Neutral Citation Number: [2005] IEHC 41

THE HIGH COURT

2003 No. 570 COS

IN THE MATTER OF WOOD PRODUCTS (LONGFORD) LIMITED AND IN THE MATTER OF AN APPLICATION PURSUANT TO SECTION 160 OF THE COMPANIES ACT, 1990 AS AMENDED AND IN THE MATTER OF AN APPLICATION PURSUANT TO SECTION 160 (6A) OF THE COMPANIES ACT, 1990 AS AMENDED

BETWEEN

THE DIRECTOR OF CORPORATE ENFORCEMENT

APPLICANT

AND

PATRICK McGOWAN AND PATRICIA McGOWAN

RESPONDENTS

Judgment of Miss Justice Laffoy delivered on 24th February, 2005.

The application

1. This is an application by the Director of Corporate Enforcement (the Director) seeking disqualification orders in relation to each of the respondents pursuant to para. (d) and/or para. (f) of s. 160 (2) of the Companies Act, 1990 (as amended).

The factual background

2. Wood Products (Longford) Ltd. (the Company) was incorporated on 2nd January, 1975. When these proceedings were initiated the respondents were the only directors of the Company.

3. On 25th June, 1999 the Company was struck of the Register of Companies and was subsequently dissolved on 2nd July, 1999 due to its failure to file annual returns pursuant to s. 12 of the Companies (Amendment) Act, 1982. In 2001 a creditor of the Company, ACC Bank Plc, brought proceedings in this court to have the Company restored to the register. By order of the court (O'Neill J.) made on 14th May, 2001, it was ordered that the Company be restored to the register. It was further ordered that within three months from the date of the order the respondents deliver all outstanding annual returns to the Registrar of Companies. The outstanding annual returns related to each year from and including 1990, the last annual return filed in 1991 having related to the year ended 31st December, 1989. It was further ordered that the respondents deliver to the Revenue Commissioners within three months from the date of the order the following outstanding returns:

(a) Corporation tax for the years ended 31st December, 1988 to 31st December, 2000;

(b) P35 returns for the years ended 5th April, 1997 and 5th April, 1998;

(c) P30 returns for the months ended 5th May, 2000 and 5th April, 2001; and

(d) Form VAT 3 for September/October, 1999.

4. It appears from the order that the Company was represented by counsel at the hearing of the application. In any event, both respondents were notified of the making of the order by letters dated 12th June, 2001, which were despatched by registered post, in which they were requested to deliver the outstanding returns without delay. When these proceedings were commenced the outstanding annual returns had not been delivered to the Companies Registration Office (CRO).

5. Further, when these proceedings were commenced the outstanding tax returns listed in the order of 14th May, 2001 had not been furnished to the Revenue Commissioners. In fact, on the application of the Revenue Commissioners, this court (Carroll J.) made an order on 13th October, 2003 extending for a period of two months the time within which the respondents were to deliver to the Revenue Commissioners the outstanding tax returns as listed in the order of 14th May, 2001. By this time the Revenue Commissioners had obtained two judgments against the Company. The first obtained in the Circuit Court on 11th February, 2003 and was for €33,525.41 together with the sum of €589 for costs. The second was obtained in this court on 12th May, 2003 and was for €246,287.63. Neither judgment had been satisfied when these proceedings were commenced. Each judgment had been registered as a judgment mortgage against the Company's property registered on Folio 1785F, Co. Longford.

6. These proceedings were commenced by an originating notice of motion dated 26th November, 2003.

The respondents' response

7. The respondents' response is contained in three affidavits sworn by the first respondent on 27th February, 2004, 4th May, 2004 and 14th May, 2004. In essence, the first respondent, on behalf of both respondents, admitted the failure to comply with the provisions of the Companies Acts in relation to filing annual returns and the failure to comply with the order of the court to file the outstanding tax returns. The first respondent advanced what I think can fairly be described as two pleas in mitigation.

