THE COURT OF APPEAL

Neutral Citation Number: [2018] IECA 300

Record No. 2018/46

2018/47

Irvine J.
Hogan J.
Baker J.

IN THE MATTER OF IRISH LIFE & PERMANENT GROUP HOLDINGS PLC

AND IN THE MATTER OF IRISH LIFE & PERMANENT PLC AND IN

THE MATTER OF AN APPLICATION FOR THE SETTING ASIDE PURSUANT

TO SECTION 11 OF THE CREDIT INSTITUTIONS (STABILISATION)

ACT 2010 OF THE DIRECTION ORDER WHICH WAS MADE ON THE 26TH

JULY 2011 PURSUANT TO SECTION 9 OF THE CREDIT INSTITUTIONS (STABILISATION) ACT 2010 AND ANCILLARY ORDERS

BETWEEN:

GERARD DOWLING, PADRAIG MCMANUS, PIOTR SKOCZYLAS AND SCOTCHSTONE CAPITAL FUND LIMITED

APPELLANTS

- AND -

THE MINISTER FOR FINANCE

RESPONDENT

- AND -

PERMANENT TSB GROUP HOLDINGS PLC AND PERMANENT TSB PLC

NOTICE PARTIES

JUDGMENT of Mr. Justice Gerard Hogan delivered on the 2nd day of October 2018

1. Where the State makes an enormous investment in the public interest in a failing institution on a compulsory basis and where these actions have been found by the Court of Justice not to contravene EU law, in what circumstances (if any) can this decision be challenged as unreasonable on domestic administrative law grounds? This is perhaps the principal question which is posed in this highly complex appeal. Before considering any of these questions, it is, however, first necessary to sketch out the factual background.

The background facts

2. In this appeal the appellants, who are shareholders of the company, seek, in effect, to challenge the validity of the mechanism whereby Irish Life and Permanent Group Holdings plc ("ILP") was recapitalised by ministerial order (known as a "direction order") in July 2011. As one might, perhaps, expect, the proceedings to date have been complex and have generated a range of interlocutory applications, a number of which have ultimately been determined by the Supreme Court.

3. The first substantive judgment was delivered by the High Court (O'Malley J.) in August 2014: see *Dowling v. Minister for Finance (No.1)* [2014] IEHC 418. In that case O'Malley J. made a number of important factual findings, but, critically, she made a reference to the Court of Justice pursuant to Article 267 TFEU concerning aspects of the Second Company Law Directive. The Court of Justice ultimately delivered judgment on the 8th November 2016: see Case C-41/15 EU:C:2016: 836. It will be necessary in the judgment to refer in greater detail to both the first High Court judgment (and the findings of facts made therein) and the judgment of the Court of Justice.

4. Following the delivery of the judgment of the Court of Justice, the present case was then resumed in the High Court when a further judgment was delivered by O'Malley J. on the 31st July 2017: see *Dowling v. Minister for Finance (No.2)* [2017] IEHC 520. In that second judgment O'Malley J. dismissed the applicants' case and they then sought to appeal against that decision. In a further reserved judgment delivered in December 2017 O'Malley J. ruled that the applicants did not require the leave of the High Court to appeal to this Court against her decision of July 2017: see *Dowling v. Minister for Finance (No.3)* [2017] IEHC 832. Separate proceedings challenging the constitutionality of the Credit Institutions (Stabilisation) Act 2010 ("the 2010 Act") have yet to be determined by the High Court. This issue of constitutional validity does not, of course, form any part of this appeal and naturally I express no view on that question.

5. Before considering any of the legal issues which arise on this appeal, it is first necessary to say something about the structure of the 2010 Act and the background to the making of the directions order. As it happens, the 2010 Act has been amended significantly by the Central Bank and Credit Institutions Resolution Act 2011. As the directions order was made by the High Court pursuant to the

provisions of the 2010 Act (as that was the relevant legislation then in force when that application was made), it is unnecessary to consider the potential impact (if any) of the amendments subsequently made.

The 2010 Act

6. The 2010 Act was enacted by the Oireachtas on 21 December 2010. The recitals to the 2010 Act in their own way bear eloquent testimony to the extent of the crisis which the State was then facing:

> "Whereas there is a serious disturbance in the economy of the state;
>
> And whereas measures are necessary to address a unique and unprecedented economic crisis which has led to difficult economic circumstances and severe disruption to the economy;
>
> And whereas there is a continuing serious threat to the stability of certain credit institutions in the State, and to the financial system generally;
>
> And whereas it is necessary, in the public interest, to maintain the stability of those credit institutions and the financial system in the state;
>
> And whereas it is necessary, in the interests of the common good, to continue the process of reorganisation, preservation and restoration of the financial position of Anglo Irish Bank Corporation limited begun with the Anglo Irish Bank Corporation Act 2009;
>
> And whereas the functions and powers conferred by this Act are necessary to secure financial stability and to effect a reorganisation of certain credit institutions;
>
> And whereas it is necessary to amend the European Communities (Reorganisation and Winding-up of Credit Institutions) Regulations 2004 (S.I. No. 198 of 2004) to implement Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 to preserve or restore the financial position of certain credit institutions;
>
> And whereas the considerable financial support provided by the State to certain credit institutions has helped those institutions to meet their financial and regulatory obligations;
>
> And whereas the State wishes to provide for the performance of the functions conferred by this Act in order to achieve the financial stabilisation of those credit institutions and their restructuring (consistently with the state aid rules of the European Union) in the context of the national recovery plan 2011—2014 and the European Union/International Monetary Fund programme of financial support for Ireland;
>
> And whereas the common good requires permanent or temporary interference with the rights, including property rights, of persons who may be affected by the performance of those functions;
>
> And whereas the urgent reorganisation of certain credit institutions is of systemic importance to the State;
>
> And whereas it is necessary to maintain public confidence in, and enhance, the protection of deposits in credit institutions generally;
>
> And whereas it is desirable to promote and facilitate investment by persons other than the state in credit institutions to reduce their reliance upon State support;
>
> And whereas because certain credit institutions in the State are parties to contracts and other arrangements governed by the law of a state other than the State; be it therefore enacted by the Oireachtas as follows:"

7. Section 4 of the 2010 Act provided that the objects of the 2010 Act were:

> "(a) To address the serious and continuing disruption to the economy and the financial system and the continuing serious threat to the stability of certain credit institutions in the State and the financial system generally,
>
> (b) To implement the reorganisation of credit institutions in the State to achieve the financial stabilisation of those credit institutions and their restructuring (consistently with the state aid rules of the European Union) in the context of the National Recovery Plan 2011-2014 and the European Union/International Monetary Fund Programme of Financial Support for Ireland,
>
> ……
>
> (e) To protect the interests of depositors in credit institutions,
>
> (f) To address the compelling need:
>
> > (i) to facilitate the availability of credit in the economy of the State.
> >
> > (ii) to protect the State's interest in respect of the guarantees given by the State under the Act of 2008 and to support the steps taken by the Government in that regard.
> >
> > (iii) to protect the interests of taxpayers,
> >
> > (iv) to restore confidence in the banking sector and to underpin Government support measures in relation to that sector,
> >
> > (v) to align the activities of the relevant institutions and the duties and responsibilities of their officers and employees with the public interest and the other purposes of this Act

(g) To preserve or restore the financial position of a relevant institution, and

(h) To empower the Court to impose reorganisation measures through orders made in reliance on the CIWUD Directive."

