THE HIGH COURT

[2017 No. 290 COS]

IN THE MATTER OF QUESADA DEVELOPMENTS LIMITED

AND IN THE MATTER OF THE COMPANIES ACT, 2014

JUDGMENT of Ms. Justice Baker delivered on the 21st day of December, 2017

1. Neil Hughes ("the Examiner") was appointed examiner of Quesada Developments Limited ("the Company") on an interim basis on the 11th August, 2017, and confirmed by my order of 5th September, 2017. The period of protection has been extended and this judgment is given on the application by the Examiner for confirmation of proposals for a scheme of arrangement ("the Scheme"), which is opposed by two directors and shareholders of the Company.

2. The petition for examinership was presented to the court by Mr. Brendan O'Hanlon, one of three directors and shareholders of the Company and who now opposes the Scheme. The Scheme is also opposed by another director and shareholder, Mr. Dermot McSherry.

3. The Examiner in his grounding affidavit describes the examinership as "most unusual and contentious", and it is clear from his affidavit and the affidavits of the persons who opposed confirmation of the Scheme that the process has been acrimonies and difficult.

4. Quesada operates a nursing home known as Beechpark Nursing Home and Convalescent Centre in Dunmurry West, Co. Kildare. The Company has 56 employees and occupies under an informal letting agreement a purpose-built nursing home facility for the care of elderly and infirm persons who live there on a long term or permanent basis. It is accepted by all parties that the nursing home is well run and that it provides a very high standard of care for all of the residents.

5. The Company is insolvent and was unable to pay its debts and sought the protection of the court in those circumstances. The auditors of the Company have resigned and there were operational losses which gave rise to ongoing management difficulties. The members of the Company are Mr. O'Hanlon and Mr. McSherry and Thomas Ryan, each of whom is an equal shareholder and director. The shareholders have been embroiled in proceedings pursuant to s. 212 of the Companies Act ("The Act") which Mr. O'Hanlon says were commenced by him and his fellow shareholder Mr. McSherry in order to prevent the continued outflow of money to Mr. Ryan from Company resources. A receiver was appointed to the nursing home premises from which the Company trades, and the receivership effectively stayed those proceedings, as no agreement could be reached with the receiver regarding the right of the Company to occupy the nursing home premises.

6. A source, albeit not the only source, of the dispute between Mr. Ryan on the one part and Mr. O'Hanlon and Mr. McSherry on the other part which gave rise to the proceedings under s. 212, and which form the backdrop to the confirmation hearing, relates to the director's loan account of Mr. Ryan, and to a lesser extent of Mr. O'Hanlon and Mr. McSherry. In simple terms Mr. O'Hanlon and Mr. McSherry argue that Mr. Ryan is indebted to the Company in a significant amount, sufficient they argue to meet the ongoing financial needs of the Company, and that it is Mr. Ryan's indebtedness to the Company which has caused it to become insolvent. Mr. Ryan on the other hand argues that he is a creditor of the Company, and that any claimed director's loan is offset by an amount owed by the Company to him in respect of other matters.

7. The directors' loans disputes relates to a large extent to the VAT treatment of rates paid by the Company to its landlord, and to the fact that Mr. Ryan and his wife are said to have used their own personal VAT registration number to deal with VAT claims and refunds. Mr. Ryan holds the legal title in the nursing home premises, on trust for himself and Mr. O'Hanlon and Mr. McSherry as tenants in common in equal shares.

The Scheme

8. The Scheme provides for the investment by Daleland Limited, a company controlled by the wife of Mr. Ryan, of the sum of €150,000 into the Company, the cancellation of existing shareholdings, the resignation of Mr. O'Hanlon and Mr. McSherry as directors, and in practical terms the Scheme will have the effect that Mr. Ryan takes over the running of the Company and its enterprise. In a parallel transaction Daleland Limited has agreed with the receiver to purchase the freehold interest in the nursing home premises and Daleland Limited has agreed to grant an occupational release to Quesada for the purpose of the nursing home business.

9. The Examiner has expressed an opinion on affidavit and in his report prepared for the purpose of s. 534 of the Act that the conditions set out in the Independent Expert's Report (IER) for the survival of the Company have been met, that the implementation of the Scheme will ensure that the continued employment of the 56 employees, and that the Company has what he describes as a "very good prospect of survival". During the currency of the examinership the Company has retained the confidence of its key suppliers and Mr. Hughes is confident that should the Scheme be confirmed no difficulty will arise with HIQA with regard to the smooth transition to new management of the nursing home facility.

