Neutral Citation: [2015] IEHC 28

THE HIGH COURT

[2012 No. 599 COS]

IN THE MATTER OF APPLEYARD MOTORS LIMITED (IN VOLUNTARY LIQUIDATION), AND IN THE MATTER OF SECTION 297A OF THE COMPANIES ACT 1963, AS AMENDED

BETWEEN

TOOMEY LEASING GROUP LIMITED

APPLICANT

AND

GRAHAM SEDGWICK, COLIN FARRELL, PAUL GREENE AND CHRISTOPHER PRATT

RESPONDENTS

JUDGMENT of Mr. Justice Binchy delivered on the 21st day of January, 2015

1. In this application, the applicant, a creditor of Appleyard Motors Limited (the "Company") seeks a declaration pursuant to s. 297A of the Companies Act 1963, that the first and second named respondents only (the third and fourth named respondents having been released from the proceedings) should be held personally liable to the applicant in the sum of €48,250.00, being the loss sustained by the applicant arising out of its dealings with the Company in the weeks leading up to the liquidation of the Company.

Facts

2. The factual background giving rise to the applicant's claim is not in dispute. Prior to its liquidation, the Company operated a Ford dealership from its premises which it leased from its parent company BFR Limited ("BFR") at 15 Maple Avenue, Stillorgan Industrial Park, Blackrock, Co. Dublin. On 17th May, 2012, a Mr. Chris Proudman, Account Manager with the applicant, sent an email to Mr. Allen Rodgers of the Company expressing an interest in purchasing three white Ford Fiesta five door cars from the Company. The applicant, never having dealt with the Company previously, carried out a credit search in advance of its dealing with the Company, which search did not indicate anything of concern regarding the affairs or financial standing of the company. Mr. Rodgers responded by email of 22nd May confirming that the Company was in a position to supply the vehicles at a price of €15,995.00 each. Subsequently, by email of 6th June 2012, the Company notified the applicant that it would have to charge an additional €260 in relation to one vehicle owing to the fact that it had to be supplied with bluetooth technology, thereby bringing the total payable to €48,250.

3. On 1st June, Mr. Proudman responded to the email of 23rd May confirming that the applicant wished to proceed with the purchase of the vehicles on the terms stipulated. By email of 6th June, Mr. Rodgers responded, giving details of the bank account of the Company and stating that "we will advise registration numbers approximately one hour after receipt of funds". Later, on 6th June, Mr. Proudman inquired if he could be given registration numbers in advance because "lack of registration numbers until receipt of funds is going to give me a problem…".

4. Mr. Rodgers replied, again on 6th June, to the effect that as soon as the vehicles are registered it "initiates full payment for the vehicles from our account. So we would need to be in receipt of funds prior to registering the vehicles. I can, however, guarantee that you will have the registration numbers within one hour of receipt of funds".

5. The following day, Mr. Rodgers sent an email to Mr. Proudman inquiring as to "how things are progressing with the payment? As you know we have the three Fiestas booked and are mindful that they have to be delivered shortly". On 12th June, Ms. Anne Beardmore of the applicant, requested bank details of the Company in order to arrange a transfer of funds. These details were furnished on the same day and on 13th June the applicant transferred funds to the Company in the sum of €48,250.00 for the vehicles. The Company had sourced the vehicles through another Ford Dealership, Ashley Motors. In compliance with an arrangement that the Company had with its principal bankers, Ulster Bank since 2010, the Company sought permission from the bank to make payment of the amount due to Ashley Motors' purchasing subsidiary, Kitale Ltd. in respect of the vehicles. This request was made by Mr Christopher Friel, Financial Controller of the Company to Mr Ciaran O'Grady of Ulster Bank. Mr O'Grady instructed the bank not to make the payment immediately and said he would first need to check with Mr Michael Fenlon of the bank, and that he would get back to the Company the following day. He did not do so however, and for the reason given below the Company became aware later that day (14th June) that it had lost the support of its bankers and consequently the Company could not pay for the vehicles, as the Company did not have the funds to do so. As a result, the Company did not take delivery of the vehicles from Ashley Motors and they were never delivered to the applicant by the Company which ceased trading on 15th June, 2012, and on 26th June, 2012, the Company was placed into creditors' voluntary liquidation. The event that made it clear to the Company that it had lost the support of Ulster Bank was the refusal on 14th June of Ulster Bank to make a payment on behalf of the Company by way of standing order in the sum of €1,000 to Gowan Motors as part of a repayment arrangement of a debt owing by the Company to Gowan Motors. The second named respondent, Mr Farrell (who was cross examined on the affidavits sworn by him in defence of this application), gave evidence that the respondents knew that the stopping of that payment indicated the withdrawal of support by the bank for the Company and for that reason the respondents immediately took steps to cease trading and to put the Company into liquidation. Before that however, recognising that the Company would not now be in a position to supply the vehicles to the applicant, Mr Friel, had sent an email to the bank requesting reversal of the payment of the sums received from the applicant, but the bank declined this request.

6. It is the applicant's case that at least by 12th June, 2012 (when the last request for payment was sent by the Company) and, failing that, by 13th June, 2012, when the monies were transferred, the respondents knew or ought reasonably to have known of the risk to the applicant's funds, given what the applicant describes as the Company's precarious financial position at the time and (the applicant asserts) that the respondents were, while officers of the Company, knowingly a party to the carrying on of the business of the Company in a reckless manner. The respondents vigorously contest this assertion.

Financial History of Applicant

7. The Company was incorporated in 1985 and until 2009 carried on the business of motor repairs. The Company was a subsidiary of

BFR as was its sister company, Appleyard Car Sales Limited. The latter operated a Peugeot franchise.