8. The 2010 Act provided that the Minister for Finance might, if he or she considered it necessary to secure the achievement of a purpose of the Act, make a "proposed order" proposing that a credit institution covered by the Act be directed to take or refrain from taking a specified action or actions. The Minister was then required to consult with the Governor of the Central Bank and then notify the credit institution concerned. Once these procedural requirements had been satisfied (s. 7 of the 2010 Act) the Minister was then entitled to make an *ex parte* application to the High Court for an order in the terms proposed.

9. The High Court was then required to make the order if it was satisfied that the procedural requirements of the Act had been complied with and that the opinion of the Minister (that the proposed order is necessary to secure the achievement of a purpose of the Act) was reasonable and was not vitiated by any error of law. As O'Malley J. made clear in her first judgment, the effects of a direction order "can be extremely wide-ranging, and there is no doubt but that they were radical in this case." As already stated, the 2010 Act was substantially amended by the Central Bank and Credit Institutions (Resolution) Act 2011, but nothing turns on that so far as this appeal is concerned.

10. The applicants seek an order pursuant to s.11 of the 2010 Act to set aside the direction order. In order to succeed, they must establish *either* that there was non-compliance with the requirements of s.7, *or* that the opinion of the respondent Minister as to the necessity for a direction order was unreasonable or was vitiated by an error of law. No issue arises in this appeal so far as the compliance with the procedural requirements specified by s. 7 of the 2010 Act is concerned. The issue, therefore, remains one as to whether the opinion of the Minister which grounded the requirements of the direction order was unreasonable or was otherwise vitiated by error of law.

The background to the application to the High Court on July 2011

11. It is next necessary to set out some of the background facts against which the application is made. Many of these facts are well known to the Irish public, but it is nonetheless necessary to set out them out in a little detail, since they formed the background to the original application to the High Court in July 2011. The two substantive judgments of O'Malley J. are of crucial importance as, indeed, are her findings of fact upon which the judgment of the Court of Justice was based.

12. The origins of the financial crisis to which the 2010 Act was directed was that Irish banks were too heavily exposed to the risk that the property market might deteriorate and were overly reliant on borrowings in international capitals markets as distinct from traditional deposit sources. When the financial crash happened and capital markets all but seized up in the wake of the Lehman Brothers collapse in September 2008, the Irish banks found themselves in a particularly vulnerable position. As O'Malley J. put it in her first judgment:

"Ireland was not unique in experiencing severe problems in the financial sector, but the link between the financial stability of the banks and the financial stability of the State was particularly strong here because of the relative size of the sector coupled with the extensive guarantee by the State of bank liabilities. The financial sector is said to have been, at its peak, five times the size of the economy. The consequence was that, while most if not all European Union members had to take radical measures to support their financial systems, the intervention by the Irish State was in relative terms enormous. By the time the State entered into the Programme of Support in 2010, it had, according to Mr Moran [the then Second Secretary of the Banking Division of the Department of Finance who swore several affidavits on behalf of the respondents], spent or committed €46 billion on the financial system. In 2011 the level of State support given to the banks was the equivalent of 223% of Gross Domestic product. The EU average was 12.5% GDP."

13. The first major step which had been taken by the State was the "bank guarantee" of September 2008, which was provided for in the Credit Institutions (Financial Support) Act, 2008. This gave a State guarantee to customer deposits for amounts over €100,000 for a period of two years. The CIFS scheme was replaced on its expiry by the Eligible Liabilities Guarantee ("ELG") scheme. This was established in 2009 as a means of providing liquidity and other financial support to Irish credit institutions. Emergency liquidity assistance funding ("ELA") funding was also available from the Central Bank of Ireland and the European Central Bank (referred to as "Eurosystem" funding).

14. As O'Malley J. pointed out, these schemes were not cost-free - for example, the banks were charged for the cover provided by the guarantee. ILP paid €45m for the first half of 2010, and €94m for the same period in 2011. It also paid the European Central Bank for liquidity assistance. Market faith in the Irish banks was not, however, restored and deposits still seeped out of the system in a form of a silent bank run. All of this simply underscored the extent to which the Irish banks (including ILP) came to be reliant upon ELA funding.

15. On the eve of the international bail-out in November 2010, ILP's share price had fallen by 69% during the course of that year. At that point it was down **93.3%** from its peak market value, **which had been €6.3 billion in February, 2007. (It was down to €3.3 billion by the end of that year)**. The equivalent percentage falls for AIB and Bank of Ireland were 82% and 51% in 2010, with drops of 98.7% and 95.5% from peak value.

16. This was all happening against a background in which the State's financial position had deteriorated. Its credit rating fell persistently from the AAA+ it had enjoyed in early 2009, culminating in a "sub-investment" (or "junk bond") rating in mid-2011. In the year to the end of October 2010 the benchmark five year bond yields (i.e., the cost of State borrowing on international capital markets) rose from 3.1% to over 7%. Long term real interest rates in that range were all but unsustainable in a low inflationary environment. The broader economy was also radically affected in terms of cuts in public expenditure and rising unemployment.

17. There was also increased tensions in the bond markets, not least because of a fear of contagion in the Eurozone. Greece had received a €110 billion bailout in May 2010 and there was considerable speculation as to whether it would be followed by certain other vulnerable, mainly peripheral, Member States, including Ireland.

18. In her first judgment O'Malley J. summarised the difficulties which were then faced within the Eurozone:

"Mr Montgomery has described the "adverse feedback loop" that was creating difficulties for governments in the Eurozone. He says there were four main factors:

- The increased perceived risk of default on sovereign debt, connected to rising debt levels;

- increased concern over losses incurred by banks, risks of defaults on bank liabilities, and increased fiscal costs borne by governments to support banks;

- recessionary conditions particularly in countries subject to banking and sovereign debt concerns, leading to increased credit losses by banks and widening government budget deficits (as tax revenues contracted and government social expenditures rose); and

- rising concerns over the possible exit by one or more countries from the euro."

The position of ILP

19. It is next necessary to examine the position of ILP. A key part of the applicant's case is that ILP had at most experienced temporary liquidity difficulties and that it was not itself insolvent. It is true that there were, admittedly, features of ILP's performance that were, at least, positive on the surface. Unlike the other Irish main banks, it had not become involved in NAMA, since it had not lent extensively to property developers. Unlike AIB and Bank of Ireland it was not, prior to the events in question, a recipient of State capital - these two banks had received €11 billion between them in the period leading up to July 2011. It had not come under State control, as had happened to Anglo Irish, EBS and Irish Nationwide. (Ulster Bank had come under the control of the United Kingdom authorities.) ILP was not insolvent and it owned a profitable asset in Irish Life. (In 2010 Irish Life made an operating profit of €200 million, while the bank made an operating loss of €400 million.)

