THE COURT OF APPEAL

Neutral Citation Number: [2015] IECA 40

Appeal No. 296/2010

[Article 64 transfer]

Irvine J.
Hogan J.
Mahon J.

PAGNELL LIMITED (TRADING AS SNAP PRINTING)

PLAINTIFF/APPELLANT

AND

O.C.E. IRELAND LIMITED

DEFENDANT/RESPONDENT

JUDGMENT of Mr. Justice Gerard Hogan delivered on 3rd day of March 2015

1. Where a defendant asserts that it was entitled to terminate a fixed term service contract prior to the end of that term by reason of the existence of an implied term justifying such termination, is this sufficient to constitute a *prima facie* defence such that it would then be inappropriate to make an order providing for security for the defendant's costs in accordance with s. 390 of the Companies Act 1963 ("the 1963 Act")? That is in essence the principal issue which is presented on this appeal, although the more specific question of whether security should be ordered where the defendant has made a significant lodgement also arises for consideration. The issue arises in the following way.

2. The appellant, Pagnell Ltd. ("Pagnell") had originally appealed to the Supreme Court against the decision of the High Court (Hedigan J.) of 11th May 2010 directing the provision of security pursuant to s. 390 of the 1963 Act. This appeal was, however, transferred to this Court by direction of the Chief Justice (with the concurrence of the other members of the Supreme Court) pursuant to Article 64 of the Constitution following the establishment of this Court on 29th October 2014.

3. Pagnell was the corporate vehicle whereby a printing service company (which traded as Snap Printing) provided certain printing services to the defendants company, O.C.E. Ireland Ltd. ("OCE"). In November 2000 OCE obtained a contract from Allied Irish Banks plc ("AIB") whereby the former was to operate the latter's central facilities printing ("CFP") from AIB's headquarters in Ballsbridge, Dublin 4. A month later OCE entered into a sub-contract with Pagnell whereby the latter company would operate the CFP from Ballsbridge for a 5 year period. Under this arrangement Pagnell invoiced OCE for services carried out on a monthly period and OCE billed AIB in turn.

4. In August 2003 OCE terminated the contract with the result that Pagnell lost the effective benefit of the AIB work. In November 2004 Pagnell commenced these proceedings seeking damages for breach of contract as a result of what it contended was the premature and unlawful termination of the contract. A statement of claim was delivered on 15th December 2004.

5. It is common case that the parties made a serious endeavour to settle the case in May 2005. When those negotiations floundered OCE delivered a defence on 9th June 2005. OCE then amended its defence to make an open lodgement of €50,000.

6. In 2006 Pagnell's principal, Mr. McGovern, fell ill. On medical advice he decided to sell the Snap Printing franchise along with the principal assets of the company and goodwill. Most of the net proceeds were used to discharge Pagnell's bank borrowings. Counsel for Pagnell, Mr. Banim S.C., did not dispute but that Pagnell is effectively being kept alive for the purpose of completing this present litigation which remains outstanding.

7. In the wake of the sale of the underlying assets, OCE's solicitors first raised the question of security for costs in April 2008. Correspondence between the parties subsequently ensued. Finally, by notice of motion issued on the 18th November 2009 OCE sought an order for security under s. 390 of the 1963 Act.

8. It was not in dispute but that Pagnell would not be in a position to pay the costs of OCE were the latter to prove successful in its defence. The application was, however, opposed by Pagnell on the basis that OCE had not, in fact, established that it had a bona fide defence. Specifically, it contended that the fact that the latter had elected to make a substantial lodgement was inconsistent with the existence of such a *bona fide* defence.

The judgment of the High Court

9. In a judgment delivered on 11th May 2010, the High Court (Hedigan J.) made an order pursuant to s. 390 of the 1963 Act that Pagnell provide security for costs in these proceedings. So far as the *bona fide* nature of the defence issue is concerned, Hedigan J. stated:

> "…it is not possible at this stage of the proceedings to hold that the defendant has not a *bona fide* defence. He may be able to convince the [trial] court that there should be an implied term for any number of reasons. It is noteworthy that no application has been brought to strike out the defence as being 'not *bona fide'* defence. He may be able to establish there was a breach of contract in terms of quality of service. He may be able to show that no less ensued as a result of the termination. All of these matters need a full hearing. All could constitute a defence. In my judgment, the defendant has set up sufficient arguments to satisfy the court that the defence furnished is a bona fide one."