8. Following the collapse of the motor industry nationwide from 2008 onwards, the Company secured a Ford franchise. According to the respondents it was decided that the Company should take this franchise and, in addition to its business of motor repairs, commence the business of selling vehicles rather than continuing to have separate entities, one involved in motor repairs and the other involved in car sales. At around this time Appleyard Car Sales Limited ceased trading, with liabilities of €887,000.00.

9. The Company traded from a premises owned by BFR which remained valued in the Company's books at €12.5m, but the true value of which was assessed by Ulster Bank at €2m. The respondents agree that the value of the premises was significantly overstated. BFR was indebted to Ulster Bank, arising from its purchase of the premises, in the sum of more than €9m. The Company (or perhaps more accurately, the Appleyard Group) had an overdraft limit with Ulster Bank of €700,000, but according to Mr. Farrell the actual amount overdrawn typically "*hovered around €800-€850,000, with it extending to €890,000 on occasion*." Again according to Mr. Farrell, the Company at no time received any specific complaint from the bank about the Company trading in excess of its overdraft facility.

10. Mr. Farrell described the relationship of the Company with Ulster Bank as intimate and, in order to ensure transparency as regards the trading position of the Company, the Company had been furnishing the bank, from 2010 onwards, with weekly statements of the anticipated receipts and payments of the Company for each prospective week. The respondents had given personal guarantees to Ulster Bank in the sum of €1,500,000 each in relation to the liabilities of the companies within the group to Ulster Bank.

11. The Company also had banking facilities with AIB Bank. The respondents had also given guarantees in relation to the liabilities of the Company to AIB Bank in the amounts of €50,000 and €130,000 each. The Company also had the benefit of a new car stocking facility operated through Lombard Ireland ("Lombard"). The Company had a separate used car stocking facility provided by Bank of Scotland Ireland. The new car stocking facility was effectively a credit facility to the Company up to the amount of €1m, which enabled the Company to purchase its stock in trade and was, therefore, essential for the financial wellbeing and day to day trade of the Company. Lombard Ireland formed part of the same group of companies as Ulster Bank.

12. In February, 2011 there were discussions between the Company and FCE Bank (Ford Credit Europe, hereinafter referred to as "FCE") with a view to FCE replacing Lombard in the provision of stocking facilities to the Company. While FCE was willing to consider an application from the Company for such facilities, it first required detailed proposals from the Company in relation to the treatment of the group's debt, other creditors of the Company and security to be provided by Ulster Bank to FCE in relation to any facilities that might be offered by FCE. Pending such proposals, FCE was not willing to provide a stocking facility to the Company.

13. From March, 2011 onwards the Company began to fall into arrears with its VAT liabilities. It received a final demand for arrears of VAT in the sum of €108,961.09 dated 10th June, 2011, in relation to which it entered into an instalment arrangement with the Revenue Commissioners (for a reduced sum of €94,810.00) in July 2011, but the Company continued to fall into arrears of ongoing VAT liabilities (notwithstanding adhering to the instalment arrangement) and received further final demands from Revenue in October, 2011 (€62,682.00 in respect of September 2011), in January, 2012 (€13,014.00 in respect of November/December 2011 VAT), and March, 2012 (€186,423.00 in respect of January/February 2012).

14. In or around August, 2011 Lombard made a decision to exit the Irish market and accordingly, requested repayment of its new car stocking facility of €1m from the Company. Relations between the Company and Lombard were good and Lombard was prepared to allow the Company the opportunity to repay the amount due on the facility from sales of new cars over a period of time. While Lombard was, in fact, repaid the bulk of monies owing to it between December, 2011 and 15th June, 2012, when the Company ceased trading, the withdrawal of this facility presented the Company with a very significant problem which it had to address as a matter of urgency if it was to continue in business, i.e. it needed some other party to provide a replacement new car stocking facility. Additionally, the withdrawal of the facility exacerbated the VAT problems of the Company because this facility enabled the Company to purchase vehicles thereby creating VAT inputs which could be used to offset liabilities created by VAT outputs resulting from the sale of vehicles, i.e. the liability to VAT was likely to increase owing to the fact that the Company was now entering a period during which it would be selling far more vehicles than it was purchasing.

15. Discussions with FCE resumed with a view to replacing Lombard and on 7th September, 2011, JPA Brenson Lawlor Limited, advisers to the Company, presented a proposal to FCE in relation to the provision of a stocking facility to the Company. These proposals were rejected by FCE in late October, 2011. While there is no written record of the reasons for this rejection, it is understood that FCE's requirements were not any different to those identified in February 2011. Following upon that rejection, the respondents engaged in negotiations, on behalf of the Company, to secure the supply of vehicles via Ashley Motors Limited, another Ford dealer. This source of supply was secured when Ulster Bank agreed to support the arrangement by providing a guarantee on behalf of the Company in the sum of €300,000.00 to Kitale Limited, Ashley Motors Car Purchasing subsidiary. This enabled the Company to continue to stock and supply new Ford vehicles for the duration of the facility which commenced on 6th January, 2012, and was to last until 30th April, 2012. On 26th April, 2012, Ulster Bank confirmed its willingness to extend this facility for the remainder of 2012 or, in the words of Mr. Michael Fenlon of Ulster Bank "until such time as issues on car stocking are clarified/resolved".

16. This facility might have enabled the Company to pay Kitale/Ashley Motors for the vehicles and deliver them to the applicant, knowing that if the Bank did not permit a further increase in the Company's overdraft it would still be obliged to honour the payment because of its guarantee. Of course this would have meant that Ulster Bank was at the loss of the funds and not the applicant, but the Bank would have been aware of such a risk when giving the guarantee. No adequate explanation was given to the Court as to why this was not done. In his evidence, Mr. Farrell at one point said he did not know why and at another point stated that the facility was for the purchase of display vehicles only. The guarantee itself was not produced to the Court and Mr. Farrell said he never saw it, and presumed it was given directly by the Bank to Kitale, and this seems likely. In any case, the facility was not used in the acquisition of the vehicles ordered by the applicant and moreover, Mr. Farrell also stated in evidence that it was not necessary at any time for Kitale to rely on this facility, which of course meant that in June 2012 the Company could have made payment for the vehicles secure in the knowledge that such payments would be honoured by Ulster Bank.