20. While all of this is true, it was by no means the full picture. As the State witnesses pointed out in the course of the first hearing (and which evidence was accepted by O'Malley J.) certain fundamental weakness had emerged in the course of 2008 in relation to ILP. By this stage its loan assets amounted to almost three times its deposits and it relied heavily on the wholesale money markets for almost two thirds of its funding. By June 2011 ILP's loan to deposits ratio of 228% as of June 2011 was significantly out of line with the figures for both AIB (143%) and Bank of Ireland (164%). ILP's reliance on monetary authority funding, expressed as a percentage of total assets, was, moreover, materially higher than AIB or Bank of Ireland (20%, as opposed to 15% for AIB and 7% for Bank of Ireland).

21. A further difficulty specific to ILP was that the percentage of its mortgage assets made up of loss-making tracker mortgages was unsustainably high - 66%, compared to 42% for AIB. "Tracker" mortgages were withdrawn as a financial product in 2008. The "Tracker" name comes from the fact that the banks typically charged a small margin over the wholesale bank interest charged by the ECB and the interest rate charged to customers then "tracked" the ECB main rate. But as those rates fell sharply, the margin rate was too low to make the tracker mortgages financially viable for a lender.

22. The real difficulties were not, however, to emerge until 2010/2011, as the full scale of the bank losses were realised and both the EBS and Irish Nationwide Building Society were nationalised. During 2010 the shareholders' equity in ILP fell to €300m. and in November 2010 the Central Bank announced that ILP was being required to raise a further €100m. of capital – a relatively modest sum in the circumstances - in order to raise its Tier 1 capital to a new target of 12.4%. Yet the share price continued to fall. While it was true that ILP owned the highly profitable Irish Life Assurance company which had a book value of some €2bn. and some investment analysts considered that ILP was undervalued, the fact remained that stock markets remained stubbornly unimpressed. ILP could not raise debt funding itself and could only secure funding through ELA from ECB. O'Malley J. found that in March 2011 ILP had to seek increased ELA from the Central Bank. This was forthcoming only on the basis of a guarantee from the Minister in the sum of up to €5bn.

23. A further stark reality was, as O'Malley J. found, that at the end of June 2011 ILP had €17.8 billion of deposits and bonds guaranteed under the ELG scheme and €9.3 billion of deposits guaranteed under the Deposit Guarantee scheme, giving the State a potential exposure of €27.1 billion.

24. By the Autumn of 2010 the State found itself effectively unable to raise funds on international capital markets, save at interest rates which were exorbitant and unsustainable. It accordingly had little option but to enter a Programme for Support ("Bailout") in order to obtain sustainable funding. Funding under the programme came primarily from the International Monetary Fund and two European Union organs - the European Financial Stability Mechanism and the European Financial Stability Facility. It was overseen by the IMF, the European Commission and the European Central Bank ("the Troika", or, more formally, "the External Partners").

25. The programme put in place an €85bn. financing facility to be drawn on as necessary, to meet funding requirements of the State that could no longer be obtained at an affordable cost in the market. The IMF and the EU contributed about €22.5bn each. The State committed €17.5 bn. from the National Pension Reserve Fund. A sum of €3 bn. was contributed by the United Kingdom under a separate bilateral agreement. The Kingdom of Sweden and the Kingdom of Denmark also made separate contributions, totalling about €1 billion, between them. These external funds were not, of course, a gift and would have ultimately to be repaid with interest, although judicial notice may be taken of the fact that subsequent to the hearing in the High Court the IMF loans, together with the loans provided by Swedish and Danish Governments, have since been repaid by the State.

26. The programme was based upon a number of core documents drawn up in December 2010 and also upon Council Regulation (EU) No. 407/2010 of the 11th May 2010 and relevant implementing decisions made thereunder. The documents and implementing decisions were updated and amended from time to time.

27. It was estimated that some €35bn. of this funding would be used for the recapitalisation and restructuring of the banking system, and part of these implementing decisions concerned the proposed recapitalisation of the banks. Much of this detail is reproduced at paragraphs 7.1 *et seq*. of the first judgment of O'Malley J. For present purposes it is, perhaps, sufficient to draw attention to the provisions of paragraphs 11 and 12 of the memorandum of understanding which provided for the stress tests for the banks.

"11. To achieve the above goals, banks will be required to submit deleveraging plans to the national authorities by end-February 2011. The plans will be prepared on the basis of clear periodic targets defined by the Central Bank, taking into account the Prudential Liquidity Assessment Review ("PLAR") to be conducted with the EC, ECB and IMF. By end-March 2011, the Central Bank with assistance from an internationally recognised consulting firm, will complete the assessment of the banks' restructuring plans (structural benchmark). The deleveraging plans will be a component of the restructuring plans to be submitted to the European Commission for approval under EU competition rules.

12. This reorganisation and downsizing of the banks will be bolstered by raising capital standards. While we expect that, in a restructured system, banks will be able to raise capital in the market, we recognise that the higher standards may imply that, in the short run, public provision of capital will be needed for banks that are deemed to be viable. To support this process - and to render it credible - we will undertake a review of the capital needs of banks on the basis of a diagnostic of current asset valuations and

stringent stress tests (PCAR 2011)."

28. The obligations regarding the stress tests envisaged that these would be conducted by internationally recognised consulting firms. The diagnostic evaluation of bank assets and the PCAR process were to be completed and published by the end of March 2011. The Council adopted an implementing decision on the 7th December 2010 on the granting of EU financial assistance, conditional on compliance with a number of specific obligations, including general economic policy obligations. Article 5 of the Decision required the State to "adequately recapitalise, rapidly deleverage and thoroughly restructure the banking system as set out in the Memorandum of Understanding."

29. As O'Malley J. pointed out in her first judgment the Central Bank conducted a Prudential Capital Assessment Review ("PCAR") and a Prudential Liquidity Assessment Review ("PLAR") of the Irish banks in the early part of 2011. The results were published as the Financial Measures Programme Report on the 31st March 2011. While these tests were avowedly conservative and designed to cater for "worst cases" scenarios where the State faced further economic disequilibria and economic shocks, the results when published at the end of March 2011, nonetheless made for sobering reading. The PLAR exercise was conducted by BlackRock Solutions, an international financial consultancy firm.

30. In her first judgment O'Malley J. summarised their conclusions thus (at paras. 12.2 and 12.3):

> "12.2 Estimates for losses were assessed both in relation to the lifetime of loans and by reference to classification of loans. For example, BlackRock assessed lifetime losses in relation to residential mortgages at €9.9 bn. in the "base" scenario (assuming the correctness of EU forecasts for the Irish economy) and at €16.9 bn. in the "adverse" or "stress" scenario (assuming, although not forecasting, a further economic contraction). The total residential mortgage exposure across the banks was put at €140.7 bn.
>
> 12.3 The relevant figures for ILP under this heading were €3.026 bn. and €5.209 bn. respectively".

