Neutral Citation Number: [2011] IEHC 455

THE HIGH COURT

2011 645 COS

IN THE MATTER OF LAKE COMMUNICATIONS LIMITED

AND

IN THE MATTER OF THE COMPANIES ACTS 1963 – 2009

Judgment of Miss Justice Laffoy delivered on 24th day of November, 2011.

1. The problem and its source

1.1 The petitioner on this application, Lake Communications Limited (the Petitioner) is a company which was incorporated in the State on 14th September, 1977. At all material times the Petitioner comprised a sole member, Inter-Tel Lake Limited (the Sole Member), which is also incorporated in the State. The Petitioner and the Sole Member are part of an international group known as the Mitel Group. Apart from the Petitioner and the Sole Member, three other companies in the Mitel Group are registered in the State, namely, Lake Datacomms Limited (Datacomms), Fernway Limited (Fernway) and Lake Electronics Technologies Limited (Electronics). In July 2009, as part of a re-organisation of the Mitel Group, the Sole Member entered into three Share-For-Share Swap Agreements dated 23rd July, 2009 (the Exchange Agreements) with the Petitioner, whereby it was agreed that the Sole Member would transfer to the Petitioner shares held by it in Datacomms, Fernway and Electronics in consideration of the allotment of shares in the Petitioner to the Sole Member.

1.2 Immediately prior to 23rd July, 2009 the authorised share capital of the Petitioner was €7,990,500 divided into –

(a) 6,125,000 ordinary shares of €1.30 each; and

(b) 400,000 11% redeemable preference shares of €0.07 each.

The problem addressed in this judgment concerns the ordinary shares. Immediately prior to 23rd July, 2009, on the evidence, 6,117,276 ordinary shares of €1.30 each had been issued and the Sole Member was the owner of those shares.

1.3 In order to discharge the consideration moving from it under the Exchange Agreements, the Petitioner was required to issue to the Sole Member 291,469 ordinary shares in the capital of the Petitioner, made up as follows:

(a) 130,995 ordinary shares as consideration for the shares in Datacomms which the Sole Member agreed to transfer to the Petitioner;

(b) 138,172 ordinary shares as consideration for the shares in Fernway which the Sole Member agreed to transfer to the Petitioner; and

(c) 22,302 ordinary shares as consideration for the shares in Electronics which the Sole Member agreed to transfer to the Petitioner.

As the authorised share capital of the Petitioner was, as I have recorded, 6,125,000 ordinary shares, of which 6,117,276 had already been issued, the shares which the Petitioner had agreed to allot to the Sole Member under the Exchange Agreements exceeded the number of authorised ordinary shares remaining to be allotted (7,724 shares) by 283,745 shares.

1.4 The steps taken by the parties to implement the Exchange Agreements were the following:

(a) the Exchange Agreements were executed by the Petitioner and the Sole Member on 23rd July, 2009;

(b) on 23rd July, 2009 stock transfer forms were executed by the Sole Member in favour of the Petitioner in respect of the shares in Datacomms, Fernway and Electronics to be transferred to the Petitioner in accordance with the Exchange Agreements;

(c) at a board meeting on 23rd July, 2009 the board of the Petitioner approved the transaction embodied in the Exchange Agreements with effect from 17th July, 2009 and resolved that 291,469 ordinary shares of €1 (rather than €1.30, there obviously being a typographical error) each be allotted and issued to the Sole Member with effect from 17th July, 2009 and that the consequential formalities be complied with; and

(d) a share certificate was executed naming the Sole Member as the registered holder of 291,469 fully paid ordinary shares of €1.30 each in the Petitioner

1.5 The steps which were not taken, but should have been taken, in order to give effect to the intentions of the Petitioner and the Sole Member were the following:

(a) the authorised share capital of the Petitioner was not increased by the creation of a further 283,745 ordinary shares to enable a valid allotment and issue of the entirety of the shares to be allotted by the Petitioner to the Sole Member under the Exchange Agreements (291,469 ordinary shares) to be effected;

(b) no formal resolution was adopted by the Petitioner in general meeting authorising the allotment and issue of 291,469 ordinary shares to the Sole Member pursuant to s. 20 of the Companies (Amendment) Act 1983 (the Act of 1983), although it is clear on the evidence that the Sole Member was agreeable that the allotment should be made, having regard to the terms of the Exchange Agreements to which it was a party; and

(c) the Register of Members of the Petitioner was not updated to reflect the purported allotment to the Sole Member.