17. In his evidence, Mr. Farrell stated that 2011 had been the best year for new car sales since the collapse of the market in 2008. The Company was optimistic that this trend would continue during 2012, but Mr. Farrell acknowledged that sales in 2012 were not as good as anticipated. It appears from information submitted by the applicant (which was not contested by the respondent) that combined sales of new and used cars during January 2012 came to 91 sold units and the profit for the period in the Company was €50,891.00. The equivalent figure for February was 49 cars sold, with a profit for that month of €12,764.00. However, by March sales had dropped away significantly and this trend continued for the remaining months of the Company's existence with trading losses recorded in March, April and May in the respective sums of €16,314.00, €13,532.00 and €16,023.00. All of this is against the background that the early part of the year is accepted as being the best time of year for new car sales (at least it was until the

introduction in 2013 of a bi-annual system of registration of new vehicles.)

18. Mr. Farrell stressed that the Company was particularly strong in its servicing and parts section and that that business at all times remained profitable. It had secured the contracts for the servicing of Garda, CAB and HSE vehicles.

19. On 18th January, 2012, the Company's financial advisers, JPA Brenson Lawlor Limited, sent to the respondents a group wide summary of the results for each company in the group, together with draft financial statements and draft abridged financial statements for each Company for the year ended 31/10/2011. While it was noted that the "Company is profitable at an operating level" serious concerns were raised about its ability to continue as a going concern. These concerns related to the significant amount owing by BFR to Ulster Bank and concluded with a warning that if the BFR loans were to fall into default, the bank might take control of the properties secured via a receivership and in turn this could trigger a knock on process leading to the closure of the Company. They also advised that the absence of a new car stocking facility was a significant concern but that owing to the arrangement entered into with Ashley Motors, the Company was able to continue trading. The auditors also advised that the book value of the premises from which the Company operated should be written down to €2,000,000. Had this been done it would have had the effect of showing a deficit on the group wide balance sheet of €7,733,000 instead of a surplus of €2,767,000 in the accounts of the group. No adequate explanation was given as to why the value of the property was never written down to market values.

20. In February 2012, the Company received a warning from AIB that it was exceeding its overdraft facility with that bank. In March and again in May, 2012 AIB returned a number of cheques to the Company unpaid; one in the sum of €951.67, another in the sum of €11,500.00, and a third in the sum of €510.00. It also declined to pay a direct debit in the sum of €74.98. Further cheques were returned by that bank in June, prior to the winding up of the Company in the sum of €770.42 and €355.63.

21. Another factor unhelpful to the financial wellbeing of the Company was that during March, 2012, Henry Ford & Son reduced its car parts credit facility available to the Company from €150,000.00 to €100,000.00. While this was part of a nationwide reduction in facilities by Ford, it represented another financial blow to the Company.

22. While there are no indications that Ulster Bank ever gave any warnings to the Company or the respondents of the impending withdrawal of its facilities, on 14th June 2012 Mr. Michael Fenlon of Ulster Bank sent an email to the respondents in the following terms:-

> *"I refer to the above account and the s/o payment this morning of €1,000 to Gowans. Please be advised that owing to:*
>
> *- The precarious financial condition of the company;*
>
> *- The sizable excess on the current accounts;*
>
> *- The fact that we have yet to know (i) if FCE are willing to provide stocking, and (ii) if a third party investment will be forthcoming*
>
> *The Bank is not prepared to facilitate this payment until such time as these matters are resolved. We cannot permit further bank monies to flow to such external parties given the circumstances.*
>
> *This s/o will therefore be returned this morning.*
>
> *Yours faithfully."*

23. According to the Directors' estimated statement of affairs as of 26th June 2012, estimated liabilities to preferential creditors of the Company were €535,923 and liabilities to unsecured creditors came to a total of €749,590.69. The second named respondent was the single largest unsecured creditor in the Company, it appearing from the estimated statement of affairs that he was owed €196,117 at that date. Of course, the sums associated with the premises from which the Company traded were not owed by the Company itself but by BFR.

Conduct of Respondents

24. During 2011/2012, the Company experienced a number of significant challenges. The first of these was that it received the final demand for VAT in the sum of €108,961.09 from the Revenue Commissioners, as referred to in paragraph 13 above. The Company responded promptly to the demand and entered into an arrangement with the Revenue Commissioners for payment of the amount due by instalments and subsequently adhered to that arrangement by making monthly payments to the Revenue Commissioners in an agreed amount per month over the following of six months.

25. When, in August 2011, Lombard demanded repayment of its new car stocking facility, the respondents entered into an arrangement with Lombard whereby the amount due to it could be repaid in an orderly manner from the sale of its stock of new cars. The respondents appraised Ulster Bank of the situation and it agreed to continue providing support to the Company on certain conditions. These conditions included the Company securing the support of FCE in providing a new stocking facility, agreement upon the restructuring of the debt owing by BFE and the introduction of new capital to the Company by way of a third party investor.

26. The respondents engaged the services of a Mr. Denis O'Riordan, a banking consultant who had previously worked with Ulster Bank and in September 2011 also engaged the auditors of the Company, Messrs. JPA Brenson Lawlor Limited, with a view to having a business plan prepared for the Company. Negotiations again re-opened with FCE on behalf of the Company with a view to the provision of a stocking facility. A recommendation for acceptance of the proposal was made by an internal credit analyst within FCE, but ultimately the proposal was rejected in October, 2011.

27. This rejection was not final, however, and left it open to the Company to come back with a fresh proposal addressing the concerns of FCE which included the provision of an Ulster Bank guarantee and the introduction of new investment capital. In order to deal with the immediate needs of the Company, however, in January 2012 the Company secured the arrangement referred to above with Ashley Motors and Kitale Limited, with the support of an Ulster Bank guarantee in the sum of €300,000.00.