31. Armed, then, with the BlackRock figures, the Central Bank projected three-year losses on residential mortgages at €5.8 billion (base scenario) or €9.5 billion (stress scenario) across the banks, and at €1.624 billion or €2.679 billion respectively for ILP.

32. These tests were also conducted in circumstances where it was clear that new rules on capital adequacy set by the Basel Committee of Banking Supervisors ("Basel III") were due to come into force on a staggered basis between 2013 and 2018. The Central Bank considered it appropriate to ensure that the banks would be in a position to comply with Basel III. The PLAR exercise also disclosed that in order to reduce the ILP's loan to deposit ratio to 122% by the end of 2013, it would be necessary to deleverage its loan book by some €15.6 bn. This would require the bank to sell its UK mortgage book and its commercial mortgage book. The assumption was that this would be done at discounts of 25% and 50% respectively. The deleveraging process was estimated to give rise to losses in the order of €2.2 bn. ILP had core tier 1 capital of 10.6% (approximately €1.7 bn.) at the end of 2010, which, as O'Malley J. found, "was insufficient to absorb these losses."

33. The Central Bank ultimately concluded that ILP would need €4bn. by way of either outside investment or State support. This would, in the view of the Central Bank, allow ILP to cover the losses associated with the deleveraging process and to maintain a core tier 1 capital ratio of 6%, plus a buffer of €0.3bn, in a stress scenario. (In a non-stressed "base scenario" this core tier 1 capital would rise to a figure of some 10.5%).

34. Within some six weeks of the stress tests the European Council had adopted a further implementing decision on the 16th May 2011 requiring the recapitalisation of the Irish domestic banks by the end of July 2011. The European Commission and Ireland then adopted an updated memorandum of understanding on the following day. The memorandum included a stipulation that plans for the recapitalisation of ILP were to be agreed with the company by the end of that month and that a process to effect the sale of Irish Life Assurance was to start immediately. In the case of ILP, a decision of the 30th May 2011 required that €2.9 billion be achieved by the end of July 2011 with the remaining €1.1 billion to be generated by the asset disposal and liability management exercise.

The developments after the publication of the stress tests

35. Immediately after the results of PCAR and PLAR were published, the then Head of Financial Regulation at the Central Bank, Mr Matthew Elderfield, wrote to ILP to the effect that, pursuant to Article 70 of the European Communities (Capital Adequacy of Credit Institutions) Regulations 2006 it was now being required to raise an addition €4bn. in capital.

36. In explaining how the figure was reached, Mr Elderfield stated that the Central Bank had reached the following conclusions:

> "(a) ILP is considered important to the financial system in the State. This is evidenced by its inclusion in financial support schemes under the Credit Institutions (Financial Support) Act 2008.
>
> (b) ILP continues to be dependent on Eurosystem funding and Emergency Liquidity Assistance from the Central Bank. The reliance on central bank funding for such a period is not conducive to the proper and orderly regulation of the banking sector or the stability of the financial system.
>
> (c) The Central Bank has had regard to the terms of the Memorandum of Economic Policies entered into between the Irish authorities, the IMF, and the European Commission in relation to a joint EU-IMF Joint Programme of Support for Ireland in consultation with the European Central Bank and the objective set out in these terms of expeditiously raising capital.
>
> (d) Under section 11(1)(b)(v) of the [the Central Bank Act 1971], a failure by ILP to, *inter alia*, maintain sufficient own funds would form grounds for the revocation of the licence of ILP to conduct banking business in the State. For the purposes of section 6A(2) of the Central Bank Act 1942, the Central Bank is of the opinion that it is necessary for the discharge of the Central Bank's objectives, including without limitation the stability of the financial system overall and the proper and effective regulation of financial service providers and markets, while ensuring that the best interests of consumers of financial services are protected, that ILP hold own funds of an amount and character such that the Central Bank can be satisfied that ILP will maintain sufficient own funds over the period to which the Capital Review related (*i.e.* the period to 31st December, 2013). In reaching this conclusion, the Central Bank is also of the opinion for the purposes of s. 5A(11) of the CBA 1942 that this is consistent with the orderly and proper functioning of financial markets, the prudential supervision of ILP and the public interest and the interest of consumers.
>
> (f) Regulation 70(1) of the European Communities (Capital Adequacy of Credit Institutions) Regulations 2006 (the '2006 Regulations') states as follows: 'The [Central Bank] shall require any credit [institution] that does not meet the

requirements of any law of the State giving effect to the Recast Credit Institutions Directive to take the necessary actions or steps at an early stage to address the situation.'

(g) Without prejudice to the generality of Regulation 70(1), Regulation 70(4) of the 2006 Regulations prescribes circumstances in which the Central Bank shall under Regulation 70(1) oblige a credit institution to hold own funds in excess of the minimum level set out in Regulation 19 of the 2006 Regulations.

(h) On the basis of the Capital Review, the Central Bank is of the opinion that

(i) the requirements in this letter are necessary to provide for ILP to maintain sufficient own funds for the purpose of section 11(1)(b)(v) of the CBA 1971; and,

(ii) the sole application of measures other than the requirements of this letter is unlikely to improve sufficiently and within an appropriate timeframe the level of own funds or the arrangements, processes, mechanisms and strategies the subject of Regulation 70(4) of the 2006 regulations.

(i) The need for the additional capital to be available to absorb expected losses and to provide for a prudent regulatory buffer up to 31st December 2013 means that the additional capital must:

(i) be restricted to the highest quality capital in terms of permanence, flexibility of payments and loss absorbency;

(ii) continue to be capable of being treated as own funds of the highest quality after the end-date for raising such capital; and;

(iii) not be distributed or included within calculations of sums available for distribution without the prior consent in writing of the Central Bank."

37. The letter concluded by notifying ILP that it would be required to submit a statement in writing of the steps that it would take to comply with this direction.

The response of ILP to the PCAR/PLAR exercise

38. It is next necessary to consider the response of ILP to these developments. The first response of ILP to these developments was in a public statement which issued on the following day in which it expressed disappointment that it was not, in effect, permitted to trade its way out of its difficulties. The statement added, however, that, unfortunately, it had become clear "in recent days that given the wider systemic crisis facing Irish banks and the Irish Sovereign, the Group would have to accept a solution designed to reassure international investors that a line has been drawn under the Irish banking crisis."

39. The statement went on to accept that ILP would have a 2013 capital ratio in the order of 33% as measured by the Central Bank's base case scenario. The company accordingly planned to generate capital in the order of €1.7 bn. as follows:

(i) €1.1 bn. from the sale of the life assurance and investment management businesses and a "liability management programme" (also referred to as a "liability management exercise" or "LME") in relation to the bank's subordinated debt (i.e. buying back at a discount debt for cash from the subordinated bondholders);

(ii) €0.4 bn. from contingent debt capital, and c. €243m. from a dividend from Irish Life.