The directors' loan account

10. From the s. 534 Report and from the affidavits and the submissions on behalf of Mr. McSherry who appeared through counsel, and of Mr. O'Hanlon who represented himself, it is clear that one of the reasons for the financial difficulties in the Company was the total breakdown of the relationship between the members and directors, and the s. 212 proceedings which remain live, have been costly in terms of resources, and show the extent to which the owners of the Company and the directors have found it impossible to continue to work with one another.

The investment process

11. Mr. Hughes explains the process engaged by him in seeking investment proposals regarded as essential in the IER to provide sufficient working capital for the Company and to pay a dividend to creditors. The process resulted in the preparation of the Scheme and the holding of meetings of classes of creditors and members on the 9th November, 2017.

12. The Examiner considered that the creditors of the company should be divided into separate classes being: super preferential creditors, preferential creditors, (both of which classes voted in support); unsecured creditors which are impaired, and which accepted the proposals; the connected creditors which class voted against; and contingent personal guarantee creditors, being Mr. Ryan and Mr. O'Hanlon, the meeting of which class was inquorate.

13. One class therefore of impaired creditors, the unsecured trade and supply creditors of the type that one would expect in a nursing

home business, voted in favour. The threshold requirement in s. 541(4)(a) of the Act is met. This is not in dispute.

14. The Scheme provides for a very small dividend of 5% to these creditors, but it is noteworthy that the Examiner avers on affidavit that he has retained the confidence of these creditors in the course of his examinership notwithstanding the insolvency of the Company and the fact that they are significantly impaired in the Scheme. This fact supports the view of the Examiner that the Company has a good prospect of survival.

15. Mr. Hughes calculates that the return to all creditors is better in the examinership than it would be in a liquidation, where the unsecured creditors and connected creditors would receive no dividend and the preferential creditors would receive 4.4%, instead of full payment of its debt as provided in the Scheme.

The confirmation hearing

16. Revenue was represented by counsel and proposed a number of modifications to the Scheme, which were ultimately accepted by the investor Mr. Ryan and by the Examiner. Details of the modification are set out later in this judgment.

17. It is clear from the s. 534 Report that the primary issue in the examinership was the issue of the directors' loans which Mr. Hughes investigated and analysed, but in respect of which he was unable to come to a determination. This issue became the centre of the argument at the confirmation hearing.

18. The Examiner explains that for the purposes of ascertaining the position with regard to the directors' loans he took the figures from the last set of audited accounts prepared in 2015, which had been signed by Mr. O'Hanlon and Mr. McSherry, but not by Mr. Ryan. They show that Mr. Ryan indebted to the Company in the sum in round figures of €147,000. They also showed that the other two directors were owed the sum of €94,000 each by the Company.

19. The extent of disagreement is apparent from an example: Mr. Ryan's position is that he is owed a sum of €234,000 by the Company and the other two directors each owe €130,000. Mr. McSherry argues that Mr. Ryan is indebted to the company in the sum of €300,000. These figures are examples of the very complex workings exhibited in the affidavits of Mr. Hughes and of Mr. O'Hanlon and Mr. McSherry, and I take no view as the correct position. I mention the figures here by way of illustration of the extent of the disagreement between the parties.

20. Because of the degree of difficulty that Mr. Hughes explains he had in coming to a determination with regard to the directors' loans, and having regard to the very significant degree of disagreement between the three directors as to the amount of any loans, and the liability of each of them in respect of the loans, Mr. Hughes, proposed a resolution process which is incorporated into the modified Scheme. The proposal made by the Examiner is for the appointment of a nominated expert to determine the true liability to the Company of each of the three directors in respect of their loans, and to determine whether any one of all of them is to be treated as a creditor of the Company. The expert is to act as expert and his determination is proposed to be final and to bind all three directors. The modified Scheme contains procedural and substantive provisions that should the expect determine that Mr. Ryan or the other two directors are indebted to the Company, payment by the relevant parties to the Company is to be made within 24 months of the date of his determination and provision is made for the payment of an additional distributive dividend to the creditors from any sums recovered.

21. Mr. O'Hanlon argues that Mr. Ryan has engaged in wrongful acts and thereby deprived the Company of working capital, and the modified proposals provide that Mr. Ryan shall voluntarily agree to be restricted from acting as a director of the Company, including acting as a shadow director, pending the determination of the expert or should he be found liable to repay monies to the Company, until such time as that liability has been discharged in full. Counsel for Mr. Ryan has offered that his client will give an undertaking that Mr. Ryan will not act or seek to act as director or shadow director of the Company for a period of 24 months from the date of the approval of the Scheme, if it is approved by the court.

