid by the company to the seller, out of profits derived by the company, and on the day the buy-back occurs.

Pursuant to section 159GZZZP(2) the remainder of the purchase price is taken not to be a dividend for the purposes of the Act.

As noted above, Optus has received accounting opinions from PricewaterhouseCoopers and KPMG which advise that the appropriate accounting treatment for the buy-back involves the debiting of share capital by the percentage of shares bought-back over the total number of Optus shares on issue. In respect of each share bought-back, the debit to share capital will be calculated as:

|  |  |  |
| --- | --- | --- |
| 1 |  |  |
| Total number of Optus shares on issue on the offer date | × | Optus share capital account on the offer date |

The balance of the Buy-Back Consideration will be debited to a buy-back reserve. A buy-back reserve is not an account of share capital.

Accordingly, the dividend component of the buy-back in respect of each share, for all purposes of the Act, will be determined under section 159GZZZP(1) of Division 16K as the Buy-Back Consideration (see earlier for calculation) in respect of that share less the amount debited by Optus to share capital i.e.:

Buy-Back Consideration

minus

|  |  |  |
| --- | --- | --- |
| 1 |  |  |
| Total number of Optus shares on issue on the offer date | × | Optus share capital account on the offer date |

[…]

1. On 18 May 2001, SingTel, through its wholly owned Australian subsidiary, SingTel Australia Investment Ltd, made a takeover offer for a majority of the shares in Optus. The Bidder’s Statement dated 18 May 2001 lodged with the Australian Securities and Investments Commission explained that the offer included a choice of three consideration options and “two disposal mechanisms (the Transfer Alternative and the Buy-Back Alternative)”.
2. Also on 18 May 2001, Optus issued its Target Statement in respect of the acquisition of Optus shares. The Target Statement in section 3.18(b) explained the bidder’s reasons for including the buy-back alternative as part of the offer as follows:

* SingTel made it clear to the Independent Directors that inclusion of the Buy-Back Alternative was required to secure SingTel’s agreement to make the Offer. For the reasons set out in the Letter from the Independent Directors, securing SingTel Australia’s agreement to make the Offer was considered in the best interests of Optus and its shareholders.
* The Buy-Back will be funded in full by SingTel by way of Subordinated Debt. The terms of that funding arrangement were negotiated by the Company with a view to ensuring that the Buy-Back will not materially prejudice Optus’ ability to pay its creditors. These funding arrangements are discussed in Section 3.18(c) below.
* Under the terms of the Implementation Agreement, Optus can require SingTel Australia to subscribe for shares in Optus on a one-for-one basis to replace the Optus Shares bought back (except if SingTel Australia is entitled to proceed to compulsory acquisition or where an insolvency event subsists in relation to Optus). This subscription will provide sufficient funds to Optus to allow it to repay the Subordinated Debt advanced by SingTel (other than the amounts referred to in Section 3.18(c)(ii) below, which are expected to be immaterial). It will also give SingTel Australia a shareholding in Optus that is commensurate with the aggregate funding outlay the SingTel Group would be required to make as a result of acceptances of the Offer through the Buy-Back Alternative. In other words, if SingTel Australia is unable to acquire 100% of Optus, Optus can ensure that the number of its issued shares remains unchanged and there is no reduction in its total shareholders' equity. This is explained in greater detail in Section 3.18(e) below.

1. The Target Statement went on to explain that the funding of the buy-back would be by SingTel lending to Optus an amount equal to the sum of, in effect, the total buy-back consideration payable on a settlement date together with any fees, and other costs and outgoings, incurred by Optus in connection with the payment mechanism. An aspect of that funding involved the possibility of new shares being issued to the bidder. Section 3.18(e) explained the placement of shares as follows:

(e) Placement

SingTel Australia may (and, if required by Optus, must) subscribe for one Optus Share for each Optus Share bought back under a Buy-Back Agreement if:

* at the end of the Offer Period, SingTel Australia is not entitled to compulsorily acquire all Optus Shares it does not own (or a Court makes an order disallowing the compulsory acquisition of those Optus Shares following an application made to the Court by an Optus shareholder); and
* no insolvency event subsists in relation to Optus.

If at the end of the Offer Period SingTel Australia is entitled to compulsorily acquire all Optus Shares it does not own, SingTel Australia will be entitled to subscribe for one Optus Share for each Optus Share bought back under a Buy-Back Agreement.

Any Optus Shares issued to SingTel Australia under the placement described above will be issued at a subscription price per share equal to the total Buy-Back Consideration divided by the total number of Optus Shares bought back. Optus will use the funds subscribed by SingTel Australia for Optus Shares under the Placement to repay an equal amount of Subordinated Debt.

It seems reasonable to infer that SingTel Australia will choose to subscribe for one Optus Share for each Optus Share bought back under the Buy-Back Alternative as:

* the Subordinated Debt does not attract interest; and
* if SingTel does not acquire 100% of Optus, SingTel Australia's shareholding will otherwise not be commensurate with the aggregate funding outlay of the SingTel Group made in connection with acceptances under the Offer.

Furthermore, Optus is in a position to ensure that there will be no overall change to total shareholders’ equity because it can require SingTel Australia to subscribe for shares in Optus to replace those shares bought back.

1. On 6 June 2001, the Commissioner issued a class ruling (CR2001/17) entitled “Income Tax: capital gains: scrip for scrip roll-over: proposed takeover of Cable & Wireless Optus Limited by SingTel Australia Investment Ltd” (with an addendum on 22 August 2001). The contents of the class ruling are not directly relevant for present purposes. We have not been provided with a copy of any class ruling in relation to the buy-back question and we are unclear as to whether a copy of any such ruling was before the primary judge; we have reviewed Appendix E to the Statement of facts not in dispute before the primary judge, but it did not address the buy-back question but rather the capital gains tax issue; moreover our searches of the publicly accessible class rulings have not revealed any class ruling concerning the buy-back question of the type that we are addressing.
2. On 13 June 2001, the Commissioner issued to the appellant a private ruling on the subject of the buy-back of the appellant’s Optus shares. On 26 June 2001, the appellant filed a further (amended) application for a private ruling. It contained a similar statement to the 10 May 2001 application that we have set out earlier. On 29 June 2001, the Commissioner issued to the appellant a further (and final) private ruling on the subject of the buy-back of the appellant’s shares in Optus. It was in the following terms (“CWAP” referring to the appellant):

**WHAT THIS RULING IS ABOUT:**

**These are the questions for which a Private Ruling is made:**

1. Will section 159GZZZP apply to deem part of the Buy-Back Consideration payable to CWAP to be a dividend?

2. Will the dividend component of the Buy-Back Consideration payable to CWAP be determined under section 159GZZZP by deducting from the Buy-Back Consideration the amount debited by Optus to its share capital account so that the dividend amount will be calculated by the following formula:

A = B – C

Where:

A = Dividend component of the Buy-Back Consideration

B = Buy-Back Consideration

|  |  |  |  |
| --- | --- | --- | --- |
| C = | 1 |  | Balance of Optus share capital account on the Settlement Date |
| Total number of Optus shares on issue on the Settlement Date | × |

3. For the purposes of determining whether in respect of the disposal of an Optus share:

(i) an amount is included in the assessable income of CWAP; or

(ii) an amount is allowable as a deduction to CWAP; or

(iii) whether CWAP makes a capital gain or capital loss,

will the amount of consideration which is taken to have been received by CWAP in respect of the disposal of the Optus share be determined under section 159GZZZQ to be equal to the Buy-Back Consideration less the amount that is taken to be a dividend by section 159GZZZP?

4. Will the Commissioner make a determination under subsection 45B(3) to apply section 45C in relation to the whole or part of the distribution of share capital to CWAP?

5. Will CWAP be liable to withholding tax payable in accordance with section 128B in respect of the dividend component of the Buy-Back Consideration?

6. Will Part IVA apply to CWAP where CWAP disposes of all or most of its Optus shares by choosing the Buy-Back Alternative?

**RULING(s):**

**The Commissioner’s opinion in relation to each question is as follows:**

1. Yes. Section 159GZZZP will apply to deem part of the Buy-Back Consideration payable to CWAP to be a dividend. The dividend will be unfranked.

2. Yes. The dividend component of the Buy-Back Consideration received by CWAP will be determined under section 159GZZZP by deducting from the Buy-Back Consideration the amount debited by Optus to its share capital account.

3. Yes. For the purposes of determining whether in respect of the disposal of an Optus share:

(i) an amount is included in the assessable income of CWAP; or

(ii) an amount is allowable as a deduction to CWAP; or

(iii) whether CWAP makes a capital gain or capital loss,

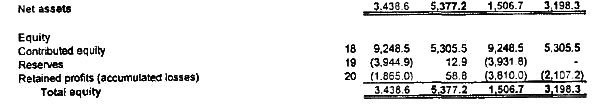
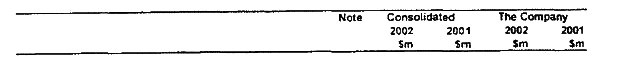
the amount of consideration which is taken to have been received by CWAP in respect of the disposal of the Optus share will be determined under section 159GZZZQ to be equal to the Buy-Back Consideration less the amount that is taken to be a dividend by section 159GZZZP.

4. No. The Commissioner will not make a determination under subsection 45B(3) to apply section 45C in relation to the whole or part of the distribution of share capital to CWAP.