10. Hedigan J. also rejected the argument that the existence of a lodgement might constitute a special circumstance such as would justify the Court in not making an order under s. 390 of the 1963 Act. By order of 13th July 2010 Hedigan J. fixed the amount of security as €140,000.

Section 390 of the 1963 Act
11. Section 390 of the 1963 Act provides:

> "Where a limited company is plaintiff in any action or other legal proceeding, any judge having jurisdiction in the matter, may, if it appears by credible testimony that there is reason to believe that the company will be unable to pay the costs of the defendant if successful in his defence, require sufficient security to be given for those costs and may stay all proceedings until the security is given."

12. The principles governing the proper interpretation of s. 390 of the 1963 Act are by now well established. These principles were helpfully summarised by Clarke J. in *Connaughton Road Construction Ltd. v. Laing O'Rourke Ireland Ltd.* [2009] IEHC 7 where he stated:

> "(1) In order to succeed in obtaining security for costs an initial onus rests upon the moving party to establish: (a) that he has a prima facie defence to the plaintiff's claim, and (b) that the plaintiff will not be able to pay the moving party's costs if the moving party be successful.
>
> (2) In the event that the above two facts are established, then security ought to be required unless it can be shown that there are specific circumstances in the case which ought to cause the court to exercise its discretion not to make the order sought. In this regard, the onus rests upon the party resisting the order. The most common examples of such special circumstances include cases where a plaintiff's liability to discharge the defendant's costs of successfully defending the action concerned flow from the wrong allegedly committed by the moving party or where there has been delay by the moving party in seeking the order sought. The list of special circumstances referred to is not, of course, exhaustive."

13. In the present case, Pagnell contends that OCE does not have a *prima facie* defence to this claim. It maintains that the existence of a substantial lodgement is inconsistent with such a defence and, in any event, that OCE have not substantiated its defence in any meaningful way beyond mere assertion. While it also contends that OCE delayed unduly in making any such application, for the reasons I am about to outline, it is actually unnecessary to address this question. The arguments which focus on the *bona fides* of the defence and the making of the lodgement can now be considered in turn.

Whether the defendant has established a prima facie defence
14. The question of what constituted a *prima facie* defence for the purposes of s. 390 applications was considered by Finlay Geoghegan J. in her judgment in *Tribune Newspapers (in receivership) v. Associated Newspapers (Ireland) Ltd. (ex tempo*re, High Court, 25th March 2011) in which she summarised thus the approach of the courts to this question:

> "What appears from the judgments, in a manner similar to the judgments in relation to summary judgment, is that a defendant seeking to establish a prima facie defence which is based on fact must objectively demonstrate the existence of evidence upon which he will rely to establish those facts. Mere assertion will not suffice.
>
> If such evidence is adduced, then the defendant is entitled to have the Court determine whether or not it has established a prima facie defence upon an assumption that such evidence will be accepted at trial. Further, the defendant must establish an arguable legal basis for the inferences or conclusions which it submits the Court may arrive at based upon such evidence."

15. While the judgment in Tribune Newspaper was *ex tempore*, the relevant passage from that judgment was incorporated and referred to by Finlay Geoghegan J. in her subsequent judgment in *Webprint Concepts Ltd. v. Thomas Crosbie Printers Ltd.* [2013] IEHC 359, a judgment to which I will later return.

16. It follows, therefore, that it is not sufficient for a defendant merely to *assert* a defence. Recalling again the underlying objective of the section – namely, that defendants should not have to face claims made by limited liability companies who would have insufficient assets to meet an order for costs – a defendant must show that there are reasonable prospects that this is likely to occur unless security is ordered. In this respect and in this particular statutory context, it should be stressed that it is for the defendant to establish a *prima facie* defence. Contrary to what Hedigan J. may have suggested in his judgment, the fact that the plaintiff has taken no steps to apply to have the defence struck out as unsustainable is not in *itself* a relevant factor. After all, the *prima facie* defence requirement imposes a higher requirement on a defendant than that required, for example, to establish a defence to an application for summary judgment where it is merely necessary to show that the defence is simply arguable: see, *e.g., Danske Bank v. Durcan New Homes* [2010] IESC 22.