1.6 The form B5 (return of allotments), which was signed by a director of the Petitioner on 23rd July, 2009, was not received by the

Companies Registration Office (CRO) until 6th August, 2010. By letter dated 25th January, 2011 from the CRO to the Petitioner's solicitors it was pointed out that the authorised share capital of the Petitioner would have to be increased before the allotment the subject of the B5 could occur. At that time, nothing was done to address the problem which the CRO had highlighted. The problem came to the fore again during the summer of 2011 in connection with the auditing of the Petitioner's accounts for the year ended 30th April, 2011. It had not been adverted to when the Petitioner's accounts for the year ended 30th April, 2010 were being audited, because the Register of Members had not been updated.

1.7 Neither the officers of the Petitioner nor the Petitioner's solicitors have been able to unearth any resolution of the Petitioner passed in July 2009 authorising the increase of its share capital to facilitate a valid allotment to the Sole Member in pursuance of the Exchange Agreements.

2. The proposed solution

2.1 The substantive relief sought on the petition presented by the Petitioner on 9th November, 2011, and on its notice of motion issued on the same day, is as follows:

> (a) a declaration pursuant to s. 89 of the Companies Act 1963 (the Act of 1963), as amended, that the creation of additional authorised share capital of €368,868.50 by the Petitioner comprising 283,745 ordinary shares of €1.30 each in or around 23rd July, 2009 necessitated and/or occasioned by the proposed allotment and the issue to the Sole Member of 291,469 ordinary shares of €1.30 each by the board of the Petitioner at a meeting held on 23rd July, 2009 pursuant to the Exchange Agreements was and is valid for all purposes; and
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> (b) a declaration pursuant to s. 89 of the Act of 1963, as amended, that the allotment and issue to the Sole Member of 291,469 ordinary shares of €1.30 each by the board of the Petitioner at a meeting held on 23rd July, 2009 (pursuant to the Exchange Agreements) was and is valid for all purposes.

2.2 The Petitioner has also sought, to the extent that it is considered necessary, directions as to the steps to be taken in relation to the hearing of the petition. I will return to that matter later. Certain ancillary orders are also sought. I will return to those matters later.

3. The law

3.1 Section 89 of the Act of 1963 (as substituted by s. 227 of the Companies Act 1990), which deals with validation of invalid issue, redemption or purchase of shares, insofar as is relevant for present purposes, provides as follows:

> "If a company has created or issued shares in its capital, . . . , and if there is reason to apprehend that such shares were invalidly created, issued . . . , as aforesaid, the court may, on the application of the company, . . . declare that such creation, issue . . . shall be valid for all purposes if the court is satisfied that it would be just and equitable to do so and thereupon such shares shall from the creation, issue . . . thereof, . . . be deemed to have been validly created, issued . ."

The apprehended invalidity in this case arises from the fact that the Petitioner purported to issue shares over and above its entitlement to do so having regard to its authorised share capital and to allot them without complying with s. 20 of the Act of 1983. Section 68 of the Act of 1963 provides that a company limited by shares, if so authorised by its articles of association, may in general meeting alter the conditions of its memorandum to provide, *inter alia*, for the increase in its share capital by new shares of such amount as it thinks expedient. It is expressly provided in the Petitioner's memorandum of association, at clause 4, that the Petitioner has power from time to time to increase or reduce its share capital and to issue any shares in the increased capital.

3.2 The only Irish authority to which the Court was referred on the application of s.89 was the decision of the High Court (Keane J.) in *Re Sugar Distributors Ltd.* [1995] 2 I.R. 194. In that case, the application by Sugar Distributors Ltd. to validate the issue of shares by it and their allocation to a subsidiary, so as to create the necessary subsidiary relationship which would enable it to obtain the benefit of the manufacturing tax rate, in circumstances where meetings had not taken place and resolutions had never been passed, although minutes purported to record such meetings and resolutions, which was objected to on behalf of the Revenue Commissioners, was refused. As the headnote in the report succinctly records, Keane J. held that the discretion conferred by s. 89 must be exercised in a judicial manner, in accordance with appropriate criteria, and, in particular, with regard to the underlying policy of the section. He held that the underlying policy of the section is the avoidance of hardship to persons who had innocently subscribed for shares which were invalid due to a defect in their title, provided the shares could be validated by the Court in a manner which was not unjust or inequitable having regard to the interests of third parties who might be affected. He held that Sugar Distributors Ltd. and its associated company were seeking to gain a tax advantage and that was not a purpose for which the procedure under s. 89 was intended to be used.