28. The respondents also sought to secure outside investment in the Company and in this regard had discussions with Mr. Henry Flanagan of Ashley Motors who, according to Mr. Farrell, indicated that he was confident that he might be able to introduce new funds to the Company through a private investor, a Mr. Alan Jones. Mr. Jones had apparently provided seed capital for Ashley Motors. According to Mr. Farrell, during the months of February, March and April, 2012 Mr. Flanagan carried out a due diligence of the Company on behalf of Mr. Jones and worked with Mr. Denis O'Riordan towards securing agreement on terms of investment. While I

believe Mr. Farrell's assertions in this regard, he was relying entirely on the assurances of Mr. Flanagan and there is no documentation available at all to demonstrate any significant intent on the part of Mr. Jones to invest in the Company. That said, as late as 1st June, 2012, Mr. Flanagan wrote to Mr. Farrell attaching what he described as an adjusted balance sheet reflecting steps that he considered necessary "before an investor could be secured," but this falls far short of an expression of interest let alone a commitment by an investor.

29. Mr. Farrell also said in evidence that at the time the Bank withdrew support he was expecting a meeting to take place between FCE, Kitale and the bank, to progress the measures necessary for the survival of the Company but his evidence in this regard was, to put it mildly, vague, and I do not believe that the Court should regard such expectations as being any more than mere hopes.

30. It will be apparent from the above that the respondents were not ignoring the difficulties of the Company and throughout the second half of 2011 and the first half of 2012, took steps to ensure the continuity and support of Ulster Bank, to replace the Lombard stocking facility with one provided by FCE and to secure an investor for the Company. Additionally, it should be noted that the second named respondent, who would otherwise have been due to be paid a salary of €10,000 per month, received only €10,000 in the five months leading up to the liquidation of the Company.

31. The respondents did not take any further financial advice other than that referred to above and in particular did not take advice from an insolvency practitioner until they knew the Company had to be wound up. With the benefit of hindsight, Mr. Farrell agreed that by accepting the applicant's money before the vehicles were registered in the name of the applicant, the Company was taking risks with the applicant's money.

32. It was suggested both on affidavit on behalf of the applicant and Mr. Farrell in evidence, that the Company should have considered placing the applicant's funds into a separate customer account which would have been secure from any actions taken by the Bank or other creditors. Mr. Farrell stated that in all his years in the motor industry he had never heard of such a proposal. Furthermore, he asked Brian Cooke, Deputy Director General of the Society of the Irish Motor Industry (SIMI) if he had ever heard of a motor dealership operating such an account and he informed Mr. Farrell that he had no knowledge or recollection of such an issue being raised at SIMI previously or of SIMI advising its members to hold separate client bank accounts. Accordingly, it never occurred to the respondents to do so.

The Applicable Law

33. Section 297A of the Companies Act 1963, provides:-

> "(1) If in the course of winding up of a company or in the course of proceedings under the Companies (Amendment) Act 1990, it appears that –
>
> (a) any person was, while an officer of the company, knowingly a party to the carrying on of any business of the company in a reckless manner, or
>
> (b) [not applicable in this case]
>
> the court, on the application of the receiver, examiner, liquidator or any creditor or contributory of the company may, if it thinks it proper to do so, declare that such person shall be personally responsible, without any limitation of liability, for all or any part of the debts or other liabilities of the company as the court may direct.
>
> (2) Without prejudice to the generality of subs. (1)(a), an officer of the company shall be deemed to have been knowingly a party to the carrying on of any business of the company in a reckless manner if -
>
> (a) he was a party to the carrying on of such business and, having regard to the general knowledge, skill and experience that may reasonably be expected of a person in his position, he ought to have known that his actions or those of the company would cause loss to the creditors of the company or any of them.
>
> (b) he was a party to the contracting of a debt by the company and did not honestly believe on reasonable grounds that the company would be able to pay the debt when it fell due for payment as well as all its other debts (taking into account the contingent and prospective liabilities).
>
> (3) Notwithstanding anything contained in subs (1), the court may grant a declaration on the grounds set out in paragraph (a) of that subsection only if –
>
> (a) paragraph (a), (b) or (c) of section 214 applies to the company concerned, and
>
> (b) an applicant for such a declaration, being a creditor or a contributory of the company, or any person on whose behalf such application is made, suffered loss or damage as a consequence of any behaviour mentioned in subs. (1).
>
> (6) Where it appears to the court that any person in respect of whom a declaration has been sought under subs. (1)(a) has acted honestly and responsibly in relation to the conduct of the affairs of the company or any matter or matters on the grounds of which such declaration is sought to be made, the court may, having regard to all of the circumstances of the case, relieve him either wholly or in part from personal liability on such terms as it may think fit."

34. It is agreed by the parties in these proceedings that the Company was at the material time one to which s. 214 of the Act applied.

35. There is comparatively little jurisprudence in Ireland on the subject of reckless trading and the leading case in the area remains that of *Re Hefferon Kearns Limited (No.2)* [1993] 3 I.R. 191. That case concerned the application of the provisions of s. 33 of the Companies (Amendment) Act 1990, which was framed in materially identical terms to s. 297A of the 1963 Act. In that case, Lynch J. in the High Court referred to the objective test of recklessness set out by the Supreme Court in the case of *Donovan v. Landys Limited* [1963] I.R. 441. In the latter case, Kingsmill Moore J. cited, with approval, the following passage from the judgment of Megaw J. in the English High Court in the case of *Shawinigan v. Vokins & Co. Ltd* [1961] 1 W.L.R. 1206 where he stated:-