22. A further modification became the focus of argument towards the end of the hearing on 19th December, 2017 relating to the costs of the expert, and I deal with that at the end of my judgment

23. Mr. Hughes has made a "working assumption" that Mr. Ryan is indebted to the Company in the sum of €147,000, but the modified Scheme is not dependent on the correctness of the assumption made by the Examiner.

24. The Examiner accepts that the Scheme is less than prefect, but expresses a view in his three affidavits sworn for the purpose of the confirmation hearing that the Company has a reasonable prospect of survival as a going concern, and that survival is in the best interests of the members and creditors of the Company, of the 50 employees whose livelihoods are dependent on the survival of the Company, and that the interests of the residents in the nursing home, would best be protected by the Scheme.

The objections

25. The primary objection made by both Mr. O'Hanlon and Mr. McSherry, albeit with different emphasis, is that Mr. Ryan will by virtue of the Scheme be permitted to take control of the Company for a sum which is very close to the amount which is shown in the 2015 accounts to be owed by him to the Company. It is argued that in effect Mr. Ryan will be permitted to "trade out of his debt" to the Company, and that he will in effect be "cleansed" of his wrongdoing. Mr. McSherry in particular argued that the correct approach of the court should be to avoid permitting the examinership process from being used as an instrument by which Mr. Ryan's wrongdoings could be forgiven or at the least ignored, and that the more robust investigative process available to the liquidator suggests that the Scheme ought to be rejected, and the Company liquidated. He relies on the *dicta* at para. 30 of my judgment in *Re Step One Permanent Solution* 2015 IEHC 284 for that purpose, and on the statement at para 8.41 of O'Donnell *Examinerships* (2nd revised ed.) that the discretion of a court may be engaged to refuse "to confirm proposals that have improper consequences", and that intention to act other than *bona fide* does not need to be established.

26. Mr. McSherry argues that, as this is a service business, there is in truth no risk that the jobs will be lost, or that the residents of the nursing home would be discomfited, as it is highly likely that another operator would immediately take over and run the business without any obvious interruption. He argues therefore that the balance of interests between the employees and the justice of the case favours the liquidation of the Company, as justice requires that the process not be used for improper purposes, or be a mechanism by which Mr. Ryan will avoid sanction.

27. Mr. McSherry also argues that the Examiner did not properly engage the investment process, that he "moved the goalposts" to give Mr. Ryan a clear advantage, and did not reply to his due diligence inquiries. The circumstances giving rise to that argument may briefly be summarised. Mr. Hughes commenced the process of seeking investment proposals and obtained eight indicative proposals. Mr. McSherry proposed that he would invest the amount of €300,000 and a bid at the same level was made from an external nursing

home operator. The Examiner then issued a letter to each of eight parties requesting further information and supporting documentation, and six parties reverted to him. Of these, he invited three parties, of whom Mr. McSherry was one, to take part in due diligence. In that process he liaised with the receiver appointed by Ulster Bank, David O'Connor, as he and Mr. O'Connor shared a view that the Company would be best protected if the same party was the preferred bidder in the receivership and preferred investor in the examinership. Ultimately, the bid of the external third party was withdrawn, Mr. McSherry did not finalise his bid and the bid made by Mr. Ryan's company, Daleland, was reduced to €101,000. The Examiner refused to accept a bid this low and ultimately Mr. and Mrs. Ryan, the controllers of Daleland, made an offer of €150,000. That was accepted as the only funded offer. It was that bid that formed the basis of the Scheme presented to the meetings of creditors and members.

Determination on the evidence

28. I have examined the correspondence and I consider that the Examiner is correct and that Mr. McSherry did indeed withdraw from the bidding and the letter from his solicitors of the 3rd November, 2017 made it clear that issues which had been raised relating to the directors' loans had to be resolved before a potential bidder could be in "an informed position".

29. The investment amount was disappointing, but I accept the evidence of the Examiner, borne out by the correspondence, that the bidding process was conducted openly and in accordance with the statutory obligations of the Examiner. Mr. O'Hanlon does not as such oppose the confirmation of some scheme, but very carefully explained in his affidavit and submissions to me a view that the calculations of Mr. Hughes and those presented to him by Mr. Ryan are incorrect, but supports the argument of Mr. McSherry that the process ought not to result in an arrangement where Mr. Ryan potentially escapes being held accountable for his wrongdoing in his management of the company.

30. Mr. McSherry and Mr. O'Hanlon argue that the Company is not suitable for examinership in the light of the intractable dispute between the directors and members regarding the loans or any money owed by the Company to them. Ironically Mr. O'Hanlon was the petitioner, and Mr. Ryan objected to the appointment. Nonetheless, while that irony might superficially suggest that Mr. O'Hanlon is no more than a disappointed investor, the matters raised by him and by Mr. McSherry are significant and have given rise to great difficulty in concluding the examinership process.