17. It is against this general background that the question of a *prima facie* case requires to be considered.

18. While the defence as delivered formally denies that there ever was an agreement or that, if there was, that it was terminated by it, so far as this appeal is concerned three substantive defences are advanced by OCE. First, it is said that there was an implied term which would justify the advance termination of the contract in August 2003. Second, it was said that Pagnell was guilty of a fundamental breach of contract by reason of the manner in which the CFP services were provided by it. Third, it was contended that Pagnell failed adequately to mitigate its loss in the aftermath of the termination of the contract. These arguments can be considered in turn.

Was there an in implied term justifying the termination?
19. It is clear from paragraph 13 of the defence that the defendant pleads that, on the assumption it terminated the agreement, there were:

> "implicit terms in the alleged contract that the defendant had an implied right to do so if the work undertaken by the plaintiff was substandard or if the underlying alleged contract between the defendant and AIB was terminated as if the work undertaken or service offered by the plaintiff offered by the plaintiff was not to the satisfaction of AIB."

20. In an affidavit sworn by David Lowe, a director of OCE, on 17th November 2009 in order to ground the application for security, it is averred that the contract contained two implied terms which permitted the termination of the agreement on (i) the giving of reasonable notice or (ii) if the printing work supplied by Pagnell was substandard or if the work undertaken or performed was not to the satisfaction of AIB. Mr. Lowe then avers that reasonable notice was given. He further stated that AIB's concerns were drawn to Pagnell's attention, "but the plaintiff failed to deal adequately with these issues." He further claims that AIB then terminated the agreement with OCE as a result.

21. It is clear that a term will only be implied into a commercial agreement of this kind where it is necessary – and not merely reasonable – to do so and the term must also be necessary to give business efficacy to the agreement: see *Meridian Communications Ltd. v. Eircell Ltd.* [2002] 1 I.R. 17, 41, *per* O'Higgins J. Having regard to the fixed term nature of this commercial supply of services contract, it seems unlikely that a term providing for reasonable notice would be implied. This is especially so, as given that the time period agreed (60 months) was by no means excessively long for contracts of this kind, it might be difficult to say that the implication of such a term was necessary to give the contract the necessary business efficacy.

22. Even if such a term could be implied, it would be necessary to have details of the extent of the notice which OCE contends it afforded to Pagnell. In *Webprint Concepts* one of the defendants seeking security for costs contended that it had a *prima facie* defence of *force majeure* in circumstances where the contract had been terminated without the plaintiff having been given the two months notice to which it was contractually entitled. Finlay Geoghegan J. held, applying the *Tribune Newspapers* test, that this particular defendant had not established *a prima facie* defence of *force majeure* because:

> "There is no evidence of any facts sought to be relied upon as *force majeure* and no evidence of a notification of any event of *force majeure* as required by Clause 11(2) of the Printing Agreement."

23. Much the same can be said by analogy in the present case, as OCE have failed to provide any objective evidence of the existence of facts such as might ground its defence of adequate notice.

24. So far as the customer satisfaction issue is concerned, there would doubtless be an implied term to the effect that Pagnell would discharge its contractual obligations in a satisfactory way. Of course, if it failed in this obligation in some fundamental or highly material fashion, this would probably have amounted to a fundamental breach of contract in its own right which would have entitled OCE to repudiate the contract, irrespective of the existence of any specific contractual term, whether express or implied.

25. Here again, however, OCE's claims in this regard fail the *Tribune Newspapers* test. No objective evidence has been advanced to substantiate the contentions that AIB were dissatisfied with Pagnell's performance or that AIB terminated OCE's contract by reason of these alleged shortcomings. In a further affidavit sworn on 4th May 2010 Mr. Lowe claimed that he was informed by AIB "that if the defendant did not terminate its contract with the plaintiff that AIB plc would end its contract with the defendant"

26. To that end Mr. Lowe exhibited a letter from OCE to Pagnell dated 7th March 2003 which raised a number of issues. The first complaint related to the attitude of Pagnell's staff which, it was said, was clearly affecting the willingness of Bank staff to approach the copying centre to have work done. OCE insisted that "a full change in staff be made". The second major complaint related to colour pricing which was said to have been uncompetitive. OCE asked for a "significant" reduction in this pricing. The write concluded by suggesting that a service level agreement was necessary in order to measure "OCE's requirements to provide AIB Central Facility Management with an excellent service."