> "In my view, "reckless" means grossly careless. Recklessness is gross carelessness – the doing of something which in fact involves a risk whether the doer realises it or not; and the risk being such, having regard to all the circumstances, that the taking of that risk would be described in ordinary parlance as "reckless". The likelihood or otherwise that damage will follow is one element to be considered, not whether the doer of the act actually realised the likelihood. The extent of the damage which is likely to follow is another element, not to the extent which the doer of the act, in his wisdom or folly, happens to foresee. If the risk is slight and the damage which will follow if things go wrong is small, it may not be reckless, however unjustified the doing of that act may be. If the risk is great, and the probable damage great, recklessness may readily be a fair description, however much the doer may regard the action as justified and reasonable. Each case has to be viewed on its particular facts and not by reference to any formula. The only test, in my view, is an objective one. Would a reasonable man, knowing all the facts and circumstances which the doer of the act knew or ought to have known, describe the act as "reckless" in the ordinary meaning of that word in ordinary speech? As I have said, my understanding of the ordinary meaning of that word is a high degree of carelessness."

36. Lynch J. observed that the inclusion of the word "knowingly" would require the director to "know very well" that his conduct would have involved a serious and obvious risk of loss or damage to others which he ignored. He stated:-

> "The inclusion of the word "knowingly" in s. 33, subs 1(a) must have been intended by the Oireachtas to have some effect on the nature of the reckless conduct required to come within the subsection. I think that its inclusion requires that the director is party to carrying on of the business in a manner which the director knows very well involves an obvious and serious risk of loss and damage to others, and yet ignores that risk because he does not really care whether such other suffers loss or damage or because his selfish desire to keep his own company alive overrides any concern which he ought to have for others."

37. Lynch J. went on to consider whether in that case the directors should be deemed reckless by provisions equivalent to s. 297(2)(b) because of their decision to keep trading when they were fully aware that all of the debts of the company could not be paid. He observed:-

> "Paragraph (b) of subsection (2) appears to be a very wide ranging and indeed draconian measure, and could apply in the case of virtually every company which becomes insolvent and has to cease trading for that reason. If, for example, a company became insolvent because of the domino effect of insolvency of a large debtor, it would be reasonable for the directors to continue trading for a time thereafter, to assess the situation and almost invariably they would incur some debts which would fall within paragraph (b) before finally closing down. It would not be in the interests of the community that whenever there might appear to be any significant danger that a company was going to become insolvent, the directors should immediately cease trading and close down the business. Many businesses which might well have survived by continuing to trade, coupled with remedial measures, could be lost to the community."

38. In the circumstances of that case, Lynch J. found that the directors could be deemed reckless and then went on to consider whether or not the directors might be exonerated from personal responsibility through the defence provided by s. 297A(6). He stated:-

> "I think that it is because subsection (2) and especially paragraph (b) is so wide ranging, that subsection (6) was included in section 33 of the Act. The UK Insolvency Act, 1986, at s. 214, subs (3) is not quite as widely drafted as subs (6) of s. 33 of the Act of 1990, and accordingly, in *Re: Produce Marketing Consortium (No.2)* [1989] BCLC 513, it was held that while the court could take account of the absence of any fraudulent intent so as to lessen the amount ordered to be paid by the directors, unless the evidence showed that the directors had taken every step to minimise loss to creditors that they ought to have taken, an order should be made against them. It seems to me that the expression "acted honestly and responsibly in relation to the conduct of the affairs of the company" is wider than the corresponding provisions in subs (3) of s. 214 of the UK Act, and the court in this jurisdiction is given specific power to relieve such a director from any personal liability whatsoever."

39. In the particular circumstances of that case, Lynch J. went on to relieve the directors of personal liability on the grounds provided for in subs 33(6) of the 1990 Act (the equivalent of s. 297A(6)).

40. The sentiments expressed by Lynch J. were endorsed by Peart J. in *Re USIT World Plc* [2005] IEHC 285. He stated:-

> "With the benefit of hindsight it is natural perhaps that a liquidator can look at the situation at a particular time and form a perfectly proper view that a situation should have been looked at differently or that a different decision ought to have been made. But that is not the point in my view when this Court must decide whether it is satisfied whether directors acted honestly and responsibly. It does not mean that decisions taken must turn out later to have been the right decisions. What is at issue is whether it was irresponsible to have taken the decision at the time. That irresponsibility implies some element of recklessness or culpable want of care on the part of a director, which in the present case is absent."

41. Peart J. in that case considered whether the decision of the directors to continue trading while insolvent was or was not an irresponsible act and stated:-

> "I think that it is important to note that it is not incumbent on a board of directors, at the first moment at which it is becoming apparent that debts may not be capable of being paid as they fall due, to immediately call in the liquidator and cease trading. Many companies will experience for many reasons unrelated to the general health of the company a downturn in profitability over a quarter, two quarters or even three quarters. That in my view does not mean that even where a risk of insolvency downstream is warned or anticipated, some reasonable effort at rescuing the situation may not be permitted to be undertaken. To attempt to trade out of a difficulty is not an irresponsible act. Care of course must be taken to ensure that effective and realistic steps are taken and that creditors' interests are kept to the fore, rather than that a careless or reckless gamble is taken without proper advice and planning to an achievable end. Some sort of short term emergency fire-fighting must be permitted to take place without those efforts, provided they are reasonable and responsible, from being made. Many companies have survived and prospered after temporary setbacks."

42. As to what is meant by the term "acted honestly and responsibly" (as referred to in s 297A(6) this was considered by Murphy J. in the case of *Business Communications Ltd v. Baxter & Anor* (Unreported, High Court, 21st July, 1995) in the context of an application to restrict directors under the provisions of s. 150 of the Companies Act 1990. Murphy J. stated as follows:-

> "To obtain exemption from the restraint which must otherwise be imposed by virtue of s. 150…all that is required is the exercise of a suitable degree of responsibility. Ordinarily, responsibility will entail compliance with the principal features of the Companies Acts and the maintenance of the records required by those Acts. The records may be basic in form and modest in appearance. But they must exist in such a form to enable the directors to make responsible commercial decision and auditors (or liquidators) to understand and follow the transactions in which the company was engaged…However, it does seem to me that the most important feature of the legislation is that it effectively imposes a burden on the directors to establish that the insolvency occurred in circumstances in which no blame attaches to them as a result of either dishonesty or irresponsibility."

