DIATREME RESOURCES LIMITED

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ASX Code: DRX

28 May 2008

Dear Shareholder

RE: IN SPECIE DISTRIBUTION OF SHARES IN XTREME RESOURCES LIMITED OCTOBER 2007

This information is for the benefit (only) of those eligible shareholders in Diatreme Resources Limited (DRX) who, effective 11 October 2007, received an in specie distribution of shares from DRX in the subsidiary company, Xtreme Resources Limited (XRL).

Your directors recently sought professional advice on the taxation implications for DRX shareholders in respect of the reduction of capital undertaken by way of the in specie distribution. That advice, dated 21 May 2008, and provided by Pitcher Partners, Accountants Auditors & Advisors, is enclosed.

It is recommended that all shareholders who received shares in XRL review the summary and then seek their own taxation advice in order to understand how the reduction of capital applies to their own particular circumstances.

On behalf of the Board

LAWRIE LITZOW
Corporate Secretary

Encl: Pitcher Partners, Accountants Auditors & Advisors letter dated 21 May 2008

Manage your holdings online

The Company's share registry, Link Market Services, operates an online Investor Service Centre allowing shareholders to create, view and manage their Company holdings. Details may be found on their website at www.linkmarketservices.com.au.

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21 May 2008

The Directors
Diatreme Resources Limited
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Dear Directors

You have requested that we provide a summary of the taxation implications for the shareholders of Diatreme Resources Limited (DRX) in respect of the reduction of capital undertaken by way of an in specie distribution of the shares DRX owned in Xtreme Resources Limited (XRL). We have outlined the taxation implications in the following Taxation Summary for Shareholders.

The following summary is not intended to constitute taxation advice in relation to the specific circumstances of DRX shareholders. The taxation position of DRX shareholders with respect to the reduction of capital will depend upon their own particular circumstances. The summary is not applicable to all categories of DRX shareholders. In particular, it applies to DRX shareholders who are residents of Australia for tax purposes and who hold their DRX shares as capital assets. The summary does not apply to DRX shareholders who are not residents of Australia for tax purposes or to DRX shareholders who hold their DRX shares as trading stock or on revenue account.

We recommend that DRX shareholders seek their own taxation advice in order to understand how the reduction of capital applies to their own particular circumstances.

TAXATION SUMMARY FOR SHAREHOLDERS

General

As stated in the Explanatory Notes to the Notice of a General Meeting of Shareholders, the reduction of capital undertaken by DRX by way of an in specie distribution of XRL shares to DRX shareholders is an Equal Capital Reduction under the Corporations Act 2001. Each DRX shareholder has received one (1) XRL share for each four (4) DRX shares they held on the Record Date (11 October 2007).

The taxation implications arising to the DRX shareholders under Resolution 4 (Equal Capital Reduction) as detailed in the Notice of Meeting, and passed by DRX shareholders at the Meeting held on 4 October 2007, is set out below.

Capital Reduction

Is the Distribution Assessable as a Dividend?

Having regard to the reasons for the Capital Reduction by DRX as detailed in the Explanatory Memorandum, it is evident that the Capital Reduction is to reduce DRX's capital base, separate gold mining assets and maximise value for DRX shareholders.

It is our opinion that the in specie distribution of XRL shares to the DRX shareholders is not an assessable (or deemed) dividend for income tax purposes. Whilst the Capital Reduction may constitute for tax purposes a demerger benefit and capital benefit to some DRX shareholders, it is considered that any tax benefit is merely incidental. The Capital Reduction is not attributed to the profits of DRX, nor does DRX's pattern of distributions indicate that it is being paid in substitution for a dividend.

Application of Demerger Tax Relief

DRX shareholders will be eligible for demerger relief under the capital gains tax (CGT) demerger relief provisions. In broad terms, under this demerger relief, DRX shareholders can choose rollover relief to defer the CGT consequences in respect of the CGT event that happens to their DRX shares upon the Capital Reduction.

CGT Consequences – Treatment of the Capital Reduction

As stated in the Explanatory Memorandum, the Capital Reduction is by way of an in specie distribution of XRL shares.

The Capital Reduction will not result in a capital gain or capital loss for DRX shareholders who choose for the CGT demerger relief to apply.

If a DRX shareholder chooses to utilise CGT demerger relief, the CGT consequences may be summarised as follows:

- the Capital Reduction will impact upon the calculation of the CGT cost base of existing DRX shares and determine the CGT cost base of the XRL shares;

- the CGT cost base and reduced cost base of each DRX and XRL share acquired or deemed to be acquired on or after 20 September 1985 (post CGT) will be determined in relation to each DRX shareholder by reasonably apportioning the cost base and reduced cost base of the post CGT DRX shares held by that DRX shareholder before the Capital Reduction between DRX and XRL shares held after the Capital Reduction.