40. This still left the sum of €2.3b. to be raised. ILP envisaged that this sum – or, at least, a good deal of it – would come from the Minister. On the 27th June 2011 the company notified shareholders of an EGM to be held on the 20th July 2011, the primary business of which would be consideration of the proposed State investment. The proposal involved:

(i) the proposed issue to the Minister of up to €3.4 billion in ordinary shares and of €0.4 billion in contingent capital notes;

(ii) the proposed application for whitewash waiver of obligation under rule 9 of the Irish Takeover Rules;

(iii) the proposed renominalisation of all ordinary shares; and

(iv) the proposed delisting of all ordinary shares from the Official List of the Irish Stock Exchange and the Official List of the UK Listing Authority.

The response of the shareholders to the ILP proposals

41. These proposals met with some resistance from ILP shareholders. In April 2011 Mr Skoczylas, the third appellant, wrote on behalf of Scotchstone to the board of directors of ILPGH, calling on it to protect the interests of the shareholders. His fundamental objection to these proposals was that the Irish authorities had imposed artificially high capital requirements on ILP and was now forcing current shareholders to dispose of valuable assets in order to contribute 44% of those requirements. It was, accordingly, preparing to dilute the ownership of the company in a manner that would not recognise the extent of that contribution. Mr. Skoczylas protested that in the event that it where to transpire that the €4bn. was not in fact needed, the Government would then be able to "pocket" most of the €1.7 bn. provided by the shareholders by way of the asset sale.

42. In subsequent correspondence Scotchstone made suggestions as to how the government investment could be made in a way that, in its view, safeguarded the interests of all concerned. It was proposed that the investment should be by way of the issue of class B preference shares, or of common stock with a call option for the company to buy back the shares after a number of years for the original price plus interest. At all times Mr. Skoczylas maintained ILP was solvent and adequately capitalised and that its problem was essentially one of liquidity rather than solvency. Similar correspondence was sent by solicitors on behalf of some shareholders to the chairman of the Board, to the Minister and to other public office holders. It was accepted in that correspondence, as it has been in the course of these proceedings, that the company was obliged by the PCAR/PLAR results to raise the sum of €4 billion and that it was likely that the Government would participate in the recapitalisation. Similar proposals emanated from other shareholders, many of

whom were less than happy with the Board of ILP and its performance leading up this crisis.

The decision of the Irish Takeover Panel

43. Rule 9.1 of the Takeover Rules, made under powers conferred by the Irish Takeover Panel Act 1997 would in normal circumstances have required the Minister, as a person taking control of a company, to make an offer to the existing shareholders to buy their shares at the price being paid by him for his new holding. By letter dated the 23rd June 2011 the chairperson of the Irish Takeover Panel, Mr Denis McDonald S.C., wrote to the Minister's solicitor to convey a conditional waiver of Rule 9.1 in the event of a direction order being made by the High Court under s.9 of the 2010 Act. The waiver was subject to certain conditions, including that no successful application was made to set aside the direction order under s. 11 of the 2010 Act.

44. As O'Malley J. noted in her first judgment, the claim made in respect of the Takeover Panel decision is essentially based on the overall contention that what the Minister did was unlawful, rather than by way of direct challenge to the waiver as such. As a result the appellants say that, assuming the direction order were to be set aside, the Minister would be obliged to make a cash offer to the shareholders.

The State Aid application

45. It is unnecessary for present purposes to deal at any length with the State aid issues, since this is exhaustively dealt with by O'Malley J. at paras. 22.1 *et seq*. of her first judgment, and is not part of the substance of the present appeal. There is, however, one aspect of the State aid issue which merits particular attention.

46. It is, I think, scarcely surprising that the proposed investment by the Minister for Finance was regarded as State aid for the purposes of Article 107 TFEU. The investment was, after all, selective and confined to ILP. The proposed recapitalisation was, moreover, made on terms which no reasonable investor expecting a reasonable return on his or her investment would ever have made, at least in the circumstances which then prevailed in July 2011.

47. Having regard to the evidence relating to the Irish economy, its banks and the position of ILP, the Commission accepted that the recapitalisation was necessary to avoid a serious disturbance in the economy of Ireland. The Commission then applied Article 107(3)(b) TFEU, which permits State aid to be regarded as compatible with the internal market if its purpose is to remedy "a serious disturbance in the economy of a Member State". In accordance with what was termed the Banking Communication previously issued by the Commission on the subject of State aid to banks, the assessment of compatibility with the internal market required consideration of the measure under the headings of "appropriateness", "necessity" and "proportionality". For present purposes it should be specifically noted that the guidance given in the Banking Communication stipulated that:

> "The Member State concerned should in principle receive rights, the value of which correspond to their contribution to the recapitalisation. The issue price of the new shares must be fixed on the basis of a market oriented valuation."

48. It may be worth observing that a key part of the argument of Mr. Skoczylas in particular is that he says that this must be understood as meaning "in accordance with the principles of the market" and that since the actual market price of the shares was the result of a "false market", an equitable price should have been determined. I propose to return to the issue of a "false market" at a later stage in this judgment.

49. In her judgments in the High Court O'Malley J. accepted the evidence advanced by Mr. Moran to the effect that the rule means that the pricing of ordinary shares in the context of a State recapitalisation must be determined by reference to the quoted market price of such shares prior to the investment. Mr. Moran had noted that the recapitalisations of RBS (in December 2008) and of Lloyds (in January 2009) were both based on a 10% discount to the quoted market price prior to investment and were approved by the Commission at that level. Germany had applied a similar discount to its recapitalisation plan in October 2008, again with Commission approval. Mr Moran further calculated that the 10% discount in fact made very little difference to the shareholders. Even without it, they would still have been diluted to less than 1%. An annex to the Commission Communication on State aid to financial institutions, intended as practical guidance, referred furthermore to the difficulties in the conditions which them prevailed during this period of forecasting future cash flows. It said that:

> "The most noticeable factor, therefore, is the quoted market price of ordinary shares. For non-quoted banks, as there is no quoted share price, Member States should come to an appropriate market-based approach, such as full valuation…"

50. This State aid measure was deemed by the Commission to be "appropriate" because the injection of equity capital was "the single most efficient and straightforward measure to shore up one bank's capital", while the contingent capital notes ensured that the additional capital would be injected only if a capital deficiency or a non-viability event occurred. A strong capitalisation of ILP was, moreover, necessary for it to able to "absorb expected and to some extent unexpected losses, engage in the necessary deleveraging process and convince private investors of its long-term viability to restart the flow of private funding towards the Irish banking system." To be considered "necessary", the capital injection had to be of the minimum amount needed to fulfil the objective. On this issue, the Commission's opinion was that this criterion was met because the amount involved stemmed directly from the PCAR/PLAR exercise and was the amount required by the Central Bank.