8. First, he averred that throughout the late 1980s and into the 1990s the Company was involved in substantial contracts at premises owned by a semi-State company and two Government Departments as a subcontractor and encountered difficulties securing payment from the main contractor. It was averred that sums aggregating in excess of €200,000 are due and owing, but it was not disclosed what, if any, steps the Company took to recover these sums. It was further averred that a policy decision was taken by the respondents not to act as a subcontractor wherever possible but to deal directly with the employer. This strategy had paid off and it was averred that by the end of 2003 the Company was in "quite a healthy financial position".

9. The second plea was that the second respondent suffered a depressive illness partly due to the difficulties in securing payment of monies due to the Company and partly due to a dispute with her former employer which had been ongoing since 1990. It was averred that the first respondent suffered from stress and anxiety as a result of the illness of the second respondent, who is his wife.

10. Following the commencement of these proceedings the following steps were taken by the respondents:

(1) The outstanding annual returns and accounts were filed in the CRO on 22nd April, 2004 and it was certified that the Company had met the annual return filing requirements of the CRO.

(2) The outstanding tax returns were filed with the Revenue Commissioners. The Revenue Commissioners issued nil assessments on foot of the Corporation Tax returns submitted.

(3) With effect from 27th February, 2004 the second respondent resigned as a director of the Company and Vincent Fox, an accountant by profession, was appointed a director in her place. On 22nd April, 2004 these changes were notified to the CRO on the relevant form (Form B10).

11. The Company's indebtedness to the Revenue Commissioners on foot of the High Court judgment had not been discharged and, in fact, further indebtedness had accrued. The evidence is that as of 31st December, 2003 in excess of €400,000 was due to the Revenue Commissioners in respect of outstanding taxes (PAYE / PRSI and VAT). After these proceedings were commenced, in separate proceedings in this court, the Revenue Commissioners had obtained an order declaring the money secured by the judgment mortgage registered in favour of the Revenue Commissioners on Folio 1785F well charged. Those proceedings had been stayed to enable the Company to raise the money to discharge the tax liabilities. Evidence was put before the court that a bank was positive to providing loan facilities for €400,000 to resolve the Company's tax liabilities, but it was made clear that approval would be subject to satisfactory repayment ability, security cover and compliance with the bank's normal lending terms and conditions. Evidence was also put before the court that the premises registered on Folio 1785F, which comprise a factory, office and showrooms on a one acre site in an Industrial Estate, have a market value of €850,000.

12. The Company continues to trade. The court was told that the Company has twelve employees.

Section 160

13. In two situations, which are not relevant for present purposes but illustrate the gravity of the type of wrongdoing which the Oireachtas considered merited automatic disqualification, by virtue of s. 160, as amended, a person is deemed to be subject to a disqualification order for a specified period. The two situations are where a person is convicted on indictment of any indictable offence in relation to a company or involving fraud or dishonesty (sub-s. (1)), and where there is not proper compliance with the requirements in the Companies Acts of disclosure of any disqualification orders made by a foreign state (sub-s. (1A)).

14. Sub-section (2) lists nine situations in which the court is given a discretion to make a disqualification order. Insofar as it is relevant for present purposes, sub-s. (2) provides as follows:

> "Where the court is satisfied in any proceedings or as a result of an application under this section that –
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> …
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> (d) the conduct of any person as promoter, officer, auditor, receiver, liquidator or examiner of a company, makes him unfit to be concerned in the management of a company; or
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> …
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> (f) a person has been persistently in default in relation to the relevant requirements; or
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> …
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> the court may, of its own motion, or as a result of the application, make a disqualification order against such person for such period as it sees fit."