43. The meaning of "responsibility", again in the context of an application under s. 150 of the Companies Act 1990, was also considered, this time by the Supreme Court, in the case of *Re Squash (Ireland) Limited* [2001] 3 I.R. 35. In that case the directors, who operated a sporting and leisure business, continued to collect subscriptions from members of the company during November and December, 1997, at a time when the directors were becoming aware that the liquidation of the company was imminent. However, the directors were at the time labouring under the misunderstanding that the company owned a valuable interest in its premises in Clontarf, which, if realised, might avoid the liquidation of the company. On 1st December, 1997, however, they were notified for the first time that the company did not have an entitlement to a new lease of its premises under the Landlord and Tenant (Amendment) Act 1980. They promptly took advice from counsel which they received on 10th December, 1997, which confirmed that the company held no valuable interest in the premises. At this stage it was clear to the directors that the company had no future and they then proceeded to put the company in an orderly way into liquidation. The main question that arose in the case was whether the directors displayed a lack of commercial probity in collecting subscriptions during this critical and sensitive time for the company. McGuinness J. stated:-

> "It is probable that the appellants should have taken positive steps to stop these demands being sent out on the 1st December, when they received the notification from the Department of Education but it is, I think, understandable that they waited until they had their own counsel's opinion on the 10th December. Probably they were hoping against hope that it would turn out that the Department of Education's position was legally wrong. What they did was open to criticism but I do not feel that it was sufficient to be categorised as irresponsible."

44. It appears that the only reported case in Ireland to date in which directors or, more accurately, a director, has been held liable for the debts of a company on the grounds advanced in these proceedings, is that of *PSK Construction Limited (in voluntary liquidation)* [2009] IEHC 538. In that case the company both underdeclared and underpaid liabilities in respect of PAYE/PRSI and RCT. The total under declaration and underpayment in respect of the PAYE/PRSI for an eight month period was €1,075,851.00 and in respect of RCT, for a nine month period, was €583,172.00. Subsequently, the company purported to correct the position by filing overstated returns and sought an instalment plan from the Revenue Commissioners which was refused. At the date of commencement of the winding up of the company, the total liability to the Revenue Commissioners stood at €2,361,314.00.

45. One of the directors, who took responsibility for the false declarations and underpayments, argued that he felt that he was delaying payment only until such time as the company left a loss making job and would then be in a position to commence making payment of the arrears. It is also a feature of the case that the company appeared to be underresourced in that it did not employ a financial controller or accountant, and that basic accounting functions were performed by employees who did not appear to have had any qualifications and further, that no management accounts were ever prepared. The director concerned, when asked if he sought professional advice when he knew the company was in trouble, stated that his auditor "suggested I give up but I kept going. I didn't get any specific advice".

46. Finlay Geoghegan J., following a review of the principles set out in *Re Hefferon Kearns Limited*, concluded that by continuing to keep the company trading by under declaring and underpaying the Revenue Commissioners, the Director, Mr. Killeen must have known that this involved an obvious and serious risk of loss or damage to creditors of the company. While she accepted that Mr. Killeen intended that the under declarations and underpayments were to be a temporary measure, Finlay Geoghegan J. stated she was not satisfied that Mr. Killeen had any reasonable basis for his belief that that might only be a temporary measure. She found that he must have been aware that the decision he made involved a risk of loss or damage to others and decided to ignore that risk because of his desire to keep the company alive, and for that reason she concluded that Mr. Killeen be held personally liable for certain of the debts of the company.

47. From the foregoing authorities, therefore, it is clear that the standard of proof required of an applicant under s. 297A of the Companies Act 1963, is very high and the only reported case to date in which such liability has been imposed, that of *PSK Construction Limited*, is one in which the director concerned deliberately filed false declarations, and consequently made underpayments to the Revenue Commissioners. While it does not appear to me to be necessary for behaviour to go that far in order to constitute reckless trading within the meaning of the section, nonetheless it is clear from a review of the authorities that the courts are very reluctant to impose personal liability on directors under section 297A.

Submissions of Counsel

48. Counsel for the applicant submitted that the company was insolvent at least from the time that it was unable to pay its VAT liabilities as they fell due in March 2011. Counsel further submits that the Company entered even more dire trading circumstances following the withdrawal by Lombard of its stocking facility in August 2011; that the sales figures of the Company were deteriorating and that it failed to achieve targets in early 2012; that the Company's auditors had specifically flagged to the respondents the Company's vulnerability to a withdrawal in support by its bankers. Counsel also submitted that the respondents had been presented with a series of indicators which would have alerted any objective observer to the fact that it was losing the support of its bankers, including the stopping of payments on the bank accounts of the Company, the negative trajectory of the Company's overdraft, the awareness of Ulster Bank of the Appleyard Group's balance sheet insolvency and the ongoing failure of the Company to secure the support of Ford Credit.

49. Against that factual backdrop, the applicant submits that the respondents were either carrying on business in a manner which they knew well involved an obvious and serious risk of loss or damage to others, and yet ignored the risk or alternatively that, having regard to the general knowledge, skill and experience that may reasonably be expected of persons in the positions of the respondents, they ought to have known their actions or those of the Company would cause loss to the creditors of the Company.

50. Counsel on behalf of the respondents submitted that the rarity of claims for reckless trading reflects the high standard that an applicant is required to meet to obtain such a draconian order and the recognition by creditors and liquidators that the courts will not easily override the protections afforded by limited liability. Counsel submitted that the conduct of the respondents in this case is not sufficiently culpable and does not "*fall within the range*" to merit sanction under s. 297A of the principal Act.