51. The Commission noted:

> "It is true that the capital will be provided ex ante for the deleveraging plan to cover the losses that will be realised in the period until 31 December 2013, so that ILP might temporarily have capital in excess of its immediate requirements. However the amount of capital needed has been established in the context of the Programme in order to allow ILP to absorb expected and unexpected losses and achieve the deleveraging target of 122.5% loan to deposit ratio as required under the [Troika] Programme. The proposed amount of recapitalisation is then limited to the minimum to meet such requirements." The sale of the Irish Life business and the LME (the liability management exercise concerning the subordinated debt holders) would limit the amount of State aid needed, since the maximum capital contribution would be extracted from the debt holders while the company would contribute to the cost of its own rescue by the sale of part of its activity. The price to be paid per share - €0.063 - was considered to be "very significant", because of the level of dilution of existing shareholders. It was noted to be a discount of 10% to the share price of the 23rd June, 2011, but also that it represented a discount of 85% on the share price of the last day before the publication of the PCAR/PLAR results. It was further noted that the contingent capital notes would be converted into ordinary shares only if the core tier 1 capital ratio of the bank fell below 8.25%, while the minimum regulatory capital requirement was 10.5%. Thus, conversion into equity would occur only if the bank was "in clear financial distress"."

52. As it happens, the Commission noted that it was "very unlikely" that the State would recoup its investment in the medium or long

term, in view of the uncertainty regarding ILP's future profitability and funding issues. Although there would be a 10% per annum payment for the contingent capital instruments, the market for such instruments was unclear. The Commission concluded, however, that:

> "ILP is in a very distressed financial situation and is unable to pay the remuneration required for distressed banks…The recapitalisation measure is a crucial element in the complete overhaul of the entire Irish banking system. ILP is one of the largest financial institutions in Ireland, with a nationwide presence and a large market share of current account holders, depositors and investors. ILP will have to go through an equally far-reaching and in-depth restructuring process…. Consequently, it is justified that a very low remuneration is paid for the measure."

53. The Commission ultimately found the proposed measure to be "proportionate" because of the following features: The shareholders would be diluted to less than 1% - this was "very material" and the burden-sharing with ordinary shareholders was "close to maximum". The maximum burden-sharing would be extracted from the subordinated bondholders through the LME. The restructuring plan to be submitted by ILP would reflect the "massive" aid injected into it, and the lack of appropriate remuneration for that aid. Sufficient "behavioural" measures (to do with corporate governance, remuneration issues etc.) had been adopted to address the distortion of competition caused by the aid during the rescue period.

54. The Commission decision identified "burden-sharing", as a critical feature of permissible State aid, especially in the context of the recapitalisation of credit institutions. It is, of course, a fundamental principle of the State aid rules that there can be no question of the State using this process to improve or even to maintain the position of shareholders in an otherwise failing institution requiring such aid. On the contrary, it is a fundamental principle that the shareholders should bear the initial burden, followed by the subordinated debt holders. The respondents make the point that this is the same as the core principle in Irish company law that creditors come first and shareholders come last, in the event of a failure of a company.

The Extraordinary General Meeting, 20th July 2011

55. The shareholders were notified of an EGM in a letter from the company chairman, Mr. Alan Cook. Having noted the results of the PCAR/PLAR exercises, and the consequential requirement made by the Central Bank that €2.9bn of the total gross capital requirement be achieved by the 31st July 2011. Mr. Cook went on:

> "Of this total gross capital requirement, €0.2 billion will be met from internal group resources. The directors have considered the possibility of raising capital from other sources. Given the ongoing systemic problems in the Irish banking system and the amount required compared to the current market capitalisation of the company, the directors do not believe that other sources of capital are currently available to the group to meet the remaining capital requirement. Moreover, the directors do not believe at the present time, that there is an alternative source to meet the remaining capital requirement other than the liability management exercise, the possible disposal of the Irish Life Group and the State investment."

56. The views of the ILP directors were summarised in the following paragraphs:

> "As expressed in our announcement on 31March 2011, the capital requirements outlined in the FMPR were more than the Directors had considered necessary even in a stressed scenario. As indicated earlier, a significant factor in this difference is that in conducting the PCAR 2011, the Central Bank used a broader framework involving a number of new and additional features (such as deleveraging and buffer capital) and revised methods and assumptions to be used in the calculation of loan losses, which were not part of any of the Central Bank's previous prudential capital assessments. While it is disappointing to have to bring these Proposals to Shareholders, the Board, having taken legal and financial advice and following discussions with the State in relation to the capital requirements of the Group, nonetheless believes them to be in the best interests of the Company and the Shareholders as a whole, given the lack of alternative options available, for the following reasons: The Bank requires the Remaining Capital Requirement of 3.8 billion, of which 2.9 billion is required no later than 31 July 2011, in order to meet the capital levels set by the Central Bank and without this capital would no longer be able to operate its banking business and would have to cease operations. If this were to occur, it is expected that the group would have to be wound up with the loss of any remaining Shareholder value; The Directors do not believe that there is currently an alternative source to meet the Remaining Capital Requirement other than the combination of the Liability Management Exercise, the possible disposal of the Irish Life Group and the State investment on the terms and structure currently being offered… ...should the State Investment not be approved by Shareholders, it is the Director's view that the Remaining Capital Requirement of 3.8 billion would have to met by the Irish State as a result of the Minister using his powers under the Stabilisation Act on terms which may be less favourable to Shareholders than those outlined in this Circular. The other alternative to the State Investment would be full nationalisation, which may result in the loss of any remaining Shareholder value. The Board believes therefore that the State Investment is the only viable alternative for the Company and the Shareholders as a whole in the present circumstances and, given the risk of further value destruction in the event that the proposals are not implemented, recommends that Shareholders vote in favour of the resolutions…"

57. The Board then put certain proposals before the shareholders which, in effect, provided for the disapplication of pre-emption and other rights which the shareholders would ordinarily have enjoyed. ILP also agreed - but, it would seem, only after the threat of legal action - to table four resolutions put forward by shareholders. In summary, these were:

> 1. To revoke the authority of the directors to allot shares in the capital of the company.
>
> 2. To appoint a leading global investment bank and a leading corporate law firm to carry out a review of recapitalisation options and to undertake a comprehensive search for investors.
>
> 3. To instruct the directors to contact the Central Bank, the Minister for Finance, the EU authorities, the IMF and the European Central Bank to ask them to review the planned recapitalisation and extend the deadline for its completion.
>
> 4. To appoint Mr Skoczylas as an additional director.

58. At the EGM the resolutions put forward by the shareholders were passed and the board resolutions were defeated.

59. Immediately in the wake of the EGM Mr. Cook wrote to the Minister to inform him of the result. Having expressed concern about the amount of the capital to be invested and the speed at which these proposed investments were proposed to be made, Mr. Cook relayed the proposal of the Board to the effect that, first, placing price of the shares should be in the range of 30-75 cents; second,

there should be a pre-emption cover claw-back for existing shareholders; third, €1.4 bn. of the capital should be by way of B shares to allow for a targeted buy-back in the event that the losses projected by PCAR 2011 did not materialise and the business thus turned out to be over-capitalised.