15. The expression "disqualification order" is defined in s. 159 as meaning –

> "an order under this Part that the person against whom the order is made shall not be appointed or act as an auditor, director or other officer, receiver, liquidator or examiner or be in any way, whether directly or indirectly, concerned to take part in the promotion, formation or management of any company or any society registered under the Industrial and Provident Societies Acts, 1893 to 1978 …"

16. In s. 159 "officer" in relation to a company is defined as including a director.

17. The court's discretion under sub-s. (2)(f) is amplified in sub-s. (3), which is in the following terms:

> "(a) For the purposes of sub-section (2)(f) the fact that a person has been persistently in default in relation to the relevant requirements may (without prejudice to its proof in any other manner) be conclusively proved by showing that in the five years ending with the date of the application he has been adjudged guilty (whether or not on the same occasion) of three or more defaults in relation to those requirements.
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> (b) A person shall be treated as being adjudged guilty of a default in relation to a relevant requirement for the purposes of this sub-section if he is convicted of any offence consisting of a contravention of a relevant requirement or a default order is made against him."

18. The expression "relevant requirement" is defined in s. 159 as meaning

> "any provision of the Companies Acts (including a provision repealed by this Act) which requires or required any return, account or other document to be filed with, delivered or sent to, or notice of any matter to be given to, the registrar of companies".

19. The expression "default order" is defined in s. 159 as meaning –

> "an order made against any person under section 371 of the Principal Act [the Companies Act 1963] by virtue of any contravention of or failure to comply with any relevant requirement (whether on his own part or on the part of any company)."

20. It is not in issue that both respondents were officers of the Company when these proceedings were commenced and that the first respondent remains an officer of the Company. It is common case that the Director has standing to bring these proceedings by virtue

of sub-s. (6A) of s. 160. It is not in issue that the Director gave the respondents notice of his intention to make an application under sub-s. (2), as required by sub-s. (7).

21. Sub-section (9A) provides as follows:

> "In considering the penalty to be imposed under this section, the court may as an alternative, where it adjudges that disqualification is not justified, make a declaration under s. 150."

22. A declaration under s. 150 is a declaration that –

> "a person … shall not, for a period of five years, be appointed or act in any way, whether directly or indirectly, as a director or secretary or be concerned or take part in the promotion or formation of any company unless it meets the requirements set out in sub-section (3) …"

23. Sub-section (3) sets out the requirements in relation to the capitalisation of, and allotment of shares in, the company. Apart from the discretion conferred on the court by sub-s. (9A), s. 150 does not come into play in these proceedings because, in its normal application, s. 150 only applies where the company is being wound up and is insolvent.

Application of section 160 (2)(f).
24. For s. 160 (2)(f) to apply, the Director must satisfy the court that the respondents have been persistently in default in relation to compliance with provisions of the Companies Acts, in relation to making returns to the CRO. Paragraph (f) does not extend to a company's failure to comply with statutory requirements to make returns to other bodies, for example, to the Revenue Commissioners.

25. The Director cannot avail of the evidential provisions contained in sub-s. (3) because there is no evidence that the respondents were prosecuted, let alone convicted, of an offence under s. 125 of the Act of 1963, as amended, for failure to make annual returns, nor is there any evidence that s. 371 of the Act of 1963, as amended, was invoked, let alone successfully invoked, against the Company or the respondents.

26. Therefore, the question which falls to be considered is whether the Director has proved in any other manner that the respondents have been persistently in default in relation to making annual returns.

27. In summary, the facts are that when these proceedings commenced, there had been default for thirteen consecutive years by the Company in making its annual return to the CRO as required by s. 125. On the evidence, the only action taken by the CRO was to strike off the Company leading to its dissolution after nine years of default. When a third party brought an application to have the Company restored to the register, the court, presumably on the application of the Registrar of Companies, made an order directing the respondents to file the outstanding returns the respondents default continued and they failed to comply with the order of the court.

28. The ordinary meaning of the verb "persist" in its primary sense is "to continue firmly or obstinately in a state, opinion, purpose, or course of action *esp*. against opposition" (Shorter Oxford English Dictionary, 3rd ed.).

29. What might be called the "three strikes" philosophy which underlies sub-s. (3) suggests that, on the proper construction of paragraph (f), persistent default is not merely default which has continued over a long period of time but is default which has continued in the teeth of intervention on the part of the courts more than once. Although the default by the Company in relation to its obligations under s. 125 over such a long period and the failure of the respondents to comply with the order of 14th May, 2001 is to be deprecated, I am not satisfied that it has been established on the evidence that the respondents have been "persistently in default" in relation to their obligations under s. 125 in the sense in which that expression is used in para. (f).