31. It is clear too that the s. 212 proceedings which have not been resolved, will effectively be terminated should the Scheme be confirmed, but I reject the argument made by Mr. McSherry that the s. 212 proceedings are most likely to lead to a court ordering the winding up of the Company, and while that is sometimes a result of such proceedings, the power of the court often results in the purchase at an agreed or determined value of the shares of the minority, or in a court imposed or agreed restructuring of membership. The continuation of those proceedings is not in the interest of the Company, and as it is clear that the Company is insolvent and that winding up by order in the examinership process under s. 535(2) is an almost inevitable result of the failure of the Scheme.

32. This indeed has been a most difficult examinership, and neither Mr. McSherry nor Mr. O'Hanlon makes any argument that the Examiner failed to perform his functions with skill and professionalism. Both of them are in different ways critical of the approach of the Examiner, but in truth each of them argues that the Scheme ought not to be approved because it is unfair to them or more especially because the practical and legal effect of the Scheme will be to forgive alleged wrongdoing by Mr, Ryan.

33. It is clear to me from hearing the submissions by counsel for Mr. Ryan and Mr. McSherry and hearing Mr. O'Hanlon in person that the degree of animosity between the parties remains at a high level, and that the dispute between them is intractable and was incapable of resolution by the Examiner. An examiner is constrained by his statutory powers and by the time limits imposed by the Act and I consider that it is not envisaged by the statutory scheme that an examiner would be required to determine matters of such a degree of factual complexity. The focus of the examinership process is the survival of a company and its enterprise, and not the resolution of inter shareholder disputes or disputes between directors as to the management of the company.

34. The judgment of Clarke J. in *Re: Traffic* 2007 IEHC 445 is of assistance in explaining the correct focus of the court, which is the preservation of a company and its enterprise, the saving of jobs, and the wider public interest. That focus is well established in the authorities. It may be the case as argued by Mr. McSherry, that the jobs of the persons currently employed by the company would be safe or relatively safe in a liquidation, but that particular response to the dilemma fails to have regard to the likely disruption of employment in the course of the liquidation, or indeed the possibility, even if it is not a probability, that the enterprise would wholly fail. In the judgment of Clarke J. in *Traffic* there was an actual and established wrongdoing by one of the directors and Clarke J. considered that the scheme should still be approved albeit with a modification that prevented the relevant director from acting as a director in the company for a period of eighteen months.

35. In another judgment relied upon by counsel for Mr. McSherry, the judgment of Clarke J. in *Laragan Developments Ltd*. [2009] IECH 390, Clarke J. refused to approve the scheme of arrangement party because he considered that the company in question was "little more than a vehicle of convenience" for its director and other companies within a group controlled by him. He considered that the relationship "lacked even the semblance of an arms' length arrangement" and came to the view that the company could not properly be the subject of an examinership "on a standalone basis" and that it was not "the sort of enterprise which can properly be described as an undertaking for the purposes of the Act."

36. In my analysis of the Scheme I consider that the alleged wrongdoing by Mr. Ryan has been adequately dealt with by the appointment of an expert who is to determine the extent, if any, of Mr. Ryan's liability to the Company and that of the other two directors should that be relevant. The Company and the creditors are to benefit from this, not Mr. Ryan. While the objections of Mr. McSherry and Mr O'Hanlon are understandable, they derive in my view from their approach to the ongoing and intractable dispute between them and Mr. Ryan, and from their, again understandable, but legally incorrect approach to the matter which fails to have regard to the separate corporate personality of the Company.

37. Mr. McSherry curiously supports the liquidation of the company, and I consider it relevant that he was one of the final three potential investors, and could in those circumstances be regarded as a disappointed investor, a party whose interests are not a relevant consideration in the examinership process.

38. The Scheme notably provides for the furnishing of the report by the Examiner and by the expert separately to the ODCE of the determination of the expert regarding the directors' loans. Mr. McSherry makes the argument that the ODCE is unlikely to engage with any alleged wrongdoing by Mr. Ryan with the same degree of enthusiasm as might a liquidator, but I regard it as relevant that the ODCE has written to Mr. Hughes on the 3rd of November, 2017 and sent a reminder on the 13th December, 2017 seeking a report in accordance with s. 534 (6) (b) of the Act and has asked the Examiner to set out the reasons why the Company entered examinership and the role of the directors in the process.