60. On the following day Mr. Moran replied on behalf of the Minister. He made four general points. First, the recapitalisation requirement had been imposed by the Central Bank in its capacity as independent regulator and had to be complied with. Second, the timing of the recapitalisation was dictated not only by the Central Bank but also by the EU/IMF and the European Council Implementing Decision, as amended. Third, ILP did not have any viable alternative source of capital investment. Mr. Moran also pointed out that it was not practical to offer a pre-emption element to the State investment, given the low level of shareholder support anticipated by the Board itself for such a proposal.

61. Fourth, so far as the issue price for new shares, Mr. Moran then noted that the issue price for the new shares had been the subject of negotiation between the company and the Minister. The Minister had initially proposed a price of 1 cent per share - this was raised to a 10% discount to market price. On this topic Mr Moran said:

> "The issue price fairly reflects the circumstances and nature of IL&P and of the State's investment. There was never any reality to an issue price of 30 to 75 cents as suggested in your letter of yesterday, particularly given the market price at which IL&P's shares were trading at the relevant time. This range was a multiple of the market price at the time (and remains even more so now)."

62. So far as the Class B shares proposal was concerned, Mr. Moran stated:

> "It would not be prudent for the State to agree to a capped upside in respect of its capital injection into IL&P by way of the use of B shares as suggested in your letter of yesterday, in circumstances where it is the State (and by consequence, the taxpayer) that is undertaking the greatest risk in the recapitalisation of IL&P to meet the requirements of the Central Bank, as Regulator, and of the External Partners."

63. Mr. Moran then stated that the Board had in its circular recommended the terms of the proposed State investment to shareholders. He pointed out that there was no option but to proceed with the recapitalisation by the 31st July 2011. Mr. Cook acknowledged that upon receipt of that letter it was obvious that ILP was in an extremely serious situation, as it was in "serious breach" of its liquidity ratios. He considered that the EGM resolution regarding a search for private investors was not a realistic proposal, because no private investor willing to invest the necessary capital had yet been found. There were, after all, only six days left to comply with the re-capitalisation requirements.

64. The shareholders - including Mr. Skocyzlas - were still unhappy. They maintained that the PCLR/PLAR exercise had imposed artificially high capital requirements and led to ILP being over-capitalised. They also contended that the proposal involved a contribution on their part of between €1.3 bn. and €1.7 bn. (because of the proposed sale of Irish Life), representing 33% to 44% of the proposed €4bn. capital requirement. They argued that they were therefore entitled to hold a stake of that order after the State investment.

65. The response to this argument was that this implied a market capitalisation of €3.6 to €4 billion after the contribution of €2.3 billion by the State. The market value of ILP Group Holdings as of the 28th February 2011 was, however, only about €271m. The company also denied that the shareholders of ILPGH could be said to be contributing €1.7 bn. in capital, since they were not the owners of Irish Life. That company was owned by ILP and not by the shareholders of ILP Group Holdings. Their claim would, it was argued, deliver to the ILPGH shareholders unwarranted windfall gains at the expense of the taxpayer or of any new investor.

66. The proposed direction order was signed by the Minister on the 25th July 2011 and it contained the following recitals in paragraph 2:

> "This Proposed direction order is made because, having consulted the Governor of the Central Bank of Ireland, I am of the opinion that a direction order in the terms of this Proposed direction order is necessary to secure the achievement of a purpose or purposes of the Act, namely:
>
> > 2.1 to address the serious and continuing disruption to the economy and the financial system and the continuing threat to the stability of certain credit institutions in the State and the financial system generally (Section 4(a) of the Act);
> >
> > 2.2 to implement the reorganisation of ILP, a credit institution in the State, to achieve the financial stabilisation of ILP and its restructuring (consistent with the State aid rules of the European Union) in the context of the National Recovery Plan 2011-2014 and the European Union/International Monetary Fund Programme of Financial Support for Ireland (Section 4(b) of the Act);
> >
> > 2.3 to protect the interests of depositors in credit institutions (Section 4(e) of the Act);
> >
> > 2.4 to address the compelling need:
> >
> > > (a) to facilitate the availability of credit in the economy of the State;
> > >
> > > (b) to protect the State's interests in respect of the guarantees given by the Government under the Act and to support the steps taken by the Government in that regard;
> > >
> > > (c) to protect the interests of taxpayers;
> > >
> > > (d) to restore confidence in the banking sector and to underpin Government support measures in relation to that sector; and
> > >
> > > (e) to align the activities of the relevant institutions and the duties and responsibilities of their officers and employees with the public interests and the other purposes of the Act (Section 4(f) of the Act); to preserve and restore the financial position of ILP and ILPGH (Section 4(g) of the Act); and to empower the Court to impose reorganisation measures on ILP through orders made in reliance on Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 (the "CIWUD Directive")

(Section 4(h) of the Act)."

67. Paragraph 3 stated that the intention of the proposed direction order was "the preservation or restoration of the financial position of ILP". Paragraph 7 described the purposes of paragraphs 8.1, 8.2, 8.3(a), 8.3(b), 8.9 and 9 of the proposed direction order as being "to ensure the immediate and effective issuance of additional share capital in ILPGH by issuing shares to the Minister:

(a) to prevent or remedy an imminent breach of the regulatory capital requirements applicable to ILP; and/or

(b) to enable ILP immediately to meet its regulatory capital targets set by the Central Bank of Ireland…; and/or to address an imminent threat to the financial stability of ILPGH and ILP; and/or to address an imminent threat to the stability of the financial system in the State."

68. Section 7 of the 2010 Act imposed extensive consultation obligations on the Minister with the Central Bank with regard to the proposed directions order. It is, I think, unnecessary for the present purposes to examine compliance with these conditions, since it is abundantly clear that the Central Bank fully recognised the need to effect an immediate recapitalisation of ILP by the July 31st deadline. Further details of this correspondence are, in any event, set out at paras. 28.1 *et seq.* of the first judgment of O'Malley J.

69. The application for a direction order was grounded upon an affidavit sworn by Mr. Moran who at the time was the Second Secretary in the banking divisions of the Department of Finance. In that affidavit the purpose of the application was stated to be the recapitalisation of ILP by the 31st July 2011 as required by:

(i) the Central Bank of Ireland;

(ii) the Commission of the European Union and the International Monetary Fund, in consultation with the European Central Bank; and

(iii) the Council of the European Union.

It was stated that the capital required by ILP amounted to €4 bn., of which €2.9 bn. had to be generated by the 31st July. The State was obliged to ensure that the recapitalisation was carried out and had agreed to subscribe €2.7 bn. for certain securities in the ILPGH Group. It should be noted that provision was also being made for a "Standby" State investment of up to €1.1 billion, in the event that the proposed asset sales were not successful. This was ultimately used when the Minister purchased Irish Life for €1.3bn. in 2012. This came about after the failure of a private sale process.