Section 160(2)(d): the authorities
30. Despite the fact that established conduct making a person unfit to be concerned in the management of a company as provided for in para. (d) has been a ground for the making of a disqualification order under s. 160(2) since the enactment of the Act of 1990, for almost 15 years, there are very few authorities on the nature of the conduct which renders a person unfit. The authorities which are available were all decided in the context of the winding up of insolvent companies.

31. In *Business Communications Limited v. Baxter and Parsons* (Unreported, High Court, 21st July, 1995,), which was an application pursuant to s. 150, Murphy J. considered that assistance may be obtained in interpreting the relevant provisions of the Act of 1990 by comparing the circumstances in which restrictions may be imposed under s. 150 and the circumstances in which directors can be disqualified under s. 160. He pointed to the mandatory nature of the jurisdiction conferred by s. 150 by contrast to the discretionary nature of the jurisdiction conferred by s. 160(2). He contrasted the specific period of restriction provided for in s. 150, five years, with the discretion given to the court in s. 160(2) in relation to the period of disqualification it might impose, such period of disqualification as it sees fit. He also stated that in relation to a disqualification order, it is clear that there is a substantial burden to be discharged before the court has jurisdiction to make the appropriate order and he referred to para. (d) of s. 160(2) as typifying the grounds for disqualification. He pointed to the fact that when a disqualification order is made it is comprehensive in its effect and it precludes the person disqualified from acting during the period of disqualification irrespective of how the company he may wish to participate in is capitalised. He concluded:

> "Clearly, it is the comprehensive nature of a disqualification order which is seen as constituting an appropriately severe sentence for conduct which is manifestly more blameworthy than merely failing to exercise an appropriate degree of responsibility in relation to an insolvent company in liquidation of which the person was a director".

32. Murphy J., as a judge of the Supreme Court, was concerned with the application of s. 160(2)(d) in *Cahill v. Grimes* [2002] 1 I.R. 372 in the context of an application by the official liquidator of C.B. Readymix Limited to have the respondent disqualified under s. 160 (2)(b) and (d) in somewhat unusual circumstances. C.B. Readymix Limited, while it was struck off the register for failing to file annual returns, had purported to pass a winding up resolution which appointed the respondent as liquidator. The respondent took control of the books and records of the company. Subsequently the company was restored to the register and the Revenue Commissioners obtained judgment against the company. The company was then wound up by the court on the petition of the Revenue Commissioners and the applicant was appointed official liquidator for the purposes of the winding up by this court, which declared that the earlier resolution of the company appointing the respondent as liquidator was invalid. On the hearing to disqualify the respondent, the respondent argued that since he had not been validly appointed he had no obligations as liquidator and had "dumped" the books and records in his possession. This court (Smyth J.) disqualified the respondent from acting as liquidator, receiver or examiner of a company for a period of seven years and restricted him to acting as director only in companies with boards of directors of three or more persons. On the appeal to the Supreme Court, Murphy J., with whom the other judges of the Supreme Court concurred, in

dealing with a submission made by the respondent that s. 160 is draconian, and, accordingly, that there is a heavy onus on the applicant to establish that the matter falls within the section and that there should be a corresponding reluctance on the court to exercise its undoubted discretion against making a disqualification order, stated as follows (at p. 381):

