



HIGH COURT OF AUSTRALIA

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COMMISSIONER OF TAXATION v HELEN MARY McNEIL

Proceeds of a share buyback scheme are taxable income, the High Court of Australia held today.

Ms McNeil's case is a test case affecting more than 80,000 taxpayers. The costs of the appeal were borne by the Tax Commissioner. In 1987, Ms McNeil acquired a parcel of St George Building Society shares, which in 1992 were converted into ordinary shares in St George Bank Ltd when St George changed from a building society to a banking corporation. St George's profitability increased and in 2001 St George announced a buy-back of ordinary shares worth \$375 million. For every 20 shares held, St George would issue one "sell-back right", which was an option to oblige St George to buy back one share for \$16.50, higher than market value. Ms McNeil held 5,450 shares, meaning she had 272 sell-back rights. The difference between the share buy-back price and the market price meant the value of Ms McNeil's sell-back rights at the listing date was \$514.

Shareholders could elect either to obtain legal title to their sell-back rights in order to sell their shares back to St George or to sell the sell-back rights on the Australian Stock Exchange. Ms McNeil made no election. This meant that St George Custodial, holding the sell-back rights as trustee, was obliged to sell those rights to merchant bank Credit Suisse First Boston. Shareholders could buy extra sell-back rights on the ASX, thereby increasing the number of their shares to be acquired by St George, so a market was created for the sell-back rights separately from the shares themselves. Eleven million sell-back rights were sold to CSFB on 20 February 2001 and these were then sold by CSFB on the ASX. Shareholders such as Ms McNeil who gave no directions about their entitlements were paid the proceeds of trading the sell-back rights on their behalf by CSFB and retained their shares. On 2 April 2001, Ms McNeil received her portion of the proceeds, \$576.64. Of that amount, \$62.64 was the increase in the realisable value of the sell-back rights and Ms McNeil concedes that this was assessable income as a capital gain.

The Tax Commissioner argues that the remaining \$514 is also subject to tax, either as income or as a capital gain. Ms McNeil succeeded in the Federal Court of Australia and the Full Court, by majority, dismissed an appeal by the Commissioner. The Commissioner appealed to the High Court, which allowed the appeal by a 4-1 majority. The Court held that the majority of the Full Court erred in applying principles relating to the derivation of income. It held that whether money received has the character of income depends upon its quality in the hands of the recipient, not upon the character of the expenditure by the other party. The character of the sell-back rights held for Ms McNeil is not determined by her entitlement arising from St George's decision to undertake a share buy-back. Her sell-back rights, which were turned to account on her behalf, did not represent any portion of her existing rights as a shareholder under St George's constitution, but rather were generated by the execution and performance of covenants in the deeds poll establishing the buy-back scheme. The Court held that on the listing date, 19 February 2001, when Ms McNeil's sell-back rights were granted by St George to St George Custodial for her benefit, there was a derivation of income by her, represented by the market value of her rights, namely \$514.

- *This statement is not intended to be a substitute for the reasons of the High Court or to be used in any later consideration of the Court's reasons.*