- DRX shareholders must base their apportionment on the market values or a reasonable approximation of the market values of DRX shares and XRL shares just after the Capital Reduction.

  Example:

  Assume, for illustrative purposes only, the market value of each XRL share is $0.039. Based on this market value of each XRL share, XRL represents 15.59% of the market value of the DRX group (based on the market value of DRX's shares on 12 October 2007 of $0.25).

  In this example, a DRX shareholder owns 10,000 post CGT DRX shares. The DRX shareholder's CGT cost base per DRX share is $0.20, being a total of $2,000.00. The DRX shareholder chooses CGT demerger relief in respect of all its DRX shares.

  As a result of the Capital Reduction, the cost base will be apportioned between the shareholder's 10,000 DRX shares and the 2,500 XRL shares it acquires as a result of the Capital Reduction. The apportionment will be as follows:

  - *the cost base of its DRX shares will be $0.1688 per share;*
  - *the cost base of its XRL shares will be $0.0312 per share; and*
  - *the sum of the cost bases of its DRX shares and its XRL shares will be $2,000.00 (ie 10,000 @ $0.1688 + 2,500 @ $0.0312), being the same as the total cost base of the DRX shareholder's DRX shares prior to the Capital Reduction.*

To assist DRX shareholders, we have attached a table illustrating the effect of the apportionment requirements of the demerger relief on the cost base of the DRX shares and how it establishes the cost base of the XRL shares (refer Appendix A).

Disposal of DRX Shares

For DRX shares acquired post CGT, the CGT demerger relief provisions adjust the CGT cost base of those shares as discussed above.

The calculation of any capital gain on a subsequent disposal of the post CGT DRX shares is dependent upon a number of factors, including the type of entity that owns the shares and the period for which the DRX shares are held prior to disposal.

Where the DRX shares are held by individuals, trusts or complying superannuation funds for more than 12 months prior to disposal, such shareholders may be entitled to a CGT discount in calculating the amount of the assessable capital gain. The relevant discount for individuals and trusts is 50%, while that applying to complying superannuation funds is 33⅓%. Companies are not entitled to any CGT discount.

Where the post CGT DRX shares are disposed of for a price less than their reduced cost base, a capital loss may arise.

Disposal of XRL Shares

For XRL shares acquired in specie in relation to DRX shares acquired post CGT, the CGT demerger relief provisions deem those XRL shares to have been acquired post CGT at the date the DRX shares were acquired.

The same CGT consequences arise to the DRX shareholders on the disposal of their post CGT XRL shares as described above in respect of any disposal of post CGT DRX shares.

CGT Consequences – No CGT Demerger Relief

DRX shareholders who do not choose for the CGT demerger relief to apply will have the same tax consequences as those detailed above subject to the following exceptions:

- If the portion of the market value of the XRL shares received per DRX share (ie the non-assessable distribution) is greater than the relevant cost base of the post CGT DRX share, the DRX shareholder will make a capital gain.

- The adjustment to the CGT cost base of the DRX shares held by DRX shareholders and the CGT cost base of the XRL shares acquired in specie are determined in the same manner as if the CGT demerger relief applied (refer above).

- All of the XRL shares transferred in specie to the DRX shareholders are treated as post CGT shares and having an acquisition date being the date when the in specie distribution is made, rather than the deemed acquisition date being the time when the DRX shareholders acquired their DRX shares.

- As all the XRL shares will be post CGT shares, the CGT discount may apply on a subsequent disposal where such XRL shares are acquired by individuals, trusts or complying superannuation funds and held for more than 12 months from the date of the in specie distribution.

Tax Reform

This summary is based on our understanding of the Capital Reduction undertaken by DRX, and our interpretation of the relevant income taxation legislation in force at the date of this summary. We have summarised the general Australian income taxation implications arising to Australian resident DRX shareholders holding their DRX shares on capital account. However, given the ongoing changes to the income tax law, the Government's proposed reform of the tax system, and that the taxation consequences can vary based on a shareholder's circumstances, it is recommended that DRX shareholders seek their own independent taxation advice in respect of the Capital Reduction undertaken by DRX.

Yours faithfully
PITCHER PARTNERS

Daryl Jones

DARYL JONES
Partner

APPENDIX A

DRX SHAREHOLDERS CGT COST BASE		
Original Cost Base of DRX Share $	**Post-demerger Cost Base of DRX Share $**	**Post-demerger Cost Base of XRL Share[(1)] $**
0.10	0.08440	0.0156
0.15	0.1266	0.0234
0.20	0.1688	0.0312
0.25	0.2110	0.0390
0.30	0.2532	0.0468
0.35	0.2954	0.0546
0.40	0.3376	0.0624
0.45	0.3798	0.0702
0.50	0.4220	0.0780
0.55	0.4643	0.0857

[(1)]The Cost Base of each XRL share represents 15.59% of the Original Cost Base of each DRX share.