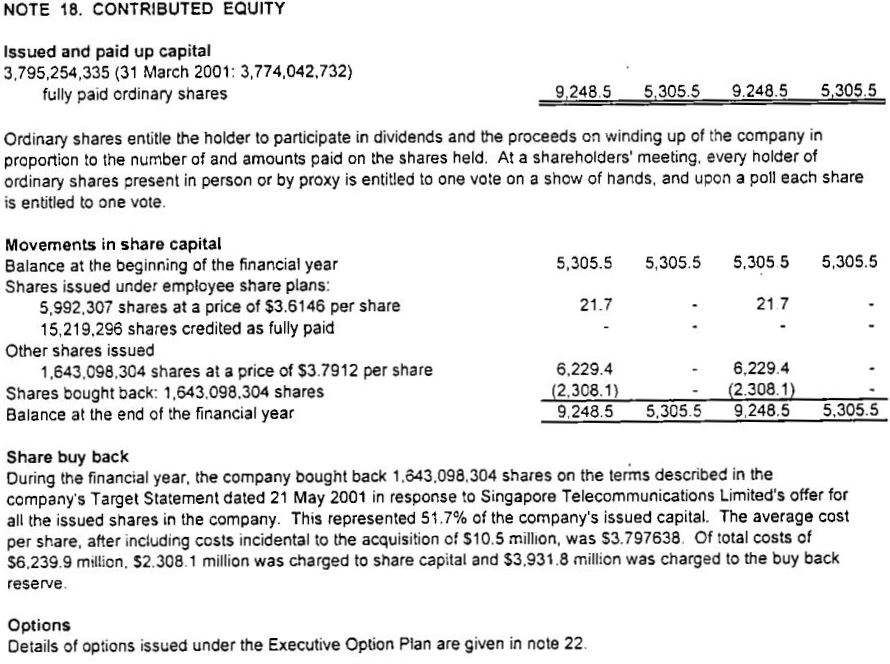
5. Yes. CWAP will be liable to dividend withholding tax payable in accordance with section 128B in respect of the dividend component of the Buy-Back Consideration. The rate of tax payable is 15% of the dividend.

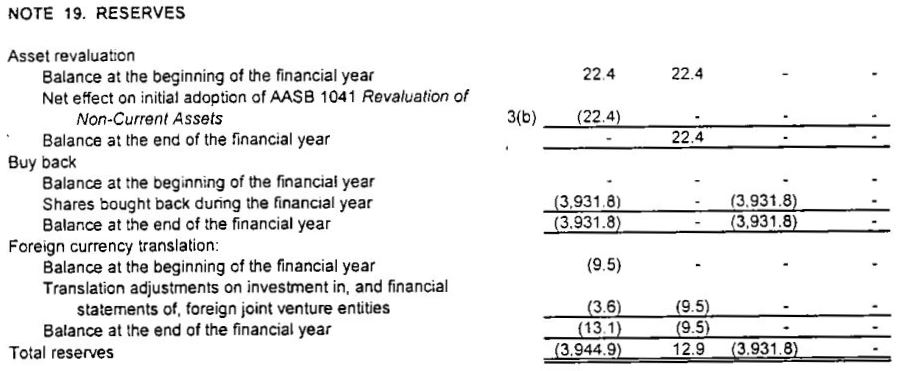
6. No. Part IVA will not apply to any of the schemes in relation to CWAP if CWAP disposes of all or most of its Optus shares by choosing the Buy-Back Alternative and dividend withholding tax is paid.

1. On 30 August 2001, the appellant accepted the buy-back alternative in respect of 1,639,849,948 Optus shares, for a total consideration of $6,216,762,899.29.
2. On 6 September 2001, Optus bought back 1,642,101,319 shares (including the 1,639,849,948 shares held by the appellant) for $6,225,502,631.68 (the first buy-back). The bought back shares were cancelled. The bought back shares represented 43% of the Optus shares that were on issue at that date.
3. On or about 6 September 2001, a total amount of $587,346,464 (including $586,983,026 withheld from the appellant) was paid by Optus to the Commissioner as dividend withholding tax.
4. On 28 September 2001, Optus bought back a further 999,985 shares (not held by the appellant) (the second buy-back). Those bought back shares were also cancelled.
5. Optus accounted for the consideration paid on the first buy-back and second buy-back by: (a) debiting the account labelled the “share capital” account by the percentage of shares bought back of the total number of Optus shares then on issue (namely, 43%); and (b) debiting the balance of the consideration to a new account labelled a “buy-back reserve” account. Those accounting transactions were consistent with the accounting treatment which had been agreed in the Implementation Agreement to facilitate the acquisition of Optus by SingTel.
6. The accounting adopted by Optus was also consistent with the basis upon which the appellant had obtained a private binding ruling(s) from the Commissioner on the subject of the buy-back of the appellant’s shares. It was also consistent with what had been represented to the Commissioner by both Optus and the appellant in their various applications for the rulings.
7. In accordance with the ruling requests, the ruling(s) and the terms of the Implementation Agreement, the total consideration paid by Optus for the buy-back of $6,225,502,631.68 was debited in part to the share capital account and in part to the share buy-back reserve account. $2,306,705,228.26 was debited to the share capital account. The balance of the consideration of $3,918,797,343.42 was debited to the share buy-back reserve account. There is no dispute between the parties that the manner in which Optus accounted for the share buy-back was acceptable under the relevant Australian Accounting Standards. Two experts gave evidence (by reference to the relevant Accounting Standards, Corporations Law requirements, Statements of Accounting Concepts, and Urgent Issues Group Consensus Views applicable to the buy-back transaction) that the accounting adopted by Optus in its general ledger was an acceptable method of recording the buy-back transaction.
8. On 30 September 2001, in respect of the first buy-back, Optus recorded the transaction in its accounts by making the following journal entries:
   1. Debit to the Share Capital account of $2,306,705,228.16;
   2. Debit to the Share Buy-Back Reserve account of $3,918,797,343.42;
   3. Credit to the Debt due to Optus shareholders account of $6,225,502,631.68.
9. Also on 30 September 2001, in respect of the second buy-back, Optus recorded the transaction in its accounts by making the following journal entries:
   1. Debit to the Share Capital account of $1,398,591.34;
   2. Debit to the Share Buy-Back Reserve account of $2,486,249.76;
   3. Credit to the Debt due to Optus shareholders account of $3,884,841.10.
10. On 30 October 2001, Optus issued SingTel with 1,643,098,304 shares for an amount of $6,229,387,472.78.
11. The accounting by Optus of the share buy-back transaction reflected the distinction between its capital and the equity of its shareholders. The statement of financial position subsequently published by Optus for the financial year ended 31 March 2002 recorded the amount of $9,248.5 million as “contributed equity”. It also showed negative reserves of $3,931.8 million. The former was to be read in conjunction with note 18 and the latter was to be read in conjunction with note 19.
12. Before setting out the notes, it is appropriate to set out an extract of the Balance Sheet (described as Statement of Financial Position (as at 31 March 2002)):



1. Notes 18 and 19 relevantly stated:





1. The financial statements recorded the buy-back transaction from the point of view of Optus as a matter affecting the equity of the shareholders. The amount shown as “contributed equity” increased from $5,305.5 million to $9,248.5 million by reason of the share buy-back as explained in note 18, namely the acquisition of 1,643,098,304 shares (a *decrease* in contributed equity, but only as to *part* of the consideration being $2,308.1 million of the total cost of $6,239.9 million) and the issue to SingTel of the same number of shares at the price of $3.7912 per share (an *increase* in contributed equity). The buy-back transaction also affected the total reserves shown in note 19. It is not necessary to set out note 20. It merely elaborates on that component of equity referable to accumulated losses.
2. At this stage, it is appropriate to make some further observations concerning the accounts and the notes:

(a) First, it is apparent from the Statement of Financial Position that “Equity” was divided into three components being:

(i) Contributed equity;

(ii) Reserves; and

(iii) Retained profits (accumulated losses).

(b) Secondly, the phrase “contributed equity” was a reference to share capital as note 18 explains. More significantly, “Reserves” were not treated as share capital.

(c) Thirdly, it is apparent that movement in reserves or retained profits (accumulated losses) could affect the overall equity, but *not* “contributed equity” as such.

(d) Fourthly, notes 18 and 19 demonstrate that the buy-back reserve was not a charge as such on “contributed equity”. The only part of the buy-back consideration that was charged to “contributed equity” was $2,308 million. This is made plain in note 18 under the heading “Share buy back”.

(e) Fifthly, the accounts were signed off by the directors, with a clear audit report from PWC. There is no issue that the accounts reflected relevant standards and legislative requirements and that the recorded transactions reflected their commercial and economic reality, ie the debit to the buy-back reserve was not treated as affecting “contributed equity” and was not seen as a reduction of capital.

1. For the years ending 31 March 2002 to 2012, the share buy-back reserve account had a negative balance of $3,931,788,979.18. The movements in the share buy-back reserve account can be summarised as follows (we note that the credit entry of approximately $10.5 million in the year ending 31 March 2002 was apparently a costs adjustment):

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Period | Debit | Credit | Balance | Cumulative Balance |
| 2001 |  |  |  | 0 |
| 2002 | 3,942,294,365.18 | (10,505,386.00) | 3,931,788,979.18 | 3,931,788,979.18 |
| 2003 - 2011 |  |  |  | 3,931,788,979.18 |
| 2012 |  |  |  | 3,931,788,979.18 |
| 2013 |  | (3,931,788,979.18) | (3,931,788,979.18) | 0 |
| 2014 |  |  |  | 0 |

1. As we have said, on 5 December 2012, the High Court handed down its decision in *Consolidated Media*.
2. On 30 January 2013, the Commissioner issued to Optus a private ruling on the subject of a proposed capital reduction.
3. On 6 March 2013, Optus undertook a capital reduction in accordance with Part 2J.1 of the *Corporations Act 2001* (Cth). As an integral part of this reduction of capital, the debit entry on the share buy-back reserve account was wiped out with a corresponding reduction of capital made. We would note that this is all consistent with the position accepted by all participants and reflecting the commercial and economic reality that the amount debited to the buy-back reserve account in September 2001 through to March 2013 was *not* treated as a reduction of capital as such, even though it may have reduced Optus’ equity position (a different concept as we will later explain). Optus recorded the 2013 capital reduction in its accounts by making the following journal entries:

Dr Share capital – Fully paid ordinary shares $3,931,788,979.18

Cr Share Buy Back Reserve $3,931,788.979.19

1. On 9 May 2013, the appellant lodged an application with the Commissioner pursuant to s 18-70 of Schedule 1 to the TAA for a refund of incorrectly withheld tax in the amount of $452,452,013. On 26 May 2014, the Commissioner advised the appellant of his decision not to refund the withholding tax sought in the appellant’s application. On 22 July 2014, the appellant lodged pursuant to the provisions of Part IVC of the TAA an objection in relation to the decision not to refund the withholding tax. On 24 October 2014, the Commissioner issued his notice of decision on objection in respect of the refund application, in which he indicated that the appellant’s objection had been disallowed in full. The Commissioner’s decision was then the subject of appeal before the primary judge.
2. In large measure, the above primary facts are not controversial as between the parties, but it has been necessary to set them out in order to appreciate our later observations. We would also note the following concerning evidence adduced before the primary judge.
3. As we have indicated, two experts gave evidence about the nature of the buy-back reserve account, but they disagreed about the substance of the share buy-back transaction and the nature of the buy-back reserve. A joint report was prepared by Mr Warren McGregor (the Commissioner’s witness) and Mr Wayne Lonergan (the appellant’s witness) in which they identified those matters on which they agreed and those on which they differed. They were each also called to give oral evidence and gave that evidence concurrently. Mr McGregor was a director of the financial reporting firm of Stevenson McGregor and a senior consultant with PWC. He was also an adjunct professor at the Department of Accounting and Finance at Monash University and had been involved in the independent setting of accounting standards domestically and internationally. Mr Lonergan was a founding director of Lonergan Edwards and Associates which was a specialist corporate valuation firm based in Sydney. He was previously a corporate finance partner at the firm of Coopers and Lybrand (which subsequently amalgamated with the firm PWC). He had been a member of a number of bodies including the Companies and Securities Advisory Committee and the Australian Accounting Standards Board.
4. The difference between the experts in how they saw the nature of the share buy-back reserve lay in the difference between them about how they saw the substance of the share buy-back transaction. Mr McGregor’s opinion was that the substance of the share buy-back transaction involved “a return of capital and a return on capital” to the shareholders (including the appellant). The amount received by the shareholders from Optus was seen by Mr McGregor to have a component representing the return *of* the capital which had been contributed to the company together with a component representing something in the nature of a reward or profit on that contribution (a return *on* capital). The former was seen to come from the share capital account and the latter from the buy-back reserve account. Contrastingly, Mr Lonergan took issue with Mr McGregor’s understanding of the substance of the transaction as involving a return on, and a return of, investment. Mr Lonergan saw the substance of the buy-back transaction “as a share capital transaction in the context of a change of control transaction” whereby the shareholders were made an offer to purchase their shares in Optus for a specified bid price. An important basis of Mr Lonergan’s opinion was that the offer to acquire shares was “linked” with the change of control and in particular with the mechanism by which “SingTel had to undertake to subscribe for share capital ([namely,] the same number of shares and the amount subscribed equating to the buy-back price excluding transaction costs) to fund the payment”. Each of the experts was cross-examined. The primary judge considered that neither view of the substance of the transaction, or of the nature of the buy-back reserve, was shown to be without difficulty or wholly without merit. His Honour considered that the substance of the buy-back share transaction, and the mechanism by which it was accounted for (including the buy-back share reserve), could with some justification be seen as involving either a share capital transaction whereby the capital in Optus of the existing shareholders was substituted with that from SingTel, or as involving a takeover in which the existing shareholders were paid an amount through the buy-back which gave them both a return of their equity and some return on the equity.
5. The experts relied upon relevant accounting standards, although none of the standards dealt conclusively with the circumstances concerning the Optus share buy-back. The only authoritative pronouncement at the relevant time specifically referring to the accounting for, and reporting of, share buy-backs was the Urgent Issues Group Abstract 22 (UIG 22) dealing with “accounting for the buy-back of no par value shares” issued by the Australian Accounting Research Foundation on behalf of the Australian Society of Certified Practising Accountants and the Institute of Chartered Accountants in Australia. Guidance had previously been issued on accounting for share buy-backs in the context of shares with a par value, but a need was felt to clarify whether the requirements of that guidance applied in accounting for a buy-back of no par value shares. The issue considered in UIG 22 was how the buy-back of no par value shares was to be recognised in the general purpose financial report of a company. UIG 22 expressed consensus that shares included in the equity of an entity which were bought back required that the equity of the entity be reduced directly by the cost of acquisition of the shares bought back. The cost of acquisition was said to comprise the purchase consideration plus the costs incidental to the acquisition, and “a description of the nature and terms of the share buy-back and any other information material to an understanding of the transaction [had to] be disclosed in the financial year in which the buy-back occurs”.
6. The discussion in UIG 22 which followed the statement of consensus by the Urgent Issues Group referred to the Statement of Accounting Concepts entitled “Definition and Recognition of the Elements of Financial Statements” (SAC 4). Paragraph 8 of UIG 22 referred to the definition in SAC 4 of distributions to owners as “future economic benefits distributed by the entity to all or part of its ownership group, either as a return on investment or as a return of investment”. Mr Lonergan emphasised the sentence in UIG 22 following this reference to SAC 4 which noted that in “the case of a share buy-back, the parties (shareholders/owners) are receiving consideration for their shares” because they are equity participants in the entity. Mr Lonergan went on to note that the discussion in UIG 22 referring to the definition in SAC 4 of a distribution to owners as “being either a return on investment or a return of investment” did “not specifically state that a buy-back has to be split between these components”. Paragraph 11 in UIG 22, however, noted the fact that the details of buy-back arrangements may vary from time-to-time and that the consensus in UIG 22 did not prescribe which equity accounts were to be adjusted for the cost of the acquisition of the shares bought back.
7. Mr McGregor also referred to paragraph 11 of UIG 22 noting that it allowed for the “accounting for the buy-back to reflect the substance of the buy-back transaction”. This was consistent with the requirements of Australian Accounting Standard AASB 1001 that accounting policies must be selected and applied in a manner which ensured that the resulting financial information satisfied the concepts of relevance and reliability. We will return to UIG 22 later.
8. Ultimately the experts agreed that the Optus buy-back transaction affected the equity in Optus but disagreed about whether the amount in the share buy-back reserve was part of the return of the investment or a return on the investment. Mr McGregor identified this difference in the joint report stating:

The difference of opinion relates to the nature of the buy-back amount, ie the “distribution to shareholders” and, as a corollary, the nature of the “buy-back reserve”. As noted […] above, the authoritative accounting literature characterises “distributions” as either returns **of** investment or returns **on** investment. Mr McGregor believes the buy-back amount comprised in part a return of investment and in part a return on investment. Optus’ accounting for the transaction was consistent with that perspective. The buy-back amount was apportioned between a reduction in paid up capital, reflecting the proportion of the total number of shareholders participating in the buy-back, and the share buy-back reserve. [Emphasis added by Mr McGregor]

1. His Honour concluded that the competing expert opinions assisted the relevant factual inquiry that he was addressing, but did not resolve it (see at [23]). We will discuss his Honour’s conclusions later, but in essence they are not inconsistent with the views expressed by Mr McGregor, which in our view his Honour was entitled to rely upon. In any event, his Honour’s principal conclusion is supportable independently of the expert evidence. We would also note for completeness that there is no ground of appeal which challenges the reasonableness of relying upon Mr McGregor’s opinion evidence if and to the extent that his Honour may have done so (see at [23] and [24] (“… to obtain a return of their capital and on their capital.”)).

# relevant legislation

1. Section 159GZZZP of the ITAA (as it stood as at the date of the first buy-back) provided:

**159GZZZP Part of off-market purchase price is a dividend**

(1) For the purposes of this Act, but subject to subsection (1A), where a buy-back of a share by a company is an off-market purchase, the difference between:

(a) the purchase price; and

(b) the part (if any) of the purchase price in respect of the buy-back of the share which is debited against amounts standing to the credit of the share capital account of the company;

is taken to be a dividend paid by the company:

(c) to the seller as a shareholder in the company; and

(d) out of profits derived by the company; and

(e) on the day the buy-back occurs.

(1A) If the dividend is included to any extent in the seller’s assessable income of any year of income, it is not taken into account to that extent under section 118-20 of the *Income Tax Assessment Act 1997*.

(2) The remainder of the purchase price is taken not to be a dividend for the purposes of this Act.

1. It is not necessary to set out s 159GZZZJ to 159GZZZN and 159GZZZQ. It is also not in doubt that the first buy-back and the second buy-back each involved an off-market purchase(s).
2. Section 6 (at the relevant time) set out definitions of, inter alia, “dividend” and “share capital account” in the following terms:

***dividend*** includes:

(a) any distribution made by a company to any of its shareholders, whether in money or other property; and

(b) any amount credited by a company to any of its shareholders as shareholders;

but does not include:

(d) moneys paid or credited by a company to a shareholder or any other property distributed by a company to shareholders (not being moneys or other property to which this paragraph, by reason of subsection (4), does not apply or moneys paid or credited, or property distributed for the redemption or cancelling of a redeemable preference share), where the amount of the moneys paid or credited, or the amount of the value of the property, is debited against an amount standing to the credit of the share capital account of the company; or

(e) moneys paid or credited, or property distributed, by a company for the redemption or cancellation of a redeemable preference share if:

(i) the company gives the holder of a share a notice when it redeems or cancels the share; and

(ii) the notice specifies the amount paid-up on the share immediately before the cancellation or redemption; and

(iii) the amount is debited to the company’s share capital account;

except to the extent that the amount of those moneys or the value of that property, as the case may be, is greater than the amount specified in the notice as the amount paid-up on the share; or

(f) a reversionary bonus on a policy of life-assurance.

