Australian Securities and Investments Commission

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Dr. John Camacho and Dr. Arthur Walsh

By email: john.rebirth2018@gmail.com;
dr.arthurwalsh@yahoo.com

Our Reference: CCU 19-0640
Your Reference: N/A

4 November 2019

Dear Dr. Camacho and Dr. Walsh

Re: Smiles Inclusive Limited ACN 621 105 824

Thank you for the following correspondence addressed to the Chair of the Australian Securities & Investments Commission (**ASIC**):

- letter dated 3 October 2019, in which you raised concerns about the rights issue being conducted by Smiles Inclusive Limited (**SIL**) based on potentially false and misleading information;

- letter dated 16 October 2019, in which you queried whether the alleged intention of the SIL directors to rely on the safe harbour protections in s588GA of the *Corporations Act 2001* (Cth) (**Corporations Act**) should be disclosed to the market; and

- email dated 28 October 2019, in which you have raised concerns about the lack of disclosure to the market about changes in substantial shareholdings, as well as directors' interests in SIL as a result of the recent rights issue conducted by SIL.

The Chair has asked me to respond to your correspondence on his

behalf. **We have made enquiries with SIL in relation to:**

- **the rights issue and the disclosures of SIL's FY19 statutory loss.**

- the alleged intention of the SIL directors to rely on the safe harbour provisions in the Corporations Act.

In relation to your concerns about the rights offer, as a result of our enquiries, SIL agreed to take remedial action to mitigate any potential harms to investors.

In relation to your concerns about non-disclosure of reliance on the insolvency safe harbour, we note that ASX Guidance Note 8 on continuous disclosure specifically deals with this issue. It provides that ASX does not ordinarily expect reliance on the safe harbour to be disclosed. To the extent that your concern also relates to disclosure about the company being in financial difficulties, we note that this has been disclosed to the market and appears to be widely known and we therefore have not at this time identified a contravention of the continuous disclosure provisions based on information currently available to us.

We note your concerns in relation to substantial shareholder notices and note that these are obligations of the substantial shareholders, and not obligations of the company. Notwithstanding this, we are continuing to assess this information. We understand that on 30 October 2019 notices were lodged with the ASX to notify the market of changes to directors' interests as a result of the rights issues.

We appreciate you spending the time to bring this matter to our attention and are continuing to monitor the situation. Due to the confidentiality restrictions placed upon ASIC by virtue of section 127 of the *Australian Securities and Investments Commission Act 2001* (Cth), we cannot disclose to you any information received by us in connection with the exercise of our powers.

If further information comes to light regarding this matter, please feel free to contact us again.

Yours sincerely

RHowitt

Rachel Howitt
Senior Executive Leader, Corporations

5. FY 2019 FINANCIAL PERFORMANCE

The first 12 months of operations for Smiles Inclusive has been dominated by poor financial performance, the protracted attempt to regain control of the company by the former CEO and Chairman and the public disruption efforts by a few opportunistic individuals. The actions of these individuals continue to be addressed by the Board and Management, with the support of the majority of the JVP group.

The preliminary financial report, released to the market on 30 August 2019, declared an underlying loss after tax of $4.497 million.

Reconciliation from Statutory to Underlying Financial Results	30 Jun 19	30 Jun 18	Movement up/(down)	
	$'000	$'000	$'000	%
Statutory loss after tax	**(18,878)**			
Integration costs	549	307	**242**	78.8%
Business acquisition costs: once-off costs	391	2,648	**(2,257)**	(85.2)%
Impairment of assets	13,700	-	**13,700**	N/A
Income tax effect of adjustments	(259)	(813)	**554**	68.2%
Underlying loss after tax	**(4,497)**	**(2,813)**	**(1,684)**	(59.9)%

Actual Statutory Loss $31m - Published on 30 September 2019 - 2 days BEFORE this document was dispatched to Smiles shareholders

The poor underlying financial result was driven by the following factors:

Revenue Losses

- The necessary temporary closure of the Smiles on Site mobile business and the unfortunate passing of the specialist JVP in Woollahra within Q1 of listing
- Underperformance of many practices compared to their pre-acquisition revenue levels.
- Breakdown of relationships with some Joint Venture Partners (JVP's), which has led to a low level of engagement.