27. This single of item of correspondence certainly shows that OCE had raised important issues with Pagnell, particularly in respect of one important aspect of staff performance. Yet taken on its own it cannot be said that it comes close to demonstrating the existence of *prima facie* defence that there had been a fundamental breach of contract on the part of Pagnell. If there had been such a deficiency of performance on the part of Pagnell or if AIB had threatened to terminate the contract with OCE unless Pagnell was not itself removed as sub-contractors one would expect that such would have attested by further correspondence after March 2003 or, at the very least, by some other documentary records which might tend to bear out these contentions.

28. In these circumstances, it cannot be said that OCE has furnished a *prima facie* defence to these claims by reason of the existence of some implied term.

Fundamental breach of contract

29. So far as the fundamental breach of contract argument is concerned, it follows that for the reasons which have just been given that no objective evidence regarding a fundamental breach of contract has been advanced by OCE. It might also be observed that the defendant does not actually plead that there was a fundamental breach of contract on the part of Pagnell. The furthest that OCE's defence is put is the claim contained in the statement of claim that the contract was terminated by reason "of AIB's dissatisfaction with both the level and quality of service being offered by the plaintiff in the CFP and the plaintiff's pricing." Even accepting that the letter of March 7th, 2003 gives some support to this argument, the fundamental complaint here – namely, that of end-user dissatisfaction with aspects of the quality, price and service – is nonetheless some distance removed from any contention that there was a fundamental breach of contract.

30. Putting this another way, OCE has not even pleaded that Pagnell was guilty of a fundamental breach of contract and, even if it had, the objective evidence adduced falls a good way short of showing that it could substantiate this claim.It follows, therefore, that OCE has not advanced a prima *facie defence* so far as the fundamental breach of contract claim is concerned.

The mitigation of loss argument

31. So far as the mitigation of loss argument is concerned, it must be recalled that this can but rarely constitute a defence in its own right. The question of mitigation normally only arises where the existence of a contractual breach is found or admitted, so that the failure to mitigate is a factor which serves to abate the amount of damages which might otherwise be awarded.

32. There are, it is true, exceptional cases where the failure to mitigate has been so gross that no award of damages at all would be justified, any breach of contract notwithstanding. An example here is *McCord v. Electricity Supply Board* [1980] I.L.R.M. 153 where the plaintiff's failure to sign a non-incriminating document saying that he had not interfered with the electricity meter was held by the Supreme Court to amount to such a gross failure to mitigate loss as to disentitle him to any damages, even though the Court also held that the disconnection of the plaintiff's electricity supply was itself a breach of contract.

33. It may be that in special and unusual cases such as *McCord* the existence of such extensive plea of failure to mitigate might have amounted to a *prima facie* defence. In the majority of cases, however, the failure to mitigate will simply go to the issue of damages and could not properly be regarded as a *prima facie* defence in its own right.

34. The present case is no different. OCE have certainly *asserted* that Pagnell failed to mitigate its loss. It may well be that at the trial of the action this can be established such that the level of damages otherwise payable in respect of any finding of breach of contract that might be made might be reduced or abated. As things stand, however, OCE have adduced no evidence to show, for example, that there was another printing contract immediately available to Pagnell in August 2003 to which it might readily have switched after the termination of the contract, thus avoiding any loss whatsoever, even if a breach of contract were to be established.

35. In this respect, therefore, this plea fails the *Tribune Newspapers* test articulated by Finlay Geoghegan J., namely, the obligation "objectively [to] demonstrate the existence of evidence upon which he will rely to establish those facts." It follows, therefore, that as the defendant has not established a *prima facie* defence, it would not be appropriate to direct the making of an order for security for costs.