***share capital account*** has the meaning given by section 6D.

1. Section 6D (as it stood as at the date of the first buy-back) provided as follows:

**6D Meaning of share capital account**

(1) A ***share capital account*** is:

(a) an account which the company keeps of its share capital; or

(b) any other account (whether or not called a share capital account), created on or after 1 July 1998, where the first amount credited to the account was an amount of share capital.

(2) If the company has more than one account covered by subsection (1), the accounts are taken, for the purposes of this Act, to be a single account.

Note: Because the accounts are taken to be a single account (the **combined share capital account**) tainting any of the accounts has the effect of tainting the combined share capital account.

(3) However, an account that is tainted for the purposes of Division 7B of Part IIAA is not a share capital account for the purposes of this Act other than for the purposes of:

(a) the definition of ***paid-up share capital*** in subsection 6(1); and

(b) subsection 44(1B); and

(c) section 46H; and

(d) subsection 159GZZZQ(5); and

(e) Division 7B of Part IIIAA; and

(f) subsection 160ZA(7A).

1. A principal objective of s 6D in the context of s 159GZZZP is to ensure that a shareholder is not taken to receive a taxable dividend to the extent that what the shareholder receives in an off-market buy-back of shares is a return of the capital which had been contributed to the company for the issue of the shares. That objective is achieved by excluding from the taxable returns to shareholders the amount which had been standing as a credit in the company’s account of its share capital. In that context, it is not necessary for the contributing shareholders to be the same as the shareholders receiving the payment.
2. In relation to the liability to withholding tax on any dividend and the payment thereof, ss 128B and 128C of the ITAA (as they stood at the relevant time) apply, although it is not necessary to set out these provisions. Relatedly, see also s 12-210 of Schedule 1 to the TAA dealing with the withholding and s 18-70 thereof (as it stood at the date of the refund claim) dealing with the refund of withheld amounts. It is not necessary to set out s 18-70 in full. Under s 18-70(1), an entity may apply in writing to the Commissioner for the refund of an amount if, inter alia, “the amount was so withheld, or paid to the Commissioner, in error”. Under s 18-70(2), the Commissioner must refund the amount if, inter alia, “the Commissioner is satisfied that it would be fair and reasonable to refund the amount, having regard to” various matters. For present purposes, we do not need to trouble ourselves with s 18-70(2). The present appeal has concerned the threshold question of whether “the amount was so withheld, or paid to the Commissioner, in error”. As is or will be apparent, we do not consider that there has been any “error”. But if there had been, the operation of s 18-70(2) would then need to be remitted to the Commissioner for further consideration.
3. Finally, on the hearing of the appeal various submissions were made concerning the then provisions of the *Corporations Act* dealing with share capital reductions and share buy-backs under the then Part 2J.1 (ss 256A to 258F). We do not need to set these out, but we will refer to some of these provisions later. Likewise, reference was made to Part 2M.2 and in particular s 286 dealing with an obligation to keep financial records. We will return to these issues later.

# primary judge’s reasons

1. His Honour accepted (at [23]) that the application of s 159GZZZP(1), coupled with the definition in s 6D, depended upon a factual inquiry to determine which part, if any, of the purchase price for the appellant’s shares bought back was debited against amounts standing to the credit of the share capital account of Optus at the relevant time. That factual inquiry depended upon whether the buy-back reserve was an account which Optus kept at the relevant time of its share capital within the meaning of s 6D(1)(a).
2. First, his Honour emphasised the circumstances of the case before him. As his Honour described it (at [24]), the Optus buy-back was part of a takeover offer whereby the bidder was funding the disposal of shares where shareholders had elected for their shares to be bought back by Optus as an option available to them. Optus was to be put in funds by SingTel to enable Optus to fund the buy-back. As his Honour perceived it, the issue for Optus was how to account for the difference between the amount it would receive to fund the payment to its shareholders and the amount it had in its share capital account that was referable to capital contributed by those shareholders. The approach taken was to create a buy‑back reserve to account for that difference. His Honour said that the character of the buy-back reserve account at the time of the debit reflected a transaction which was part of or facilitated a funding mechanism for the Optus shareholders to obtain a return *of* their capital and a return *on* their capital. As his Honour saw it, the shareholders were selling their shares in Optus to enable SingTel to acquire them at the amount offered. He considered that the role played by the buy‑back reserve account was to facilitate the payment of the consideration to the shareholders to the extent that the consideration exceeded the amount standing in the accounts of Optus as capital contributed by shareholders.
3. His Honour went on to discuss the relevance of the option given by cl 5.1 of the Implementation Agreement. We will return to this later.
4. Secondly, his Honour at various points in his reasons distinguished the nature and type of account dealt with in *Consolidated Media* from the circumstances of the present case.
5. As his Honour explained, correctly in our view, *Consolidated Media* was dealing with a different context.
6. Like the present case, in a general sense *Consolidated Media* was concerned with whether an account labelled a “share buy‑back reserve account” was an account which a company had kept of its share capital within the definition of s 6D for the purposes of s 159GZZZP. But the context was quite different. Publishing and Broadcasting Limited (PBL), the relevant taxpayer, received consideration for the sale of its shares to Crown Limited (Crown) in an off-market buy-back in the year ending 30 June 2002. PBL owned all of the nearly 3 billion issued and paid up ordinary shares in Crown for the whole of the year ending 30 June 2002. On 28 June 2002, PBL and Crown agreed for Crown to buy back 840,336,000 of its issued shares in order for Crown to return the capital to PBL which was in excess of Crown’s needs. The agreement between Crown and PBL provided for PBL to sell 840,336,000 shares to Crown by 1 August 2002 for a purchase price of $1 billion. Crown had created accounts in its general ledger before 28 June 2002, including those labelled a “shareholders’ equity account” and an “inter-company loan (payable) account”. On 28 June 2002, Crown created a new account in its general ledger labelled a “share buy-back reserve account”. On that date, a debit of $1 billion was made to the share buy-back reserve account and a credit of $1 billion was made to an account labelled “inter-company receivables account”, although the latter was subsequently reversed by correcting journal entries processed on 25 July 2002, with effect from 30 June 2002, which resulted in a credit being recorded in the inter-company loan (payable) account. No entry was made in the shareholders’ equity account in relation to the buy-back, although Crown’s financial report for the year ending 30 June 2002 showed a reduction of $1 billion in the item for “contributed equity” during the year. Note 16 to the accounts against the item “contributed equity” disclosed a reduction in the number of shares from 2,938,587,410 to 2,098,251,410 shares. The trial judge in *Consolidated Media* found that the debit recorded in the share buy-back reserve account was to an account kept by Crown of its share capital for the purposes of ss 6D and 159GZZZP. The High Court upheld the view that both the shareholders’ equity account and the share buy‑back reserve account were share capital accounts that were to be taken as a single share capital account against which the purchase price was debited.
7. It was in that context that the High Court made its observations at [44] to [46] to which we will return later.
8. The primary judge in the present case distinguished *Consolidated Media*. His Honour said (at [9]) that the fact that the buy-back reserve account in that case was held to be a share capital account did not carry with it the conclusion that all accounts with the label “buy-back reserve” account are share capital accounts within the meaning of s 6D and for the purposes of s 159GZZZP. Clearly that is correct.
9. His Honour then went on to contrast the type of buy-back addressed in *Consolidated Media* with the facts of the present case. *Consolidated Media* involved a buy-back of shares by Crown from its sole shareholder for the purpose of returning to that shareholder capital that was in excess of the needs of Crown. It was a return by a company to its shareholder of capital that was in the company before the buy-back and which, upon its return, reduced the share capital in the company. Contrastingly, so his Honour held, in the present case the buy-back of the appellant’s shares was different in substance and form from the transaction in *Consolidated Media*. His Honour said that the buy-back in the case of Optus did not return capital to its shareholders in excess of the needs of Optus but could, in an economic sense, be seen as a substitution of the capital which had previously been contributed by its previous shareholder with that funded by its subsequent shareholder. The buy-back of the appellant’s shares in Optus occurred in the context of the appellant, as the majority shareholder in Optus, disposing of its shareholding in Optus as part of a takeover by the SingTel group. The agreement which emerged for the acquisition by SingTel of the appellant’s shares in Optus included a proposal for all of the then existing Optus shareholders to be able to elect to have their Optus shares bought back in an off‑market buy-back. The proposal contemplated that Optus might be called upon to pay for the shares bought back and required that Optus be put in funds by SingTel to pay for the shares to be bought back. As his Honour perceived it, Optus, unlike the company in *Consolidated Media*, was neither reducing nor seeking to reduce its capital by the proposed buy-back, but was seeking to facilitate the substitution of its shareholders. There are some aspects of his Honour’s characterisation (and purportedly relevant distinguishing features) that are problematic, but we do not need to dwell on this for the moment.
10. His Honour later said (see at [28]) that the Optus accounts did not reveal a situation, unlike *Consolidated Media*, of a financial position in relation to share capital that could only be understood by subtracting the total consideration for the buy-back as a reduction of the credit balance in Optus’ share capital account. We agree with that statement at least. We will return to *Consolidated Media* later.
11. Thirdly, his Honour pointed out that neither the appellant nor Optus had at the time of the relevant transactions treated the buy-back reserve account as a “share capital account” within the meaning of s 6D for the purposes of s 159GZZZP. The application for a private ruling from the Commissioner and that ruling in June 2001 in fact treated the buy-back reserve account as not a “share capital account”.
12. Fourthly, his Honour also pointed out that the provisions of the Implementation Agreement made a distinction, when dealing with the accounting for the consideration of the buy-back, by:
    1. debiting the account labelled the “share capital” account by the percentage of shares bought back of the total number of Optus shares then on issue; and
    2. debiting the balance of the consideration to a new account labelled a “buy-back reserve” account.
13. This was also consistent with how Optus accounted for the consideration in its own books by inter alia the two debit entries. It was also not in dispute that the manner in which Optus accounted for the share buy-back was acceptable under the applicable Australian Accounting Standards (see at [6]).
14. Generally, his Honour emphasised the significance of the accounting treatment of the consideration for the buy-back (see at [16]). Only part was treated as a debit against the share capital account. The other part was debited not against the share capital account but rather the buy-back reserve account.
15. Fifthly, his Honour distinguished between the concept of equity and the concept of capital contributed to a company (see at [17]). His Honour was correct to do so. Indeed, the appellant’s failure to do so highlights one of the major misconceptions in its argument before us. His Honour held that the accounting by Optus of the share buy-back transaction reflected the distinction between its capital and its equity. So, the relevant balance of the consideration for the buy-back was not a return of capital which had been contributed to Optus, but was reflected in the accounts as “a matter of equity” and was to constitute a negative reserve (at [16] and [17]). His Honour said (at [28]) that the buy-back reserve account had an impact upon the equity of shareholders, but it did not record the financial position of Optus “in relation to its share capital”. We agree.
16. As his Honour put it (at [27]), the buy-back reserve account was not a record of a transaction reducing the share capital of the company. The buy-back reserve account was needed to account for the payment of part of the consideration paid for the shares bought back from money lent to Optus by SingTel for that purpose. His Honour said that the key requirement of the appropriate approach to account for the buy-back was that the equity of Optus was reduced by the cost of acquisition of the shares bought back. Optus had only two accounts which could have been used to reflect the reduction in shareholders’ equity, namely, the share capital account and the retained profits account. The buy-back reserve account was created as a new equity account to carry the negative reserve occasioned by payment of the difference between the total consideration and the amount standing in the credit of the share capital account referable to the capital contributed by shareholders whose shares were bought back. Accordingly, the buy-back transaction had an impact upon the equity in Optus because of the amount of the consideration to be paid in the buy-back. But importantly, the buy-back reserve account did not record a transaction reducing (or increasing) the contributed capital of the shareholders to Optus at the time of the debits. Again, in our view this analysis is correct.
17. Sixthly, his Honour said (at [26]) that every share buy-back involves a reduction of capital to the extent that shares bought back are cancelled (see s 257H(3) of the *Corporations Act*), but the consideration payable for the shares bought back and cancelled need not be from funds previously contributed to the company for the acquisition of those shares. In the present case, his Honour said that the consideration debited to the share buy-back reserve account came from borrowings pursuant to an agreement for the funding of a takeover in which the buy‑back was a component. The SingTel bidder subsequently acquired shares and the purchase price for the subsequent acquisition was credited to the account labelled “share capital”. On 30 October 2001, Optus issued 1,643,098,304 shares to SingTel for an amount of $6,229,387,472.78 and on 31 October 2001, a credit of that amount was made to account 310100 being the account labelled “share capital”. A corresponding debit of that amount was made to account numbered 295400 being the account labelled “subordinated debt”.
18. Seventhly, his Honour said (at [29]) that the buy-back in the present case was governed by, and took place under, Division 2 of Part 2J.1 of the *Corporations Act*. A reduction of share capital by Optus buying back its shares was authorised by s 258E(1)(b) “if the shares [were] paid for out of share capital”, but there was no restriction on the source of funds that Optus could use to effect its buy-back. Section 257A(b) permitted Optus to buy back its own shares provided that it followed the procedures laid down in Division 2 of Part 2J.1 of the *Corporations Act*. The buy-back of Optus’ shares fell within the provisions governing the selective buy-back of shares and required, amongst other things, the lodging with the Australian Securities and Investments Commission of the offer documents: see s 257E. The accounting entries in Schedule B to the Implementation Agreement expressly provided for a pro rata reduction in the share capital account to the number of shares bought back. His Honour held that it was *that* reduction of share capital which was authorised by s 258E as a reduction in share capital, namely, the proportion of the consideration to be debited against the share capital account.
19. Eighthly, his Honour rejected the argument that as Optus had no positive equity reserves and no retained profits, the financial position of Optus in relation to its share capital could only be understood by subtracting the debit balance in its buy-back reserve account from the credit balance in the share capital account. His Honour said (at [31]) that the fact that an outgoing has an impact upon equity does not stamp the outgoing as a reduction in capital. And Optus was able to make the buy-back regardless of whether it had available profits, an asset revaluation reserve or any positive equity account. We would interpolate here that it was able to do so through borrowed funds.
20. Ninthly, his Honour (at [32]) rejected the argument that the subscription for further share capital by SingTel on 30 October 2001 in an amount equivalent to the total buy-back consideration changed the characterisation. His Honour accepted that SingTel contributed capital to Optus within several months after the buy-back, but held that the subsequent contribution of capital to Optus told against the view that the funding recorded in the buy-back reserve account had previously been contributed as capital. The later subscription of shares by SingTel was a subsequent transaction and was recorded by a credit to the share capital account and a debit to the subordinated debt account. As his Honour analysed the matter, the journal entries thus confirmed the source of the previous payment to the appellant as being from the money borrowed by Optus for the payment and not from amounts which had been contributed as capital. Again, in our view this analysis is correct.
21. Tenthly, his Honour noted that on 30 January 2013, the Commissioner issued a further private ruling in the context of a proposed reduction of capital which proceeded on the basis that the buy-back reserve account was a share capital account (see at [7] and [33]). It may be noted that this ruling was after the decision in *Consolidated Media*, which had been handed down on 5 December 2012. His Honour said that he did not need to consider the correctness of the 2013 private ruling. But in any event he held that the history of the transactions on the buy-back reserve account between September 2001 and March 2013, when the debit balance of the account was in substance set off against the credit balance of the share capital account, was consistent with the treatment of the buy-back reserve account as a negative reserve, rather than as a share capital account.
22. Finally, his Honour rejected the appellant’s argument that its position was consistent with the legislative purpose of s 159GZZZP as being (at [34]) only “to prevent profits from being used to pay for share buy-backs and distributed to shareholders as a return of capital rather than as a taxable dividend by treating amounts other than share capital returned to shareholders as a dividend”. As his Honour said:

The text and policy of s 159GZZZP(1) does not require an inquiry into whether the payment is from the company’s distributable profit but, rather, whether it is from what the company had received as contributions of capital from its shareholders.

# grounds of appeal

1. Before discussing the grounds of appeal, it is appropriate to make the following general observations.
2. First, the issue before us is whether the buy-back reserve account was a “share capital account” within the meaning of s 6D(1)(a) as it then stood. The meaning of “share capital account” was recently illuminated and expounded in *Consolidated Media* at [42] to [44]. The present appeal involves no more than the application of that meaning (as so expounded) to the transactions and accounts before us.
3. Secondly, *Consolidated Media* stated that whether an account falls within that meaning does not necessarily turn on how the account is described. Moreover, it does not necessarily turn on any amount having been *credited* to the account (at [43]). So much is accepted by the parties before us. But this is not to say that these matters are irrelevant to the commercial context or significance of the relevant transactions or the characterisation of the account(s) that recorded or reflected them, which context and significance need to be considered in order to answer the ultimate question of the characterisation of the particular account in question.
4. Thirdly, *Consolidated Media* stated at [44]:

In a context in which the relevant record-keeping obligation of a company under Pt 2M.2 of Ch 2M of the Corporations Law was to keep written financial records that correctly recorded and explained its transactions and financial position and performance and that would enable true and fair financial statements to be prepared and audited, it was sufficient for an account to answer the description in s 6D(1)(a) of “an account which the company keeps of its share capital” (emphasis added) that the account, whether debited or credited with one or more amounts, be either a record of a transaction into which the company had entered in relation to its share capital, or a record of the financial position of the company in relation to its share capital.