Cost Overruns

- Poor execution of an unrealistic implementation strategy for the Smiles business establishment, practice integration and future business planning with JVPs/Practice Leaders.
- Failure to develop appropriate business systems processes and people to deliver the business model.
- Litigation issues which have and continue to distract management from the operations of the business and result in significant legal costs.

The Company's result for FY19 remain unaudited. The audit process could result in a materially adverse adjustment of these results, including an impairment of the value of the practices (which would be a non-cash adjustment on the balance sheet). The Company has not received any indications as to whether or not its audited accounts may be subject to a modified opinion, emphasis of matter, or other matter.

Actual Cash Position as at 30 September 2019
$345K (per Smiles 4C)

5. CURRENT FINANCIAL POSITION

	30-Jun-18 $'000	Unaudited 30-Jun-19 $'000	Impact of Rights Issue $'000	Pro-forma Post Rights Iss $'000
Assets				
Cash and cash equivalents	2,009	1,595	765	2,360
Receivables	2,813	3,491		3,491
Inventories	-	558		558
Deferred tax assets	2,631	4,393		4,393
Property, plant & equipment	3,681	10,596	750	11,346
Intangible assets	62,208	49,272		49,272
Total Assets	**73,342**	**69,905**		**71,420**
Liabilities				
Payables	5,186	6,944	(890)	6,054
Deferred revenue	564	570		570
Provisions	2,087	2,405		2,405
Interest bearing liabilities	10,940	23,413	(675)	22,738
Joint Venture Partner Contribution	21,435	21,109		21,109
Total Liabilities	**40,212**	**54,441**		**52,876**
Net Assets	**33,130**	**15,464**		**18,544**
Contributed equity	38,085	39,297	3,080	42,377
Retained earnings	(4,955)	(23,833)		(23,833)
Total Equity	**33,130**	**15,464**		**18,544**

- Property Plant and Equipment: This balance comprises practice dental, IT and office equipment and fit-outs, the mobile business trailers and motor vehicles. The movement is predominately attributable to the capitalization of leased assets.
- Goodwill: Goodwill was taken up as the difference between the purchase price of the practices and the net tangible assets acquired. At balance date, its carrying value was compared, on a practice by practice basis, to the likely future cashflows of the practice and to the market capitalization of the company, in accordance with current accounting standards.
- While management believe practice performance is recoverable, assessment of the balance was required as at 30 June 2019. Consequently, the overall poor financial performance in FY19, together with the higher than expected costs involved in establishing the business to date, required impairment of the balance of goodwill as at 30 June 2019.
- Joint Venture Partner Contribution: The JVP program is an investment in the ongoing financial performance (EBIT) of a practice. Although divisible and transferable, it does not represent a share in the ownership of the underlying practice. Future sales of a JVP interest may or may not be more or less than the amount invested by the JVP, depending on the performance of the practice.
- Similar to goodwill, this balance is required to be revalued each financial year, using the likely future discounted cashflows of the practices. The carrying amount, is affected by the poor financial performance of the practices in FY19.
- In the release of the preliminary financial result, the net impact on the revaluation of the goodwill and JVP Contribution balances, has been quantified at $13.7 million, however this amount is subject to audit.
- Interest Bearing Liabilities: Included in this balance is approximately $19 million owing to the business' primary banker NAB. Subject to servicing exiting commitments, the next review date is the end of November 2019.

The Company's result for FY19 remain unaudited. The audit process could result in a materially adverse adjustment of these results, including an impairment of the value of the practices (which would be a non-cash adjustment on the balance sheet). The Company has not received any indications as to whether or not its audited accounts may be subject to a modified opinion, emphasis of matter, or other matter.