SANDON CAPITAL

Sandon Capital Pty Ltd
ABN 98 130 853 691
AFSL 331 663
Level 5, 139 Macquarie Street
Sydney NSW 2000
Tel 02 8014 1188 Fax 02 8084 9918

The Directors
A2B Australia Limited

[redacted]

19 January 2022

Dear Directors,

We are writing to raise concerns we have regarding A2B Australia Limited's (**A2B** or **the Company**) property assets, in particular the reported fair value of the property located at 9-13 O'Riordan Street Alexandria (**the O'Riordan Street Property**). These concerns raise serious issues regarding the proposal to swap the O'Riordan Street Property and the potential resulting tax consequences.

<u>We believe the Company should immediately abandon plans for the proposal to swap the O'Riordan Street property.</u>

Over many years, A2B's property portfolio has grown to be worth vastly more than its reported book value. The 2021 Annual Report acknowledged this explicitly when it noted that, following an independent valuation, the fair value of the Company's land and buildings ($81.1 million) is significantly higher than the reported book value ($10.7 million). Despite this disclosure of the revised fair value, we believe the market value of Company's property assets is significantly higher.

O'Riordan Street's Fair Value

To validate our assessment of the value of A2B's O'Riordan Street Property, we commissioned an independent indicative assessment from respected independent property valuers, JLL Australia (**JLL**). Based on JLL's assessment, we believe the O'Riordan Street Property is worth significantly more than the $57 million value adopted by the Company. [1] In JLL's most recent report to us, they considered the value of the O'Riordan Street property on an "as is" basis and having regard for its commercial redevelopment potential. Their indicative assessment of the value of the O'Riordan Street Property was $77.4 million. [2]

Further evidence that the O'Riordan Street Property is worth far more than the value adopted by the Company came very recently when the NSW Valuer-General (**the Valuer-General**) announced its annual review of land values. As of 1 July 2021, the Valuer-General valued the land-only component of the O'Riordan Street Property at $71.0 million.[3]

If a public marketing campaign were to be conducted ***and development approvals were obtained***, we believe that the market price of this property would likely exceed both these valuations significantly.

[1] As disclosed in the ASX announcement on 17 November 2021.

[2] We acknowledge the conclusions of the indicative assessment are limited by the fact only limited external and/or kerbside inspections were undertaken. Given the under-developed nature of the property, we do not believe this lack of access impedes meaningful insights.

[3] NSW Valuer-General online land value search for property number 2138398 (https://www.valuergeneral.nsw.gov.au/services/lvs.htm?execution=e3s1)

While Directors may feel that an August 2021 valuation of the O'Riordan Street Property may be sufficiently up to date, we believe the Valuer-General's latest land value assessment – that is 25% above this August valuation – warrants an immediate and thorough independent review by the Company. Our view is strengthened by the work undertaken by JLL on our behalf and we expect that other shareholders would agree.

Reporting of the fair value of the O'Riordan Street Property

We believe the Company has materially under-reported the value of its property assets for some time, notwithstanding the recent disclosure in the FY21 Annual Report.

The timing of the property revaluation on the same day as the release of the Annual Report, would indicate that the Company had set its mind to obtaining an independent valuation of the property assets well before the signing of the accounts on 26 August 2021. However, there is no mention of the possibility of such a substantial property revaluation in section 7, entitled "Events Subsequent to reporting date" of the Annual Report. Nor is there any mention of any property revaluation in the "Outlook" section of the financial reports on page 24, to which the "Likely Developments" section refers the reader. The only mention is in Note 10 on page 57 of the 2021 Annual Report.

We find it curious that such a substantial property revaluation does not warrant mention in the audited accounts as an "event subsequent" or at least as a "likely development".

The reporting of the fair value of the Company's property assets is important. Readers of the financial reports produced by the Company do so to gain an understanding of the Company's performance and net worth. They may also use the information in the financial reports to attribute a value to the Company. The importance of these disclosures cannot be understated.

As you know, each year ASIC highlights areas for attention in financial reporting. In early June 2021[4], ASIC highlighted its "key focus areas" for the reporting periods ending 30 June 2021. ASIC expected directors, preparers of financial reports and auditors to pay attention to, inter alia, "*asset values*", "*events occurring after year end and before completing the financial report*" and "*disclosures in the financial report and Operating and Financial Review.*"

In the attachment to the media release, ASIC listed seven examples of matters that may require the focus of directors, preparers and auditors in relation to the values of property assets. On 9 December 2021, ASIC practically repeated these focus areas for consideration ahead of the 31 December 2021 half year reporting period.