1. As explained, a “share capital account” could be an account, whether debited or credited with one or more amounts, that was “a record of a transaction into which the company had entered in relation to its share capital”. Alternatively or as well, it could be an account, whether debited or credited with one or more amounts, that was “a record of the financial position of the company in relation to its share capital”.
2. Fourthly, the appellant in some respects in its submissions has sought to parse the language of these descriptions. Moreover, it has understandably sought to bring the buy-back reserve account under either or both descriptions. But care needs to be taken not to decontextualise these descriptions from the factual circumstances that the High Court was addressing, particularly as those descriptions are not the express statutory language. Further, although each description uses the phrase “in relation to”, which words in other contexts can be of extensive ambit, in the present context they resonate more with “concerning”. We, of course, have applied these descriptions but recognise the need for such contextualisation.
3. Fifthly, we would note at this point that there are substantial differences between *Consolidated Media* and the present case including the following. In *Consolidated Media*, it was apparent that the entirety of the debit to the buy-back reserve was intended to reflect a reduction of capital, commercially, economically and legally. That is not the present case. Unlike *Consolidated Media*, in the present context there was a separate debit on the share capital account for that purpose. In the present case the debit on the buy-back reserve account was not intended to and did not reflect such a reduction. In *Consolidated Media*, the debit on the buy-back reserve was to be seen and treated as a charge to “Contributed Equity” (see at [46] and [47]). But as we have set out earlier, in the present case, the debit on the buy-back reserve account was not seen as such a charge. It was seen as a charge on *total* equity. It was only in 2013 that the debit was in substance charged to “contributed equity” or the share capital account effectively by the setting off. Such distinguishing features in and of themselves are sufficient to distinguish *Consolidated Media*.
4. Generally, whatever criticisms may be made of aspects of the primary judge’s characterisation of the transactions or the accounts which recorded them or part of his analysis of *Consolidated Media*, those criticisms do not undermine the essential distinctions set out in the preceding paragraph.
5. Sixthly, before proceeding further it is necessary to be clear about what is meant by “capital” or “shareholders’ capital”. In the present context, we are concerned with share capital rather than other commercial contexts such as working capital. As explained by Gower and Davies’ *Principles of Modern Company Law* (9th edition by Paul Davies and Sarah Worthington) at [11-1], in the present context, “capital” connotes the *value* of the assets contributed to the company by those who subscribe for its shares; we are not, of course, here dealing with the market value of shares. We have emphasised the “value” of what is contributed, as it is this concept rather than the assets themselves (say subscription money) that is being referred to; it may also be appropriate to describe this in terms of the “amount of the share(s)” so contributed (see for example, *Archibald Howie Pty Ltd v Commissioner of Stamp Duties (NSW)* (1948) 77 CLR 143 at 153 per Dixon J). The assets will change their form, indeed may be disposed of or lost. But this is not a reduction of capital as such. Likewise, the company may create or acquire new or enhanced assets through, for example, trading profitably, borrowing money from a third party or asset revaluation. But this is not share capital as such in that form. Moreover, a share capital account is not as such an asset account.
6. The concept of “capital” as used in the present context is also to be distinguished from “equity”. The concept of “equity” usually describes a surplus of assets over liabilities. It is not the same as capital. So, in the present case, for Optus in the year ending 31 March 2002, total equity equalled net assets. Total equity itself can be divided into components. So, for Optus for the year in question, it was divided into “contributed equity”, “reserves” and “retained profits (accumulated losses)”. But the only component of total equity referable to “capital” or “shareholders’ capital” was “contributed equity”. And, as we have indicated earlier, the debit on the buy-back reserve account was not in form or in substance a charge on contributed equity. It was never seen as such commercially or economically by any of the (highly sophisticated) relevant participants (the complete opposite to the scenario in *Consolidated Media*).
7. Seventhly, it is appropriate to make several other points concerning reductions of capital. 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 (see for example, cl 28.1 of Optus’ constitution at the relevant time and generally *Archibald Howie Pty Ltd v Commissioner of Stamp Duties (NSW)* at 152 per Dixon J). 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 (as Dixon J explains), whatever may have happened to the money originally contributed.
8. Further on this aspect, it may be accepted that a buy-back of shares and their cancellation may constitute a reduction of capital. But the question is what the monetary quantification of that reduction is taken to be. It is erroneous to assert that it must be the total consideration paid for the buy-back. After all, part of the consideration may be referable to or reflective of realisable profits or other reserves/accounts other than share capital.
9. Further and relatedly, it is appropriate to make some brief observations concerning Chapter 2J of the *Corporations Act*. Division 2 of Part 2J.1 (ss 257A to 257J) deals with share buy-backs. It was not in dispute before us that the buy-back in the present case was a selective off-market buy-back and that an exemption was given by ASIC under s 257D(4) to the otherwise requirement for shareholder approval under either option set out in s 257D(1). Accordingly, ss 257A and 257B were satisfied. Moreover, cancellation of the shares bought back took place in accordance with s 257H(3). To what extent did the *Corporations Act* treat this as being a reduction of capital? The answer to that question is provided by s 258E, which at the time relevantly provided the following:

**Other share cancellations**

(1) Any reduction in share capital involved in:

(a) the redemption of redeemable preference shares out of the proceeds of a new issue of shares made for the purpose of the redemption (see section 254K); or

(b) a company’s buying-back of its own shares under sections 257A to 257J if the shares are paid for out of share capital

is authorised by this section.

(2) A company may cancel shares returned to it under section 651C, 724(2), 737 or 738 and any reduction in the company’s share capital that is involved is authorised by this subsection.

(3) Any reduction in a company’s share capital because of an order under section 1325A is authorised by this subsection.

1. It can be appreciated from s 258E(1)(b) that in the buy-back context, it was only taken to be a reduction of share capital (and accordingly authorised) “if the shares are paid for out of share capital”. In other words, if the shares are paid for out of something else (ie retained profits or some other reserve), it may not be a reduction of capital at all (and accordingly requires no authorisation). Section 258E does not state or necessarily imply that on a buy-back there is necessarily a reduction of capital and that the buy-back consideration must all be “paid for out of share capital”. But *if* some of it is paid for out of share capital, and there is a reduction to that extent, then that reduction is taken to be authorised (s 256B does not then operate). What is meant by “paid for out of share capital”? We take that to refer to a debiting or charging of share capital of the type identified in Optus’ accounts. The concept “paid for” is not literally referring to payment as such, as a share capital account is not an asset account.
2. We emphasise the difference at this point because of the conceptual confusion in some of the appellant’s submissions. The appellant submitted that because there was no other positive equity account, then the amount debited to the buy-back reserve account must have been paid out of the share capital account and accordingly there had been a reduction of capital also constituted by that debit entry. This is wrong at a number of levels. In reality, the amount debited to the reserve was paid for by the borrowings from SingTel. Further, it was not “paid for out of share capital” in the sense of being *charged* thereto, which is the only relevant context given that the share capital account is not an asset account.
3. Finally, we should make some observations concerning UIG 22 issued in June 1999 after the concept of par value had been abolished. The consensus (see at [4]) was that where shares included in the equity of an entity were bought back, the equity of an entity was required to be directly reduced by the cost of acquisition (total consideration in the present case) of the shares bought back. This is reinforced at [8]. But, importantly for present purposes, what is emphasised at [11] is that:

This Consensus does not prescribe which equity accounts are to be adjusted for the cost of the acquisition of the shares bought back. It allows the accounting for the buy-back to reflect the substance of the buy-back transaction.

1. This reinforces the point that we have made earlier that although the buy-back consideration had to be a charge to equity, it did not all have to be a charge to share capital. Optus’ accounts reflect the substance of what occurred. Part of the consideration for the buy-back was a charge to contributed equity (share capital). The balance was a charge to the buy-back reserve.
2. Having made these general observations on some matters of principle, it is now convenient to address the grounds of appeal under the following subject headings as the appellant has done in its submissions. We have notionally allocated the numbered grounds of appeal to these subject areas, but that exercise is to some extent artificial. Moreover, there is considerable overlap in the grounds of appeal. Accordingly, rather than separately enumerate and proceed in the order of each ground of appeal, it is more convenient to deal with the appellant’s criticisms by reference to subject areas.

## (a) Mischaracterisation of the reserve (grounds 3 and 4)

1. It is said that the primary judge (at [24], [27] and [29]) mischaracterised the buy-back reserve by in effect holding that it was in substance a funding mechanism for the buy-back and that it facilitated the payment of the buy-back consideration.
2. Rather, so the appellant contends, the reserve was newly created and the entries made to record the buy-back were debits. It is said that contrary to the primary judge’s reasons at [24] and [27], there were no amounts “standing in credit in that account” or “standing in the account to pay part of the consideration to shareholders”. It is said that contrary to his Honour’s reasons at [29], there were no “funds in the share buy-back reserve account” and that it played no substantive role as a funding mechanism.
3. We reject these criticisms of his Honour’s characterisation.
4. First, his Honour appreciated that there was no amount “standing in credit” to the buy-back reserve. His Honour appreciated that it had a negative balance at all relevant times (see at [16], [17], [27], [28] and [33]). We do not consider that any looseness of language used by his Honour in [24] should be taken as any indication that his Honour misconceived the true characterisation of the reserve.
5. Secondly, his Honour appreciated that the buy-back reserve was an equity account as distinct from an asset account (see at [16], [17], [27] and [28]).
6. Thirdly, when his Honour used the language of “funding mechanism” and said that the “role played by the buy-back reserve account was to facilitate the payment of the consideration…” (at [24]), his observations should not be decontextualised. His Honour was aware that the assets used to fund the buy-back were moneys borrowed from SingTel (or a related entity). The reserve created and the debit entry were part of the necessary book-keeping or accounting transactions required. In that sense it could properly be said, in a general sense, to be a part of the funding mechanism and in that sense to facilitate what was ultimately occurring.
7. It is also said that the primary judge (at [24]) mischaracterised the transaction by finding that the appellant sold its shares to enable SingTel to acquire them. It is said that the shares bought back were cancelled and therefore not acquired by SingTel. But we reject this characterisation of his Honour’s reasons. His Honour understood that there was no direct sale; see for example at [4] and [25] which indicate that his Honour clearly appreciated that the shares were bought back by Optus and cancelled.
8. Finally on this aspect, even if (contrary to our assessment) his Honour mischaracterised some aspects of the buy-back reserve, that does not avail the appellant. Even on a correct commercial characterisation of that reserve, the appellant still fails. The reserve was not a “share capital account” for the purposes of s 6D(1)(a) and s 159GZZZP for the reasons that we have elaborated on.

