IN THE HIGH COURT OF THE COOK ISLANDS
HELD AT RAROTONGA

OA No. 3 /93

IN THE MATTER of the Cook Islands International Companies Act 1981-1982

AND

IN THE MATTER of Section 66 of the Trustee Act 1956 as applicable in the Cook Islands pursuant to Section 639 of the Cook Islands Act 1915 and Article 77 of the Constitution

AND

IN THE MATTER PACIFIC INVESTMENT FUND LIMITED a Company incorporated under the Cook Islands International Companies Act 1981-1982 having its registered office at Rarotonga, investment fund company.

Applicant

Hearing: 9 December 1993
Counsel: Mr B H Giles for Company in support
Mr G V Hubble appointed by the Court to represent shareholders
Judgment: 9 December 1993

REASONS FOR JUDGMENT

The applicant company was incorporated under the Cook Islands International Companies Act 1981-82 as an investment company. It was initially administered from the Cook Islands, but in 1988 changed to being administered from New Zealand and accordingly became New Zealand tax resident. The management, acting on advice which turned out to be erroneous, filed tax returns in New Zealand as a result of which the company was assessed for income tax and payments of tax were made as follows:

13 November 1989 first provisional 1990:	$ 70,000.00
7 March 1990 terminal 1989:	541,953.00
7 March 1990 second provisional 1990:	130,000.00
18 June 1990 third provisional 1990:	100,000.00
	$841,953.00

These payments were made upon the basis of the mistaken belief by the management that the company was an investor in shares rather than a trader in shares. As a result no claim was made to set off losses incurred following the 1987 sharemarket crash. Those losses had been substantial, amounting to $15,745,048.

Following a change in the company's management fresh advice was taken as to the company's tax position and that advice was that the company should have been treated as a trader in shares with the consequent right to set off previous losses. This advice was plainly correct and was duly accepted by the Commissioner of Inland Revenue with the result that the company was re-assessed. On 24 February 1992 a refund of the total tax paid, namely $841,953, was received by the company.

The question then arose as to how the refund should be treated, and more particularly, as to who should receive the benefit of it. Accordingly the present application was made seeking the directions of the Court. On an interlocutory application Mr G V Hubble, a barrister and solicitor of Auckland, was appointed by the Court as counsel to represent the interests of all shareholders.

A full history of the facts was put before the Court in affidavit form, and written submissions were made by Mr Giles, counsel for the company, and by Mr Hubble. Both counsel duly appeared on the hearing of the application.

I do not propose to set out all the facts and the various considerations dealt with. These all appear from the documents filed. I set out only a summary of the position sufficient, I believe, to enable an understanding to be obtained of the basis upon which the decision was given.

The money subscribed to the company was invested and the total investment fund was valued monthly. Shareholders were able to redeem all or part of their shares upon the basis of the current monthly valuation. There was, therefore, a changing number of shareholders, and a changing value in the investment fund depending upon the way in which the fund was being managed.

The problem which arose following the tax refund was to determine which of the company's shareholders should benefit from what was, in effect, a windfall.

Six potential classes of shareholders were identified as possible beneficiaries of the refund:

1. All those who held redeemable shares as at the date of the particular tax payment irrespective of whether they have since redeemed or not.

2. All those shareholders who actually disposed of their shares upon the valuation date next after the date of the tax payments. These are a sub-class of Class 1.

3. All those who held redeemable shares as at the date of the tax payments and who continue to hold those shares. These are a second sub-class of Class 1.

4. All those who held redeemable shares in the Fund at the first valuation date following advice of a confirmed tax position.

5. All those who have redeemed shares at any time after the tax payments were made, irrespective of when they acquired shares. This is an expansion of Class 2.

6. All those shareholders who purchased shares at the time the company became New Zealand tax resident, whether their shares were redeemed or not.

Each of these possible classes was considered but both counsel concluded that only those in Class 1 could properly be regarded as entitled to benefit from the refund. With this view I was in agreement and made an order to that effect.

There seemed no doubt that any benefit from the refund had to be regarded as accruing to shareholders as distinct from the company as a separate entity. It was impossible to determine what might have been

the effect on individual shareholders in their decisions whether to redeem shares or not at any given moment had they been aware that the tax payments ought not to have been made. If those payments had not been made the monthly valuations would presumably have been affected, but it would only be a matter of speculation as to whether the difference would have been such as to have resulted in different decisions being made. Any attempt to identify the possible impact on the shareholders in any of the six classes could have been no more than guesswork.

In these circumstances I was satisfied that it was necessary to take a broad and practical view of the matter and to direct that the refund should be distributed to the class of persons who created or funded it. This view is, I think, supported by several considerations:

1. The refund arises from a fundamental error of law and of fact which ought not to have occurred.

2. Had that error not occurred the payments would not have been made, and the fund should, in effect, be restored to its condition if the money had never left the company.

3. The payments were made from existing cash resources and did not involve any borrowed money.

I do not consider any satisfactory argument can be advanced to say that any of the other five classes of shareholders have a better right than those in Class 1.

This was the basis upon which I was prepared to direct that the refund was to be held by the company for those shareholders who held shares in the company on the respective dates of payment of the tax.