The making of the lodgement

36. Central to OCE's case regarding the lodgement is that it was made without any admission of liability and without prejudice to its defence. Counsel for OCE, Mr. Delahunt, submitted that no inference regarding the *bona fides* of the defence could properly be drawn from the existence of such a lodgement. It is, of course, perfectly true that lodgements are made for any number of reasons and the making of a lodgement is not necessarily inconsistent with a defence on the merits. A common example is where defendant elects to make a small lodgement even in the face of an unmeritorious claim on the purely practical basis that it makes more economic sense to dispose of the claim in this manner at an early stage rather than endure lengthy litigation and thereafter attempt to recover any award of costs from an impecunious litigant.

37. The present case cannot, however, be realistically viewed in this manner. While it is true that the present claim is valued by the plaintiff at over €400,000 and the lodgement is but a fraction of that claim, the sum itself so lodged is nevertheless a significant one, even if the security subsequently fixed by Hedigan J. at €140,000 is also a very large one. It is also significant that a lodgement of this nature was made well in advance of any suggestion that an application for security for costs might even arise. This is surely a factor to which the court can properly have regard in the particular circumstances of this case, since it suggests that the defendant itself had thereby tacitly acknowledged that the plaintiff's claim is one of substance ever before the question of security for costs actually arose.

38. This matter was considered by the English Court of Appeal in *Parkinson & Co. v. Triplan Ltd.* [1973] 1 Q.B. 609, a case where the defendant made an open offer in correspondence but later sought security for costs. While the exact sum tendered was not disclosed in the judgment – as an arbitration was pending – it appears to have been a significant sum. The Court certainly saw the existence of such a lodgement as a highly relevant factor.

39. Lord Denning M.R. first helpfully set out some of the governing considerations regarding the exercise of discretion in matters of this nature. These included ([1973] 1 Q.B. 609, 626):

> …whether the company's claim is *bona fide* and not a sham and whether there is an admission by the defendants on the pleadings or elsewhere that the money is due. If there was a payment into a court of a substantial sum of money (not merely a payment into court to get rid of a nuisance claim) that, too, would count. The court might also consider whether the application for security was being used oppressively – so as to stifle a genuine claim. It would also consider whether the company's want of means has been brought about by any conduct on the part of the defendant, such as delay in payment or delay in doing their part of the work."

40. Lord Denning went to say ([1973] 1 Q.B. 609, 627) that an open offer of a substantial sum was:

> …a matter which the court can take into account. It goes to show that there is substance in the claim: and that it would not be right to deprive the company of it by insisting on security for costs."

41. Applying these principles to the present case, it can be said that the existence of a substantial lodgement of this kind made by way of open offer well in advance of any application for security for costs may be regarded as recognition by the defendant of the fact that the plaintiff's claim is one of substance and is likely to succeed, at least in substantial part. As Lord Denning pointed out, it would be generally inappropriate to insist on security in cases of this kind. To do otherwise would be to invert the appropriate priorities to which the legal system should properly have regard, since it would enable the well resourced defendant to employ a statutory power - which was designed to ensure that the privilege of limited liability is not itself abused in order to defeat orders for costs - for another purpose entirely. The Oireachtas plainly did not intend that s. 390 of the 1963 Act would be utilised to suppress claims which the defendant by its very own conduct – namely, the making of an open lodgement for a substantial figure – must be taken to have acknowledged are meritorious and substantial in their own right.

42. In my view, therefore, the very fact that the defendant has paid a substantial sum into court by way of open lodgement in the circumstances in which it did in this case well in advance of any subsequent application in respect of security for costs can only be regarded as an acknowledgment that the plaintiff's case has significant merits. In these circumstances, this in itself is a reason not to order security for costs under s. 390 of the 1963 Act.

Conclusions

43. The defendant has not established a *prima facie* defence. Its claims that that it was entitled to terminate by reason of the existence of an implied term of reasonable notice or by reason of manifest dissatisfaction with the method of performance of the contract have not been substantiated by the necessary objective evidence which might otherwise have possibly provided the foundation of a *prima facie* defence.

44. The existence of a substantial open lodgement made well in advance of the circumstances giving rise to an application for security for costs can only be regarded as a tacit admission that the plaintiff's claim is significant and meritorious. The making of the lodgement in the present case amounts to special circumstances such as would justify this Court in refusing to make an order for security pursuant to s. 390 of the 1963 Act.

45. It is for these reasons, therefore, that I would allow the appeal and set aside the order directing that Pagnell furnish security pursuant to s. 390 of the 1963 Act.