## (b) Meaning of “share capital account” (grounds 1, 2, 5 to 15)

### General

1. The appellant contends that an “account” is a record of debits and credits relating to a designated topic. For present purposes, we accept that description. We also accept that a record will answer the statutory description of a share capital account if it is either: (a) a record of a transaction into which the company had entered in relation to its share capital; or (b) a record of the financial position of the company in relation to its share capital. Moreover, we accept that the mere labelling of a reserve may not necessarily answer the statutory description of whether one has a share capital account. Relatedly, we accept that an account will not be precluded from being a share capital account merely because it is not labelled a share capital account or is not an account to which the paid up capital of the company was originally credited.
2. The appellant contends that there is no principle that a share buy-back must involve a return to shareholders of only an amount of share capital which bears the same proportion to the total share capital of the company as the number of shares bought back bears to the total number of shares on issue. It is said that with the abolition of the concepts of par value and nominal share capital, and the possibility of selective share buy-backs, shareholders whose shares are bought back may receive an amount, debited to amounts standing to the credit of share capital, which is disproportionate to the number of shares held in the company. We do not dispute any of these contentions in the generality with which they have been expressed, but they do not take the matter far in the present case for the reasons that we have explained and will explain further.
3. Before proceeding further, it is appropriate that we state our principal views in summary, which generally accord with the primary judge’s analysis.
4. First, the buy-back reserve was an account of equity, not a share capital account.
5. Secondly, the “contributed equity” or share capital account did not require for its understanding any reference to the buy-back reserve (or the debiting thereof) to be made.
6. Thirdly, the only return of capital as such was the proportionate return of capital being the proportion of shares bought back multiplied by the share capital account balance of Optus. This was the amount debited to the share capital account, but not the amount debited to the buy-back reserve. If anything, that latter additional amount was a return *on* capital rather than a return *of* capital.
7. Fourthly, the rulings sought and obtained from the Commissioner, the Implementation Agreement, and the financial accounts and statements of Optus for the year ending 31 March 2002 and thereafter, which we assume (and the experts so agreed) complied with s 286(1) of the *Corporations Act*, all reflect the commercial, economic and legal reality that the debit to the buy-back reserve was not and was not seen to be a reduction or a return of capital. Indeed, the reduction of capital that occurred in 2013 reflected and assumed that prior reality.
8. Fifthly, even though the buy-back reserve obviously concerned shares, this did not make the reserve a share *capital* account. The concept of “capital” is a reference to the value or amount that shareholders had originally contributed.
9. Sixthly, *Consolidated Media* is distinguishable. The buy-back reserve in that case was both a record of a transaction reducing share capital and a record of Crown’s financial position in relation to its share capital. Contrastingly, in the present case the debit entry to the buy-back reserve did not record a transaction reducing share *capital*. Moreover, the reserve and the debit entry recorded Optus’ financial position in relation to part of its *equity*, but not share capital or as described in the accounts, “contributed equity”. The 31 March 2002 Optus’ accounts reflected that reality.
10. The relevant parts of Optus’ accounts are set out earlier at [40] and [41], including note 18 concerning “Contributed Equity” and note 19 concerning “Reserves”. Note 18 recorded a reduction in *contributed equity* by $2,308.1 million and the latter note recorded a debit to reserves of $3,931.8 million. Note 18 also explained:

During the financial year, the company bought back 1,643,098,304 shares … This represented 51.7% of the company’s issued capital. The average cost per share, after including costs incidental to the acquisition of $10.5 million, was $3.797638. Of total costs of $6,239.9 million, $2,308.1 million was charged to share capital and $3,931.8 million was charged to the buy back reserve.

1. The accounts distinguished between equity and share capital. Contrastingly, in *Consolidated Media* at [14], Crown’s financial statements “showed a reduction in ‘Contributed Equity’ of $1 billion from an opening figure of just over $2.4 billion … to a closing figure of just over $1.4 billion”. Crown’s position could not be understood without subtracting the $1 billion total consideration from Crown’s contributed equity of $2.4 billion. That is not the present case.

### Record of a transaction in relation to Optus’ share capital (grounds 5, 6 and 15)

1. The appellant asserted that once it is accepted, as it is said the primary judge did, that: (a) every share buy-back involves a reduction of capital to the extent that the shares bought back are cancelled (at [26]); (b) the Implementation Agreement required that part of the consideration for the buy-back be debited to the share capital account and part to the buy-back reserve (at [16]); and (c) the shares bought back were all cancelled (at [4]), it follows, so the appellant said, that the debit to the buy-back reserve was a record of a transaction in relation to the company’s share capital. It is said that the primary judge erred in concluding otherwise. But with respect, this argument involves a non sequitur. Moreover, as the Commissioner correctly contended, if such a submission was accepted this would lead to the “remarkable” conclusion that all debits to an equity account in a buy-back would necessarily be debits to amounts standing to the credit of a share capital account. The proposition would be even more bizarre if the debits were to an accumulated profits/retained earnings account; counterintuitively, s 159GZZZP would not then operate to treat the amount as a dividend.
2. It is said that the primary judge’s reasons for distinguishing *Consolidated Media*, and concluding that the buy-back reserve was not a record of a transaction reducing Optus’ share capital “are difficult to discern” and are “clearly affected by the factual errors identified” earlier. But as we have said already, a fair reading of the primary judge’s reasons does not disclose factual errors. Further, we do not consider his Honour’s reasons for distinguishing *Consolidated Media* to be opaque or in any way difficult to discern. But in any event this is no answer to the principal distinguishing features that we have identified for ourselves in these reasons.
3. It is said that his Honour’s observation that the transaction in *Consolidated Media* involved a return of capital to the shareholder that was in excess of the needs of the company, and that the substance of the buy-back in the present case involved a company that was “neither reducing nor seeking to reduce its capital by the proposed buy-back, but was seeking to facilitate the substitution of its shareholders” (at [10]), even if correct, was irrelevant to the application of s 159GZZZP. Generally, it is said that there are three flaws in the primary judge’s reasoning.
4. First, it is said that there is nothing in *Consolidated Media* to suggest that the reasoning was limited to cases involving a return of capital to a shareholder “that was in excess of the needs” of the company. There might be a variety of reasons why share capital would be used to buy back shares. It is said that distinguishing the reason for the implementation of the buy-back is not a basis for distinguishing *Consolidated Media*. It is said that the reasoning in *Consolidated Media* makes no reference to this factual aspect of the case being an important, or even relevant, consideration. It is said that the question in the present case is whether analysis of the substance of the arrangement discloses that, in this case, the debit to the buy-back reserve represented share capital used to effect the buy-back.
5. Secondly and relatedly, it is said that whether a company has capital surplus to its needs is irrelevant to a determination as to the character of an amount to be returned to shareholders; cf *Re Westburgh Sugar Refineries Ltd* [1951] AC 625 at 636 where, so the appellant contended, such a consideration was considered by Lord Radcliffe to be irrelevant to whether the Court should approve a return of capital. Similarly, it is said that the issue is irrelevant to whether a company can buy back its own shares under relevant provisions of the *Corporations Act*.
6. As to these two points, we accept that his Honour did distinguish the different buy-backs as between *Consolidated Media* on the one hand, and the present case on the other hand. But his Honour was simply making the obvious point that in *Consolidated Media*, *all* of the consideration for the buy-back was treated as a reduction of capital, whereas in the present case that was not reflected in the commercial arrangements or financial and accounting records concerning the amount debited to the buy-back reserve. His Honour’s observations relating to capital being in excess of a company’s needs was simply part of the context to explain why in *Consolidated Media* all of the consideration for the buy-back was treated as a reduction of capital. His Honour was not saying that the legal question of whether one had a “share capital account” within the meaning of s 6D rose or fell on the question of whether capital was in excess of a company’s needs. His Honour properly focussed on the nature and character of the buy-back reserve, the need for the debit entry and the broader context, including the creation, recording and accounting of and for the subordinated debt. Finally and accordingly on this aspect, we consider *Re Westburgh Sugar Refineries Ltd* to be of little, if any, assistance on the issues with which we need to deal. The issue identified by Lord Reid at 631 has little to do with the issue that we are addressing, it being accepted in that case that on any view there was a reduction of capital, albeit that the assets transferred were valued at more than the share capital; nevertheless the reduction was sanctioned. It is not in dispute that a reduction of capital can be effected in many and varying ways subject to complying with a company’s constitution and legislative requirements.
7. Thirdly, it is said that the fact that as a result of the buy-back arrangement Optus neither reduced nor increased its share capital supports, rather than detracts from, the conclusion that the whole of the purchase price for the buy-back was applied to reduce share capital. It is said that the only way in which the share capital of the company could remain unchanged at the end of the arrangement was if the whole of the purchase price for the buy-back was debited against share capital. It is said that this is because under the Implementation Agreement, the placement was for an amount equal to the buy-back purchase price. Indeed, it is said that the buy-back reserve was set up to account for the buy-back only as no other entries were made to this account until it was set-off against the share capital account in 2013. In our view this contention misunderstands his Honour’s reasoning at [13]. His Honour did not say that as a result of the entire transaction, including the later subscription for shares, Optus’ share capital account remained unchanged. In fact it was altered. The later subscription was in its entirety recorded as an accretion to share capital, whereas the buy-back was recorded only *partly* as a depletion of that account. In saying that the borrowing was not intended to affect the share capital position, his Honour was simply making the point that the borrowing to fund the buy-back was *not* a transaction that affected Optus’ capital position. And that is for the reason that a borrowing is reflected on the balance sheet as giving rise both to an asset (cash) and a liability (the borrowing). It does not of itself affect any account of share capital as such. No substantial criticism can be made of his Honour’s observations at [13]. The primary judge was also correct to observe that the buy-back affected both share capital *and* equity other than share capital (see at [24] and [27]).
8. Generally, we disagree with the appellant’s contention that the primary judge’s findings about the substance of the arrangement lead inexorably to the conclusion that the amount debited to the buy-back reserve was, in fact, a debit to Optus’ share capital account. We also do not agree that the primary judge erred by directing attention to the supposed intention of those implementing the arrangement as indicated by labels used by the parties for the accounting entries in Schedule B to the Implementation Agreement. This was part of the relevant background. We of course accept that the understanding of the parties and the labels used by them to reflect those understandings or planning objectives are not determinative.

### Record of financial position of Optus in relation to its share capital (grounds 7 to 14)

1. The second of the tests identified in *Consolidated Media* directs attention to whether the debit to the buy-back reserve was a record of the financial position of Optus in relation to its share capital. In *Consolidated Media*, it was concluded that the information recorded in Crown’s financial reports relating to the derivation of the figure for contributed equity illustrated that the financial position in relation to its share capital could only be understood by taking into account the debit balance in the share buy-back register. The appellant contends that the same conclusion is demonstrated in relation to Optus by reason of the following matters:

(a) First, the manner of reporting of the buy-back in the financial reports of Optus.

(b) Secondly, the absence of any equity funds, other than share capital, which were available to fund the buy-back.

(c) Thirdly, the clear relationship between amounts debited to the buy-back reserve, and the amount of the replacement share capital subscribed by SingTel, confirming that the latter was a subscription of share capital to replace the former.

(d) Fourthly, the set-off of the debit balance in the buy-back reserve against the account labelled “Share Capital” in March 2013.