3.3 A number of Australian authorities had been cited in *Re Sugar Distributors Ltd*. and counsel on behalf of the Petitioner cited further Australian authorities in support of the Petitioner's application pursuant to s. 89. It was submitted that an Australian authority, *Re Farnell Electronic Components Pty Ltd.* (1997) 25 ACSR 345, is very similar on the facts to this case. That was a decision of the Supreme Court of New South Wales, Equity Division. The problem addressed by the court arose because, in 1990, the plaintiff, after a meeting of directors held by telephone, purported to issue 3,500,000 redeemable preference shares for $1 each. At the time, the plaintiff's authorised capital was $100,000. Resolutions were passed in 1997 altering the memorandum and articles of association, increasing the authorised capital of the plaintiff and providing that the redeemable preference shares could be redeemed at par at the request of the holder. The plaintiff then sought an order validating the allotment of redeemable shares pursuant to s. 122 of the Companies (NSW) Code, which the court noted was virtually identical with s. 194 of the Corporations Law. In dealing with the application to validate, Young J. stated:

> "As I have already mentioned, the Court of Appeal in Moran's case suggested that one does need to find something justifying validation where there has been simply a disregard of basic procedures. . . .
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> I consider that the true rule is that a court does have a wide discretion under s. 194 of the Corporations Law or its predecessor in the Code. If there is an ex parte case where all interested parties join in and no one is prejudiced, then the court may very well make an order for validation notwithstanding that there has been some extremely casual work done at the time of the allotment. However, if there is a contested case and the parties do not all agree that a validation is proper, then it is necessary for the person seeking the validation to point to some factor which justifies it over and above the fact that there was a careless allotment."

On the facts of the case, Young J. held that, as no party had been detrimentally affected by the allotment of the redeemable preference shares, it was appropriate to make the order validating the allotment.

3.4 In a decision of the Supreme Court of New South Wales, Court of Appeal, which was considered, and referred to in the passage quoted in the next preceding paragraph, by Young J. – *Moran v. Moranco Enterprises Pty Ltd.* (1996) 22 ACSR 65 – the text of s. 194 of the Corporations Law is set out as providing:

> "Where a company has purported to issue or allot shares and:
>
> > (a) the creation, issue or allotment of those shares is invalid by reason of any provision of this or any other Act or of the memorandum or articles of the company or for any other reason; or
> >
> > (b) . . . .
>
> the Court may on application by the company . . . on being satisfied that in all the circumstances it is just and equitable so to do, make an order:
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> > (c) validating the purported issue or allotment of those shares; or
> >
> > (d) confirming the terms of the purported issue or allotment of the shares;
>
> or both."

That case was a contested case where the shares in the Petitioner had originally been issued to several members of the same family, but subsequently a resolution was passed at a meeting, of which not all of the shareholders were given notice, purporting to issue additional shares to one member of the family. The Court of Appeal upheld the decision at first instance that it was not just and equitable to validate an issue of shares when not all of the shareholders had a chance to participate in the decision to issue the shares.

3.5 Counsel for the Petitioner also referred the Court to a more recent decision of the Federal Court of Australia in *Re Onslow Salt Pty Ltd*. (2003) 45 ACSR 322. The statutory provision which was invoked in that case did not incorporate the requirement that it be just and equitable to make the validating order. However, in delivering judgment, French J. referred to an earlier Australian decision, which was cited with approval by Keane J. in Re Sugar Distributors Ltd. – *Millheim v. Barewa Oil and Mining NL* [1971] W.A.R. 65. French J. quoted the following passage from the judgment of Burt J. in that case, which was also quoted by Keane J. (at p. 207):

> "[The section] is designed to enable the court to make good what is really a defective title to shares in a company – using the words 'defective title' in the quite non-technical sense.
>
> It is directed to cases where the shares have been issued, which represent a bundle of rights proprietary in character and valuable in terms of money, and where it appears for some reason or other there has been an irregularity in the issue or the allotment which in strict law would result in the issue of the shares being, as the section says, 'invalid'."