51. Counsel further submitted that if the Court considers that the conduct of the respondents requires review and appropriate sanction, that is a matter for the liquidator to pursue by way of an application for restriction under the Companies Acts. Counsel submitted that notwithstanding the strident criticisms levelled at the respondents by the applicant, the liquidator has not made a similar application or been joined in this application. It was further submitted that there is a hierarchy of statutory penalties which may be imposed upon the directors of an insolvent company, and the courts have acknowledged that the behaviour that would attract a sanction under s. 297A far exceeds that which would merit restriction under s. 150 or indeed disqualification under s. 160 of the Companies Act, 1990. Counsel for the respondents submits that, if the court were, in this case, to make the "unusual" order of imposing personal liability on the respondents, this would essentially reformulate the sensible, sober, realistic approach set out in the seminal case of *Hefferon Kearns* and encourage an entirely new type of claim by aggrieved creditors pursuing the directors of failed companies.

Conclusions

52. Along with many other motor dealerships during the boom years of the Irish economy up to 2007/2008, the Appleyard Group acquired and developed a premises leaving it with a substantial indebtedness to its principal bankers, Ulster Bank, stood at approximately €9,000,000 as of 2011. On top of that, the motor industry in particular was affected by the collapse of the economy. This combination of high indebtedness to its bankers and a massive fall off in sales created very significant problems for the Appleyard Group, and these problems were of a kind that were being experienced across the country by motor dealers.

53. In 2009, the Company, which until then had only undertaken the business of servicing and provision of parts, began trading as a Ford dealership and it is clear to the Court that at the time, notwithstanding the financial difficulties, the Company and the group as a whole enjoyed the support of its principal bankers, Ulster Bank. The Company also had the benefit of a new car stocking facility up to €1,000,000 in value provided by Lombard Ireland, which was a finance house within the same group of companies as Ulster Bank.

54. While 2011 was, in terms of car sales, the best year for the Company since the downturn in the economy nonetheless during 2011 it began to experience additional and significant difficulties which ultimately lead to its liquidation. In March 2011, it started to fall into arrears with its VAT repayments necessitating an instalment arrangement with the Revenue Commissioners. In August 2011 Lombard informed the Company that it was withdrawing its stocking facility and even though it did not require immediate repayment of the amount owing (€1,000,000), the withdrawal of the facility created a number of difficulties for the Company.

55. Firstly, the Company needed a facility of this kind in order to be able to trade at all and this was fully appreciated by the directors. Without such a facility not only would the Company be unable to keep up its levels of stock, but it would, as a result, find itself in a position whereby it had significantly more VAT outputs than inputs, meaning that its VAT liability was increasing all the time. Initially the Company hoped that it might persuade FCE to provide the stocking facility, but FCE made it clear that it would only do so if it received a guarantee of the facility from Ulster Bank and also provided the Company met other requirements for FCE.

56. Having initially rejected an approach from the Company (long before Lombard terminated its stocking facility) in February 2011, FCE again declined to provide a stocking facility in October 2011. While the respondents maintain that the application with FCE remained ongoing and that they remained optimistic that the facility would ultimately be secured through FCE, there is a significant dearth of correspondence or documentation available to support the optimism of the respondents and their optimism in this regard was not reasonably well founded.

57. Throughout the relevant period, the Company (or more accurately, the group) was operating significantly in excess of its overdraft facility. While, according to Mr. Farrell, this had been ongoing for a number of years and did not present any immediate threat to the Company, it must nonetheless have been a matter of concern for both the bank and the Company and it left the Company vulnerable to the withdrawal of facilities by the bank at any time.

58. The respondents clearly recognised the difficulties that the Company was in and in my opinion they at all times acted honestly and for a significant period acted responsibly in the steps that they took to keep the Company viable. These included the taking of professional advice from JPA Brenson Lawlor Ltd, the engagement of Mr. Denis O'Riordan, the efforts made to replace Lombard with FCE and the efforts to secure new capital for the Company from a third party investor. In addition, the Company secured a facility for the supply of new vehicles through its arrangements with Ashley Motors, and the guarantee of that facility by Ulster Bank.

59. Without the Ashley Motors guarantee, there can be no doubt but that the Company would have been obliged to cease trading some time early in 2012. The provision of that facility however, in my opinion, entitled the directors to continue trading for the first quarter of 2012 at least in the hope that sales in the early part of the year would live up to projections. These are precisely the kind of measures I believe were envisaged by Mr. Justice Lynch in *Hefferon Kearns* and Mr. Justice Peart in *Re USIT World Plc*, when they refer to the desirability of affording companies a reasonable opportunity to trade out of difficulties.

60. Unfortunately, the Company failed to achieve its sales objectives for the first quarter of 2012 and while it made an operating profit for January and February 2012, it slipped into operating losses for each of the remaining months prior to its liquidation. It did receive a fillip however when Ulster Bank confirmed on 26th April 2012 that it would, as it had promised to do in January of that year, extend the guarantee facility for the acquisition of cars from Ashley Motors for the remainder of 2012. I believe that this entitled the directors to consider that there was no immediate threat of the withdrawal of Ulster Bank facilities at that point in time and that it was reasonable for the Company to continue to trade for a period thereafter, while at the same time addressing the matters that had for some time been identified as key to the survival of the Company.

61. However, the directors remained under an obligation to keep the overall position of the Company under review given the fundamental insolvency of the Company, and in the words of Mr. Justice Peart in *Re USIT World Plc*. "to keep creditors interests to the fore." The directors were aware that, for the survival of the Company, it was necessary to procure a stocking facility from FCE; to agree terms on reorganisation of its debt with Ulster Bank and to secure the introduction of new capital to the Company. On Mr. Farrell's own testimony and as is evident from the documentation produced to the court, these matters were all intertwined and failure to secure any one of these three key objectives inevitably would mean that it would not be possible to achieve any other of them as a result of which the Company was bound to fail sooner rather than later.