> "In principle this argument is correct. The onus does fall on the applicant to establish the allegations on which he relies and, even where a case is made out, the use of the word 'may' in s. 160(2) confers a discretion on the court whether or not to make the order as was pointed out in *Re Newcastle Timber Ltd.* [2001] 4 I.R. 586.
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> The appropriateness of the sanction imposed by the trial judge must be considered in the light of the conduct of the respondent and the purpose for which the section was enacted.
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> In In *re Lo-line Ltd.* [1988] Ch. 477, Browne-Wilkinson V.C. provided a general approach to the application of the United Kingdom disqualification provisions in the following terms at pp. 485 to 486:-
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> > 'What is the proper approach to deciding whether someone is unfit to be a director? The approach adopted in all cases to which I have been referred is broadly the same. The primary purpose of the section is not to punish the individual but to protect the public against the future conduct of companies by persons whose past records as directors of insolvent companies have shown them to be a danger to creditors and others. Therefore, the power is not fundamentally penal. But, if the power to disqualify is exercised, disqualification does involve a substantial interference with the freedom of the individual. It follows that the rights of the individual must be fully protected. Ordinary commercial misjudgement is in itself not sufficient to justify disqualification. In the normal case, the conduct complained of must display a lack of commercial probity, although I have no doubt that in an extreme case of gross negligence or total incompetence disqualification could be appropriate.'
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> That passage was quoted with approval by the trial judge and likewise was adopted by Shanley J. in *La Moselle Clothing Ltd. v. Soualhi* [1998] 2 I.L.R.M. 345, by McGuinness J. in *Re Squash (Ireland) Ltd*. [2001] 3 I.R. 35 and in the judgment of McCracken J. in *Re Newcastle Timber Ltd.* [2001] 4 I.R. 586.
>
> It is I believe a correct statement of the law and represents a proper approach to the application and interpretation of s. 160 …"

33. Later in his judgement, Murphy J., having counterpointed the importance of appropriate documentation being available to liquidators and the gravity of the misconduct of the respondent, dealt with an argument advanced by the respondent -that a liquidator or director should not be severely penalised for one error in relation to a particular company in a context where no allegations of inappropriate conduct are made against him in respect of many such other offices held by him. While noting the "considerable force" of the argument, Murphy J. stated that it was the fact that the respondent could not, during the hearing at first instance in the High Court, or on the hearing of the appeal, appreciate the gravity of his misconduct that justified the conclusion that he was unfit to hold the office of liquidator and cast serious doubt upon his suitability to participate in the management of any company. The Supreme Court affirmed the order of the High Court, holding that it is open to the court under s. 160 (2) to impose conditions on a person the subject of an application for a disqualification order and, in the event of non-compliance with the conditions, it must be anticipated that a comprehensive order will then be made.

34. The applicant in *Re Newcastle Timber Ltd.* (In Liquidation) was the official liquidator of two companies which had the same directors who were the respondents on the application. The official liquidator was seeking an order under s. 160 or, in the alternative, both companies being insolvent, an order under s. 150. On the facts, McCracken J. found that, in relation to the application under s. 160, the official liquidator had discharged the onus on him in relation to three of the five grounds advanced by him: the failure to lodge annual returns in the CRO; that the company traded while insolvent for four years; and that after the company ceased to trade, the respondent discharged trade creditors in priority to the Revenue Commissioners. Having quoted, in part, the passage from the judgment in *Re Lo-line Motors Ltd.*, which was quoted by Murphy J. in *Cahill v. Grimes* which he considered was the proper approach to be taken both under s. 150 and s. 160, McCracken J. went on to deal with the application under s. 160 as follows (at p. 592):

> "As I have already said, many faults can be found in the conduct of the respondents in the present case. I have no doubt that they acted incompetently, and, particularly in relation to insolvent trading and preference of trade creditors, I think they behaved irresponsibly. However, the applicant has not satisfied me that the respondents were so much in breach of their duties that they are unfit to be concerned of the management of a company, particularly in view of the undoubted discretion which I have in this regard. The applicant did rely to a considerable degree on the fact that the Revenue Commissioners' debts remained unpaid, and cited a number of authorities as to the importance of this aspect of the case, but taking the overall behaviour of the respondents into account I do not think that it could be said that a disqualification order is necessary to protect the public against their future conduct. I say this particularly as it is now some six years since Newcastle ceased trading, during which time the first respondent has been intimately concerned in the management of another company, which appears to be trading successfully and is complying with its obligations to the Revenue. Accordingly, I will refuse an order under s. 160."