1. As to the first matter, it is said that the financial reports recorded the amount of $9,248.5 million as “Contributed Equity” and the amount of $3,931.8 million as negative buy-back reserve, with no buy-back reserve in the previous financial year. It is said that note 18 to the accounts, which related to “Contributed Equity”, revealed that after removing the effect of shares issued under employee share plans, there was: (a) an apparent net increase of $3,921.3 million in share capital as a result of the arrangement; and (b) a corresponding decrease to the buy-back reserve, being a total debit of $3,931.8 million ($3,921.3 million plus $10.5 million in costs incidental to the buy-back). It is said that importantly, both the net increase in share capital and corresponding decrease to the buy-back reserve were described as matters relating to Optus’ “Contributed Equity”.
2. We reject the appellant’s reading and characterisation.
3. The appellant has sought to make the point that note 18 records a net increase in share capital and note 19 records a “corresponding” decrease in the buy-back reserve (after transaction costs are excluded) and that the inference is that they must both relate to contributed equity, as the amounts equate. But the net increase in share capital is as a result of SingTel subscribing shares *subsequent* to the buy-back. That later subscription does not govern the character of the earlier buy-back. Indeed the later subscription was one that may or may not have occurred. As the primary judge correctly found, at the same time as SingTel agreed to ensure Optus had funds to acquire the appellant’s shares, SingTel reserved the right not to call for the issue of replacement shares but instead pay interest on the subordinated debt if it reached 100%.
4. SingTel’s later subscription for shares did affect Optus’ contributed equity. The appellant contends that that increase as well as the decrease to reserves were both “described as matters relating to Optus’ ‘Contributed Equity’”. The appellant relies on note 18 which reported the share buy-back under the contributed equity figures and stated that “$2,308.1 million was charged to share capital and $3,931.8 million was charged to the buy back reserve”. But contrary to the appellant’s position, that statement supports the Commissioner. It confirms that contributed equity was only reduced by the former sum, but not the total of both sums. Further, the fact that part of the description in note 18 referred to the buy-back reserve did not entail that “contributed equity” was affected by or could only be understood by reference to that reserve. The note was simply explaining how the “total costs of $6,239.9 million” had been allocated to make it clear that only $2,308.1 million was being charged to share capital (as the accounting entries set out in note 18 stated).
5. As to the second matter, it is said that notes 18, 19 and 20 to the financial reports made it clear that the only equity funds available to Optus to be utilised to fund the buy-back consideration were the share capital of the company. It is said that the primary judge found that Optus only had two accounts which could have been used to reflect the reduction in shareholder’s equity: share capital and retained losses (at [27]). It is said that there was no suggestion the buy-back could have been debited against the retained losses account. It is said that accounting practices may have permitted Optus to record the buy-back by making debit entries totalling $3,931,788,979 in the buy-back reserve, but the financial position of Optus in relation to its share capital could only be understood by subtracting the debit balance in the buy-back reserve from the credit balance in the share capital account. It is said that the company had no positive equity reserves and no retained profits. It is said that the only available source of equity was share capital. Accordingly, it is said that if, as the primary judge concluded, the buy-back had an impact on the equity of shareholders, and the only positive equity was share capital, a priori the debit to the buy-back reserve was a debit against amounts standing to the credit of an account Optus kept of its share capital.
6. It is said that the primary judge described (at [27]) the buy-back reserve as being “created as a new equity account to carry the negative reserve occasioned by payment of the difference between the total consideration and the amount standing in the credit of the share capital account referrable [sic] to the capital contributed by shareholders”. It is said that there was no legal impediment to that difference being met by Optus returning its share capital to shareholders. It is said to be illogical to suggest that where the only positive equity is share capital, a negative entry of $3,921.3 million in respect of buy-back consideration paid to shareholders is anything other than a return of that share capital to shareholders.
7. It is said that the primary judge concluded that the buy-back reserve impacted equity but did not impact on share capital (at [28]). It is said that the flaw in the primary judge’s analysis is that if the debit to the buy-back reserve did not impact share capital it must have affected some other equity. His Honour’s explanation on this point was that Optus used assets sourced from the Implementation Agreement loans as consideration for the buy-back. It is said however that this confuses the source of the purchase price with the manner of its recording in the accounts. It is said that the buy-back consideration was paid out of Optus’ assets. As a matter of accounting it was necessarily the case that the buy-back element of the arrangement would lead to a reduction in the shareholders’ equity section of the balance sheet. Necessarily, the purchase price paid by Optus had to be reflected in a debit to the shareholders’ equity part of the balance sheet. It is said that the fact that Optus had no positive equity accounts other than share capital cannot be avoided by referring to the fact that the buy-back was funded through the use of assets.
8. We reject these contentions as well. They manifest an error of the type that we have identified earlier at [99] and [100] and confuse or conflate the distinction between capital and equity.
9. The appellant presupposes that there must be a positive equity account. Moreover, the appellant’s submission fails adequately to address the fact that even on its own argument, Optus’ then share capital account balance of $5,327,193,221 was less than the buy-back consideration of $6,225,502,631.68, which would have been insufficient if 100% of the shares were to be bought back.
10. In our view, the appellant’s contentions were rightly rejected by the primary judge. Not every transaction that impacts a company’s equity impacts share capital. It is incorrect to say that Optus’ financial position in relation to its share capital could not be understood without having regard to the buy-back reserve. Notes 18 and 19 make plain that the buy-back affected the equity accounts as described, namely by reducing share capital proportionately and by debiting the balance to the buy-back reserve.
11. The appellant has submitted that the primary judge identified (at [31]) the loaned funds from SingTel as the source of the buy-back consideration, and accordingly has contended that this “confuses the source of the purchase price with the manner of its recording in the accounts”. But his Honour did not confuse such matters. A clear distinction was and is to be made between the published accounts, which showed the impact on equity, and an identification of the *assets* used to pay the consideration. In explaining that “Optus used its assets as consideration”, his Honour was simply observing that the absence of a positive equity account was not an impediment to the buy-back, for assets were available to enable it to be implemented.
12. As to the third matter, it is said that the reporting of the arrangement in this manner was consistent with the economic substance of the arrangement, which it is said the primary judge correctly described “in an economic sense, … as a substitution of the capital which had previously been contributed by its previous shareholder with that funded by its subsequent shareholder” (see at [10]). It is said that the precise alignment of the number of shares bought back with the number issued to SingTel, and of the total amount of the buy-back consideration with the share capital subscribed by SingTel, made clear that the latter was subscribed as a replacement for the former.
13. The appellant criticises the primary judge’s dismissal of that linkage (see at [32]). It is said that this dismissal is unpersuasive in the light of two matters. The first matter is the precise alignment of the number of shares issued to SingTel (and the amount of share capital subscribed by it) with the results of the buy-back. It is said that as a practical matter the subscription could not be completed until after the results of the buy-back were known, and when the number of shareholders who had elected for the buy-back alternative was clear. It is said that the sequence was dictated by the practicalities of the buy-back arrangement. The second matter is that the option of such a subscription being made by SingTel had been expressly provided for in cll 5.1 and 5.2 of the Implementation Agreement.
14. We reject these criticisms as well.
15. The appellant relies on the primary judge’s statement (at [10]) that “in an economic sense” the subscription by SingTel can be seen as a substitution of previous shareholders’ capital. But in our opinion this does not advance the issue. The characterisation of the later subscription transaction, which may not have occurred, does not govern the characterisation of the buy-back, let alone the debit to the buy-back reserve. Further, the appellant has relied on SingTel’s option to subscribe for shares, but has ignored SingTel’s option not to subscribe for shares but instead to receive interest on the subordinated debt if it reached 100% of the shares. The primary judge rightly took this into account. Moreover, SingTel’s subscription was a *subsequent* transaction and was recorded by a credit to the share capital account and a debit to the subordinated debt account.
16. As to the fourth matter, it is said that the purported set-off in 2013 of the debit balance of the buy-back reserve against the share capital account, properly understood, provides confirmation that the debit to the buy-back reserve was from the outset a debit against the share capital of Optus. We disagree. We would have thought that the reverse conclusion follows. In our opinion the set-off more than 10 years later supports the reverse conclusion, namely that the reserve was not an account of share capital or debit against share capital. If the appellant was correct that the reserve was a debit against share capital, then there would have been no need for any reduction of share capital in 2013.
17. Further, it is said that his Honour (at [29]) was incorrect in concluding that s 258E of the *Corporations Act* authorised only the proportion of the buy-back consideration debited to the share capital account as a reduction in share capital. But we see no error; see our earlier discussion on s 258E.
18. Finally, it is said that the conclusion for which the appellant contends is consistent with the legislative purpose of s 159GZZZP. Reference is made to the explanatory memorandum to the *Taxation Laws Amendment Bill (No 3) 1990* (Cth) at pages 20 and 21 which stated that “[i]n broad terms s 159GZZZP will provide that, to the extent that an off-market purchase is funded from a company’s distributable profits, the purchase price will be treated as a dividend paid by the company to the shareholder” (see also pages 4, 5, 16 to 18). It is said that the financial reports show there were no undistributed profits (only accumulated losses) and no other equity amounts, other than share capital, that could have been used to support the buy-back. We do not consider that resort to legislative purpose takes the appellant far. No doubt, s 159GZZZP clearly applies where the buy-back consideration comes from distributable profits, but it is also broader. Its text and evident purpose is that it in essence treats as “profit” any part of the consideration for a buy-back if it is not debited to amounts standing to the credit of a share capital account.

# conclusion

1. None of the appellant’s grounds of appeal has been made good. Moreover, even if the primary judge mischaracterised some aspects of the commercial arrangements, that would not justify a different conclusion on the principal question in any event.
2. The appeal should be dismissed with costs.

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| I certify that the preceding one hundred and fifty-one (151) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Chief Justice Allsop and Justices Middleton and Beach. |

Associate:

Dated: 1 May 2017