In acceding to the application before him, French J. stated:

> "The question remains whether or not the order sought should be made. Both shareholders support it. The application is non-contentious. There is no basis for inferring any prejudice to any person arising out of the validation. Nor is there any ground for inferring that the failure to comply with the statutory requirement was anything other than an oversight at the time it occurred. I note that the affidavit material did not explain the oversight. In the ordinary course such an explanation should be proffered. In this case however, there is no reason to suspect that the shares were issued other than with a careless failure to have regard to the requirements of the law. The terms of the resolution itself indicate a slap-dash approach to its form and content. But I do not think that the non-compliance reflects a reckless or blatant disregard of the law which attracts the public policy considerations referred to earlier. Nor is there any indication on the materials before me of any purpose, served by the application, which could be characterised as unworthy or contrary to public policy."

3.6 By way of general observation, I have found the approach adopted by the Australian courts to be persuasive.

4. Application of the law to the facts

4.1 The first question which arises on the application of s. 89 is whether there is reason to apprehend that the creation and allotment of 283,745 ordinary shares in the Petitioner to the Sole Member was invalid. Having regard to the fact that the evidence indicates that no formal steps were taken by the Petitioner to increase its authorised share capital before making the purported allotment to the Sole Member, one must conclude that the purported creation and allotment were invalid.

4.2 The next question is whether the Petitioner is an appropriate applicant for an order under s. 89. As the company the shares of which were purported to be created and allotted, it clearly is.

4.3 The final question which the Court has to determine is whether it would be just and equitable to validate the creation, and the allotment to the Sole Member, of 283,745 ordinary shares in the Petitioner and to make the declarations necessary to achieve that end. Before determining that issue, it is necessary to outline certain additional steps which have been taken in relation to the transaction between the Petitioner and the Sole Member.

4.4 First, there have been exhibited in the grounding affidavit copies of three statutory declarations made by Caoimhin O'Laoi, a director of the Petitioner, which established that the Petitioner and the Sole Member were associated companies at the time of the execution of the Exchange Agreements and the share transfers in relation to the shares in the associated companies effected by the Sole Member to the Petitioner on foot thereof. The purpose of the statutory declarations was to demonstrate to the Revenue Commissioners the relevant facts which were necessary to enable the transferee of the shares, the Petitioner, to obtain relief from stamp duty pursuant to s. 79 of the Stamp Duties Consolidation Act 1999 in relation to the transfer of the shares to the Petitioner. The significance of that action on the part of the Petitioner is that disclosure was made to the Revenue Commissioners in relation to the transaction. Apart from that, there is absolutely nothing in the evidence before the Court to suggest that the motivation of the Petitioner and the Sole Member in entering into the Exchange Agreements was other than to effect a restructuring of companies in the Mitel Group. In particular, there is nothing to suggest that their objective was to gain some tax advantage, of the type found by

Keane J. in *Re Sugar Distributors Ltd*. not to be within the intendment of s. 89.

4.5 Secondly, in anticipation of the bringing of the application which is under consideration, it is averred in the grounding affidavit that the Sole Member adopted the following resolutions:

> (a) an ordinary resolution that it was the clear intention of the Petitioner and the Sole Member to increase the authorised share capital of the Petitioner on and from 23rd July, 2009 in the manner necessary to give effect to the Exchange Agreements;
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> (b) an ordinary resolution that it was the clear intention at all material times of the Petitioner and the Sole Member, for the purposes of s. 20 of the Act of 1983 or otherwise, to allot 291,469 ordinary shares of €1.30 each to the Sole Member and that such intention was in fact evidenced by the entry of the Petitioner and the Sole Member into the Exchange Agreements;
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> (c) an ordinary resolution that the Petitioner was unconditionally authorised to bring the petition before the Court pursuant to s. 89 to validate the allotment and issue of 291,469 ordinary shares of €1.30 each and the creation of the authorised share capital to permit such allotment and issue;
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> (d) a special resolution that, contingent upon obtaining an order from this Court under s. 89, the Petitioner amended and was thereby authorised to amend its memorandum of association to reflect the validation of the creation of 283,745 ordinary shares of €1.30 each arising from the allotment and issue of 291,469 ordinary shares of €1.30 each, thereby substituting a new clause 4 in the memorandum of association stating the share capital of the Petitioner as set out in the minute referred to at para. 5.1 below; and
>
> (e) a special resolution that, contingent upon the obtaining of the order under s. 89, the Petitioner amended and was authorised to amend its articles of association in a similar manner.