35. However, McCracken J. went on to find that the respondents had been sufficiently irresponsible to warrant a restriction order being made under s. 150: to have kept the company trading insolvently for some four years and allowing revenue debts to build up appeared to him to be totally irresponsible. Accordingly, he made an order under s. 150 against both directors, recognising that once the respondents had failed to satisfy him that they had acted responsibly, he was bound to make such an order.

Application of the law to the facts

36. Over a protracted period the respondents as directors of the Company blatantly disregarded their statutory duty to make annual returns. I think it is not unreasonable to conclude that to some extent this was facilitated by a failure on the part of the CRO to take action to ensure compliance with s. 125 until the late 1990s. Further, the respondents, as directors of the Company, defaulted on their statutory obligations to make returns to the Revenue Commissioners under the tax code. They even ignored an order of this court ordering them to remedy the defaults. However, the most reprehensible conduct on the part of the respondents, as directors of the Company, was the failure to discharge the Company's tax liabilities to the Revenue Commissioners. This failure must be roundly condemned given that, presumably, it involved a failure to remit to the Revenue Commissioners Value Added Tax paid by third parties to the Company and a failure to remit PAYE and PRSI deducted from the Company's employees' pay packets. Not only did they fail to discharge their tax liabilities but they suffered judgment for the sums due to the Revenue Commissioners and they even put at risk the industrial premises from which the Company carries on its business by permitting a "well charging" order to be made against those

premises in a mortgage suit, with the prospect of a court sale if the liability to the Revenue Commissioners is not discharged.

37. In my view, the explanations proffered by the respondents in an attempt to mitigate the consequences of their conduct do not excuse their failure to comply with the law and protect the assets of the Company and the interests of the generality of its creditors and its employees.

38. I have no doubt that the respondents acted irresponsibly. In the context of the application of s. 160, the question which arises is whether they have displayed a lack of commercial probity or, as it is sometimes put, whether they have fallen below the standards of commercial morality. In my view, the conduct of the respondents has come very close to that threshold, but has not quite reached it. The saving grace is that the first respondent eventually, albeit when faced with an application by the Director for a disqualification order, remedied the breaches of the Companies Acts and the taxation code in relation to making returns. Both parties combined in restructuring the corporate governance of the Company, which, hopefully, will prevent a repetition of the defaults which occurred in the past. The first respondent, on behalf of the Company, has evinced an intention to discharge the Company's indebtedness to the Revenue Commissioners. While, given that the "sword of Damocles" in the form of the mortgage suit hangs over the Company, little credit accrues to the respondents on this account, it is in the interests of the employees of, and third parties dealing with, the Company that the eventuality of a forced sale of the Company's premises be avoided. On the evidence, that can be achieved.

39. In the circumstances, I consider it appropriate not to make a disqualification order against either respondent. I am satisfied it is not necessary to do so to protect the public.

40. The court has a discretion under sub-s. (9A) to make a declaration under s. 150. Having regard to the finding that the respondents have acted irresponsibly, if the court was dealing with a separate application under s. 150 in the context of the Company being wound up as an insolvent company, on the basis of that finding, the making of a restriction order under s. 150 in the case of each respondent would be mandatory. However, I am satisfied on the evidence that the Company is solvent, that it is capable of discharging its indebtedness to the Revenue Commissioners, and that it is operating satisfactorily as a going concern. To make a restriction order against the first respondent would undoubtedly impact on the ability of the Company to give effect to its intention to discharge its liabilities to the Revenue Commissioners and to carry on as a going concern. Because of the pending mortgage suit, if it is to continue as a going concern, it must discharge its tax liabilities. In the circumstances I think it appropriate not to make a restriction order against the first respondent.

41. The second respondent has already resigned as a director of the Company. In view of the evidence as to the health of the second respondent, which is supported by a medical certificate from her general practitioner, I think it appropriate not to make a restriction order against the second respondent.

Order
42. There will be an order dismissing the Director's application.