39. I am satisfied therefore that sufficient civil remedy and regulatory oversight has been put in place to allay some, even if not all, of

the concerns of Mr. McSherry and Mr O'Hanlon regarding Mr. Ryan.

Legal principles
40. This case brings into focus the question of the extent to which a court should favour examinership over liquidation in a suitable case. The examinership process was introduced by statute to avoid the catastrophic effect on employees, and on the "wider community interest", a phrase used by Clarke J. in *Re Laragan Developments Ltd.*, of the more blunt instrument of liquidation. In essence the examinership process permits a breathing space and interposes an expert whose statutory function is to seek an investment by which a company is given a reasonable prospect of survival, and the result of which is likely to afford a better return for creditors than would be achieved in the more costly option of liquidation.

41. In *Re Ladbrokes (Ireland) (Limited),* [2015] 1 IR 243, 2015 IEHC 281, Cregan J. stressed the importance of the "commercial judgment" of an examiner in the "weighing up and calibration" of competing interests. Mr. Hughes has made it clear that in his commercial judgment the Company has a "very good chance of survival", and has also explained in some detail the reason why he accepted a bid which was disappointing having regard to earlier indicative bids. A significant factor in the view of Mr. Hughes is that the freehold of the premises is now subject to a contract for sale to Daleland and accordingly Mr. Ryan's wife will have a controlling interest in the landlord and will in those circumstances be more likely to put in place a leasehold arrangement that is beneficial to the Company and its ongoing operation.

42. I am satisfied that the remedial measures proposed in the Scheme are adequate to deal with the disputed directors' loans. I accept what is argued by Mr. McSherry and Mr O'Hanlon, that the Scheme is not perfect, but the achieving of perfection having regard to the degree of animosity between the three directors and the intractable nature of their dispute which is already the subject matter of court proceedings made it impossible in my view for the Examiner to achieve an end result that would satisfy all three directors, or at least give each of them the solution that they preferred.

43. The focus of a court in considering whether to approve a scheme is the survival of the company and not the resolution of disputes between members. While it would have been preferable had the Examiner been in a position to ascertain the correct position regarding the directors' loans, I accept the evidence of Mr. Hughes that this has not been possible, and I consider that the Examiner could not have been expected to resolve that issue in the short statutory time frame in which he was operating, and the degree of animosity and lack of trust between the three directors made it difficult, if not impossible, for Mr. Hughes to resolve, with the limited statutory mechanism available to him, a matter of such complexity and in respect of which there was such a degree of factual disagreement.

44. Mr. O'Hanlon has proposed an additional modification which would have involved a "standstill" period of a further 30 days. The statutory time limits under the Act are short and the time ahs already been extended on two occasions. The hearing was had on days 123 and 124 of the process. The proposed modification could result in the Scheme being modified to an extent that changes its meaning and effect and might not be sufficiently similar to that voted for at the relevant meetings to permit it to be confirmed. Further, I do not consider that the Act envisages a court staying the process pending the determination of a dispute for the 30 day period proposed by Mr. O'Hanlon, which is disproportionate having regard to the very narrow time limit of 70 days in s. 520 of the Act. An examiner has limited functions and ought not be permitted to engage executive powers under s. 528 of the Act for a further period than is desirable to achieve agreement on a scheme for presentation to the court. The Examiner has already completed the statutory process The proposed modifications are now too late to be incorporated into the Scheme for that reason

Decision
45. Because I am satisfied that the Company has a reasonable chance of survival, and because of the fact that the resolution mechanism is sufficiently robust to deal with the issues that have arisen in the course of the confirmation hearing, I propose making an order confirming the coming into operation of the Scheme as modified. Two modifications were made to the Scheme and the revised modifications before the court on the 19th December 2017 is to be the annexed to my order.

46. I propose a further modification pursuant to my power under s. 541(3)(b) of the Act so as to provide for the costs of the expert as follows:

> *the Company is to be responsible for the costs and expenses of the expert in connection with his determination of the issues, subject only to the entitlement of the Company to seek a contribution from Mr. Ryan, Mr. O'Hanlon and Mr. McSherry or any one of them pro rata to the amount that any of them is found by the expert to be liable to the Company.*

47. I will receive the undertaking from Mr Ryan not to act as director or shadow director of the Company for a period of two years. This is an approach favoured by Clarke J. in *Re Traffic* which I find suitable to deal with some of the concerns of the objectors. The ODCE has already shown an interest in the process and the Scheme provides for the furnishing of a report by the expert to that office, as well as expressly reflecting the statutory duty of the Examiner to furnish such report. That process has already commenced and may offer further comfort to the objectors.