It was averred that the purpose of the said resolutions was to record, *inter alia*, the consent to the allotment and issue of the shares in the Petitioner to which the Sole Member was entitled under the Exchange Agreements at all material stages and for all relevant purposes. In other words, the purpose of the resolutions was to signify the consent of the Sole Member to what was purported to be done on 23rd July, 2009 and to what is necessary to validate the fulfilment by the Petitioner of its obligations under the Exchange Agreements. However, the date of the passing of the resolutions is not stated in the grounding affidavit, which was sworn by a partner in the firm of solicitors acting for the Petitioner, nor are minutes of the resolutions exhibited. I consider that a supplemental affidavit sworn by a director or the secretary of the Sole Member should be filed proving the date of passing of the resolutions and exhibiting minutes thereof.

4.6 Returning to the question whether it would be just and equitable to validate the creation of the necessary shares and their allotment to the Sole Member pursuant to s. 89, I am satisfied that it would. This application is non-contentious and could not be otherwise. The only parties affected are the Petitioner and the Sole Member. No third party could be prejudiced by the validating of the increase in the authorised share capital of the Petitioner and the allotment to the Sole Member. There is no shareholder other than the Sole Member. No creditor could be prejudiced. I am satisfied that the objective of the transactions embodied in the Exchange Agreements was to effect a restructuring within the Mitel Group, not to gain a tax advantage. Having regard to the evidence, and, in particular, the evidence furnished to the Revenue Commissioners with a view to obtaining relief from stamp duty on the share transfers to the Petitioner, I consider it reasonable to infer that the validation of the transaction would not involve any prejudice to the Revenue Commissioners. There are no public policy considerations which would militate against validating the increase in the authorised share capital of the Petitioner or the allotment to the Sole Member. On the contrary, public policy would seem to dictate that the Sole Member, which is a limited company, should be put in the position of validly obtaining what it bargained for under the Exchange Agreements, lest its members or creditors be prejudiced by its defective title to 283,745 ordinary shares in the Petitioner. I accept that the failure to take the formal steps to increase the share capital of the Petitioner in accordance with law and to effect a valid allotment to the Sole Member pursuant to the Exchange Agreements was due to an oversight in July 2009 in the implementation of complex transactions. I think the probability is that the oversight is attributable to the solicitor who was dealing with the matter at the time, who has since ceased to be employed by the Petitioner's solicitors. As submitted by counsel for the Petitioner, validation of the allotment could not be regarded as a charter for careless implementation of regulatory and contractual formalities in relation to company transactions.

4.7 Because I have formed the view that there is no prejudice to any third party in acceding to the Petitioner's application and that to do so has no adverse public policy implications, I have come to the conclusion that it is not necessary to give notice to any party of the petition.

4.8 The one aspect of this matter with which I have had a slight difficulty is the manner in which the declaration sought, which I have set out at (a) in paragraph 2.1 above, is formulated. The difficulty is that I am satisfied on the evidence that the Petitioner did not formally in accordance with law create the additional authorised share capital necessary to make the allotment to the Sole Member in fulfilment of its obligations under the Exchange Agreements. Moreover, it would appear that it has not increased its share capital in accordance with its constitutional documents prior to this petition. It is true that it was implicit in the resolution passed by the board of the Petitioner on 23rd July, 2009 that the share capital of the Petitioner should be increased because it was required to be increased in order to facilitate the allotment purported to be effected by that resolution. Therefore, I have come to the conclusion that the difficulty can be overcome by validating under s. 89 "the creation by implication" of the necessary additional authorised share capital.

5. Form of order

5.1 Subject to the affidavit referred to at para. 4.5 above being filed, the Court will make an order which contains the following elements:

> (a) the declarations sought by the Petitioner pursuant to s. 89 subject to the amendment that the declaration in relation to the validation of the creation of additional authorised share capital shall refer to "the creation by implication" of additional authorised share capital;
>
> (b) an order directing the Petitioner to deliver for registration to the Registrar of Companies within 21 days of the perfection of the order, and directing the Registrar to register, a copy of the order of the Court and a copy of the minute of share capital of the Petitioner in the following terms:

"The authorised share capital of the Company is €8,359,368.50 divided into 6,408,745 ordinary shares of €1.30 each and 400,000 11% Redeemable Preference Shares of €0.07 each.

The issued share capital of the company is 6,408,745 ordinary shares of €1.30 each and 6 11% Redeemable Preference Shares of €0.07 each";

and

(c) an order directing that notice of the registration of the order and of the said minute be published once in Iris Oifigiúil within 21 days of registration.