We believe ASIC's stated position demand that the Directors obtain updated independent valuations of the property holdings, in particular the O'Riordan Street Property. A failure to do so exposes all those involved in preparing the Company's financial reports to criticism of non-compliance and potential losses by the Company.

Adverse tax consequences of the Proposed Land Swap

Based on the information provided, we believe the proposed land swap may lead to significant, and adverse, tax consequences for the Company. Please note, we are not purporting to provide any tax advice. Rather, based on our understanding of how tax would generally be levied, we are raising issues we believe the Company has either overlooked or failed to disclose.

[4] ASIC Media Release, 10 June 2021, 21-129MR "ASIC highlights focus areas for 30 June 2021 financial reports under COVID-19 conditions".

If the land swap occurred as described in the Memorandum of Understanding (**MoU**) Announcement on 17 November 2021, we believe the Australian Tax Office (**ATO**) would likely argue that A2B would be disposing of its current land in consideration for two lots of property:

1. Unencumbered land value of the properties at 20-24 Bourke Road; plus

2. The right to have a commercial office block constructed on the premises at no charge.

Subsection 116-20(1) of the 1997 Tax Act states that:

"The capital proceeds from a CGT event are the total of … the market value of any other property you have received, or are entitled to receive, in respect of the event happening (worked out as at the time of the event)"

It would be a question of fact and valuation what each item of property (that is, points 1 and 2 above) would be worth at the time of the sale. However, there is a strong risk, and in our view very likely, that the ATO would argue that the combined value would be the "estimated value" of $135 million, as disclosed in the MoU Announcement. [5]

If the ATO was to argue this, there would be a capital gain for A2B equal to the difference between its tax cost (generally, the purchase price of the O'Riordan Street Property) and $135 million, at 30%.

Given that this land swap would not generate any cash, the tax payable on such a sale could cause a cash strain on A2B and potential short term liquidity issues. This is a problem with all barter type transactions. However, where a barter type transaction is coupled with "marketing" (such as the MoU Announcement) which places a very high value on the property to be received, we suspect the ATO would generally seek to tax the maximum capital gain.

One of the advantages of A2B today is that its balance sheet is unencumbered. The potential tax liability of the proposed transaction could be tens of millions. The Company does not have sufficient cash to pay such an amount and would likely need to borrow to pay the tax. We doubt shareholders would be very supportive of such borrowings.

The Proposed Land Swap should be abandoned

The fair value of the properties is typically a theoretical question, especially when there is no intention to sell the properties. As of 17 November 2021, when the MoU to facilitate a proposed land swap with Addenbrooke Pty Ltd was disclosed, A2B made the property values a practical question, not a theoretical one.

The Company has sought to present the proposed property swap as a transaction where it would swap a property it values at $57 million (as of August 2021) for land upon which a new property will be built that will be worth an "estimated" $135 million.

We consider the transaction proposed by the MoU Announcement is uncommercial and not in the best interests of shareholders.

[5] We note the announcement provided no basis for this "estimated" value.

As shareholders, we prefer to contemplate the proposed property swap from a different perspective: The Company will swap a property whose 8,489 square metres of land is valued at $71.0 million for a property whose 2,449 square metres of land is valued at $19.6 million and be left with a potentially significant unfunded capital gains tax liability.[6] This simply does not stack up for the Company. It also leads to serious questions about the Directors' judgement and compliance with their duties.

We believe the proposed land-swap transaction that was described in the announcement made to the market on 17 November 2021 must be abandoned immediately.

Whilst we doubted the commercial rationale when first announced, the increase in the value of the land, the change in relative values of each other properties subject to the land swap and the potential for significantly adverse tax consequences, have done nothing but galvanise our views. As an MoU is not a legally binding document, abandoning it should be straightforward.

Given we believe these matters could have a serious impact on the value of the Company, we will be sharing our views with other shareholders.

We look forward to meeting with you all on 2 February. In the meantime, if you have any questions or would like to discuss this matter further, please email me at gabriel@sandoncapital.com.au or feel free to call me on 0408 936 357.

Yours sincerely,

Gabriel Radzyminski

Director, Sandon Capital Pty Ltd
Investment manager of Sandon Capital Activist Fund, Sandon Capital Investments Ltd and Sandon Capital Master Fund.

[6] We have used the NSW Valuer-General's 1 July 2021 values for each property.