62. In this regard however, there was no evidence given to the court either by way of testimony from Mr. Farrell or through documentation produced to the court that would indicate that the Company was at the end of April 2012, any closer to achieving those objectives than it was at the end of October 2011 when FCE declined for the second time to provide a stocking facility. Nor was any evidence given as to what further steps the respondents were taking to secure these objectives from 26th April 2012 onwards. According to Mr. Farrell who swore the affidavits on behalf of both himself and the first named respondent, Mr. Sedgwick, Mr. Jones who was contemplating investment in the Company had conducted a due diligence into the Company in the months of February, March and April which undoubtedly was an adequate time to conduct such an exercise for a company of this size. While in

evidence, Mr. Farrell stated that he did not wish to press the would-be investor too hard, in my view, given the importance attached to this investment the directors were under a duty to bring this issue to a head one way or another, within a reasonable period from the conclusion of the due diligence, which coincided with the extension by Ulster Bank of the guarantee facility for the purchase of cars from Ashley Motors. However, I believe that the directors probably took too much assurance from the extension of this facility by Ulster Bank and as a result did not give adequate attention to the risks posed to creditors by the continued trading of the Company.

63. By the end of May, 2012, therefore the following would have been apparent to the Company, and the respondents:

1. No investor had been secured; and nor were the respondents close to reaching agreement with an investor;

2. No replacement had been found for Lombard to provide a stocking facility to the Company;

3. No agreement had been reached with Ulster Bank regarding the reorganisation of its debt;

4. the Company had fallen well short of its sales targets for 2012 and had just concluded a third successive month with an operating loss;

5. AIB cheques had been returned unpaid in March and May 2012;

6. The value of the Henry Ford car parts facility had been reduced from €150,000 to €100,000 in March 2012.

In short, the financial position of the Company was deteriorating, not improving, and with no reasonable prospect in sight for improvement.

64. The applicant was not an ordinary creditor of the Company, in the sense of being a trade creditor. The applicant was a customer of the Company, which became a creditor because it paid in advance for vehicles which it did not receive, rather than making payment against delivery. Against the troubled background in which the Company was trading, it had a duty to take special protective measures for customers such as the applicant.

65. One such measure that the Company could have taken would have been to ensure that it did not receive funds from the applicant until the Company itself had taken delivery of the vehicles. The Company was in a position to do this because it knew that upon making payment for the vehicles to Kitale/Ashley Motors, Ulster Bank would have to honour payment for the vehicles by reason of its guarantee. This would have been done with very limited risk to the Company because it would then only effect delivery to the applicant upon receipt of cleared funds. This was surely the principal purpose of the Ulster Bank guarantee i.e. to enable the Company to purchase stock and indeed this was identified by the Company's auditors in their report of 18th January 2012 to the Directors as being the key facility that enabled the Company to continue trading. Furthermore, it seems to me that there was no reason why the Company needed to seek the permission of the bank to make payment for the vehicles even after the bank refused to honour the payment to Gowan Motors on 13th June 2012, because the bank would in any case have been bound to honour the payment to Kitale/Ashley Motors by reason of its guarantee. If for whatever reason, not explained to the Court, it was not open to the Company to acquire the vehicles from Kitale/Ashley Motors, through reliance on the Ulster Bank guarantee, whether before of after 13th June 2012, the Directors were under a duty to take professional advice or alternative measures to protect creditors such as the applicant or if no such measures could be identified, to wind up the Company.

66. As stated above, the extension by Ulster Bank of the guarantee facility for the acquisition of cars from Ashley Motors on 26th April 2012 afforded the Directors some breathing space, however they remained under an obligation to keep the overall position of the Company under review and to keep the creditors' interests to the fore. In practical terms this meant that in the ensuing weeks and certainly no later 31st May 2012, the Company needed either to secure the measures necessary for its survival, or to obtain further professional advice to establish if the continued trading by the Company could be justified. While I believe that the directors acted honestly and responsibly up to 26th April 2012, I consider that their failure to take further professional advice regarding the future of the Company no later than 31st May 2012, and/or to take appropriate measures to protect creditors or alternatively to take steps to wind up the Company as of that date, was not responsible conduct in light of all of the information that they had in relation to the Company, including the previous advice they had received from their consultant, JPA Brenson Lawlor Ltd as far back as January 2012. The directors were at this point failing to keep the interests of creditors to the fore, which was clearly required of them given the precarious state of the Company and the group as a whole.

67. In my opinion, any objective analysis of the affairs of the Company as of 31st May 2012, and quite probably earlier, would have demonstrated that the Company had no future and steps should have been taken no later than that date to wind up the Company or alternatively steps should have been taken to protect creditors such as the applicant. While I do not believe that the evidence demonstrates that the respondents were knowingly parties to the carrying on of any business of the Company in a reckless manner, I am of the view that the respondents may be so deemed pursuant to the provisions of s.297A (2) of the Companies Act, 1963 in that having regard to all of the information available to them, and, having regard to the general knowledge, skill and experience that may reasonably be expected of persons in the position of the respondents, they ought to have known that their actions or those of the Company would cause loss to the creditors of the Company or any of them, after 31st May 2012.

68. Since I have already found that the failure of the Directors to take further professional advice and/or to take measures to protect creditors or to wind up the Company in the period between 26th April 2012 and 31st May 2012 was not responsible conduct, the respondents are not entitled to be relieved of liability on the grounds set out in section 297A(6) of the Companies Act, 1963 and accordingly I find that the applicants are entitled to a declaration in the terms of para. 1 (a) of the notice of motion herein and also to the declaration sought under para. 2 of the notice of motion to the effect that the respondents are personally liable to the applicant in the sum of €48,250.