70. Mr. Moran's affidavit also recited the events which had led up to the July 2011 EGM and its aftermath. He also explained the extent of ILP's liabilities and the fact that standard debt markets were closed to it. It was also heavily dependent on the Credit Institutions (Eligible Liabilities Guarantee) Scheme, which had been established by the Minister in 2009 and without such participation it would have been unable to maintain its retail and corporate deposits above the threshold of the deposit protection scheme operated in accordance with domestic and EU statutory requirements relating to the Deposit Guarantee Scheme. It was, in addition, hugely dependent on the Eurosystem and the provision of ELA through the ECB.

71. Mr. Moran further maintained that ILP's funding position was more precarious than most other credit institutions because it had a loan to deposit ratio significantly higher than the others. Mr Moran also stated that the Minister would have preferred to see the required capital raised from private sources rather than by the application of public funds, in order to reduce the overall cost to the taxpayer. The Minister, however, had been advised by the National Treasury Management Agency, that private capital was currently unavailable to ILP and that parties other than the State would not invest in it. This was for

"…..a wide variety of reasons including fundamental issues arising in the ILP business model, including:

(i) a large tracker mortgage book and excessively high loan to deposit ratio,

(ii) over-reliance on ECB and ELA funding,

(iii) the high quantum of capital required, and

(iv) the continued uncertainty surrounding a recovery of the Irish economy."

72. The undeniable fact, therefore, was that as O'Malley J. found, there was no credible private investor available to invest in ILP in July 2011. (I will describe these efforts at a later point in this judgment).

73. So far as the pricing of the equity investment at a discount of 10% of the market price, Mr. Moran said that the advice given by Goldman Sachs was that for all placements over €50m. since 2007, where more than 20% of the equity was sold, the average discount was 9.6%. The European Commission had approved a 10% discount and ILPGH had agreed to a placing at that price.

74. So far as the necessity for the direction order was concerned, Mr. Moran addressed the possible consequences if the order sought was not granted. It was plain that these would be potentially catastrophic for ILP, for the banking system as a whole and, indeed, for the State. As far as ILP was concerned, breach of the recapitalisation deadline would create unacceptable uncertainty as to its future. This would have an adverse effect on its business and on its reputation for solvency, potentially leading to a run on deposits such as had happened in the case of the UK bank, Northern Rock, in September 2007. Such a run would ultimately result in ILP having to cease trading and being would up as insolvent.

75. Nor could one avoid observing that even if this scenario did not come about, the bank would not be able to secure funding. ILP was already drawing down substantial amounts of ELA funding, collateralised in part by the ELG scheme. If it breached its regulatory requirements it would not be able to access debt markets, since it could not give the necessary undertakings relating to those requirements. The Central Bank might not, in its discretion, provide further ELA funds. Failure to comply with a requirement imposed by the Central Bank, which that body considered to be essential, could lead to sanctions including suspension of the business or revocation of the banking licence. On this point, Mr Moran observed that:

"From both a regulatory and reputational perspective, it would be regarded as inconceivable that the Irish authorities would allow ILP to operate in continuing breach of its regulatory capital requirements."

76. The State was furthermore legally obliged to recapitalise ILP on foot of the Programme for Support and the Implementing Decisions. If it failed to do so it could be subject to a range of sanctions, including the withholding of instalments or the withdrawal of funding altogether. There would also be the risk of imposition of penalties pursuant to Article 260 TFEU.

Alternative means of raising capital

77. It is next necessary to rehearse briefly the efforts made to secure alternative investors in ILP to raise capital in this way. Much of this material is covered at length at paragraphs 32 et seq. of the first judgment of O'Malley J. and it is, perhaps, unnecessary to record it in great detail here. The fact is, as Mr. Cook, set out in his affidavit, all attempts to raise €4bn. – or, for that matter, any additional money – from private debt markets foundered.

78. The ILP management team had kept open contacts with a variety of institutional investors with a view to securing an investment in the company. To this end they retained both Davys and Deutsche Bank to advise on this. Deutsche advised that expecting any third party investment in these circumstances was quite unrealistic.

79. The reasons specific to ILP were as follows: First, it was relying on State guarantees for up to 40% of its funding. No dividend could be paid while its liabilities were guaranteed by the State. (This was a condition of the State support.) Second, 65% of its mortgages in Ireland and 98% of its mortgages in the UK were loss-making trackers. Third, the €4 bn. would be applied, not to expand the business of the bank but to cover its losses. Fourth, the company was the only Irish bank whose future was not clear after the PCAR/PLAR results (i.e., it was not designated as a "pillar bank" and was not merged with another bank).

80. It is perhaps also worth noting that, as Mr. Cook observed in his affidavit, at no stage has Mr Skoczylas, or, indeed, any of the applicants, identified any investor who would have prepared to make a" meaningful" contribution, which he (Mr. Cook) considered would have to have been in the order of 5% of the €2.7bn required (about €135m).

81. Mr. Moran put the matter even more starkly. He acknowledged that it would in fact have been the preferred option of the Minister if ILP could have met the recapitalisation requirements by raising private capital itself. Unlike, however, the position with regard to the Bank of Ireland there were no private investors available to invest in ILP in July 2011 and it had no realistic prospect of gaining access to international capital markets within the time frame required. His bleak assessment was that:

> "….. the most obvious practical problem in terms of investing in ILP in 2011 is that it was almost certainly guaranteed to lose money. It is difficult to comprehend how an investor, who requires a commercial return, would have invested any amount (still less €2.7 billion) in a company where losses on that investment were virtually assured. The overarching reality, as it has in fact turned out to be the case, was that an investment in ILP at any price sufficient to meet regulatory capital requirements would have lost money."

82. There was still the issue of the pre-emption rights of shareholders. While I propose to address this point presently, it is important to recall that a key part of the respondents' submission was that this was in the circumstances a quite unrealistic option. In her first judgment O'Malley J. found (at para. 32.24 *et seq.*):

"In the period between the announcement of the 2011 PCAR/PLAR results and the 23rd June, 2011 the market price of ILP shares averaged at 0.1193 per share, suggesting a market value of the existing equity of €33 million. However, in the month prior to the 23rd June 2011 the average market price of a share was 0.0864, equivalent to a market value of the equity in the company of €23.9 million. …..In these circumstances, the opinion of the Minister's deponents is that it would not have been conceivable that shareholders would have been willing, in sufficient numbers or with sufficient resources, to invest 2.3 billion in the company. This would have required, on average, a contribution from each shareholder of approximately 120 times the value of his or her investment. On this basis, according to Mr Moran, the applicants would have been required to invest €5.7 million between them, with €4.3 million coming from Scotchstone. This would have been 42.9 times the net assets of Scotchstone as set out in its audited accounts."

83. The judge further noted that in July 2011 there were approximately 135,000 shareholders in total. Based on the June 23rd figures, 134,000 of them had a shareholding worth less than €500, with the average value being €32. To take up their full rights in a pre-emptive offer would have cost an average of €3,812 per person.

The "false market" issue

84. It is next necessary to address the question of the alleged false market in ILP shares. A critical part of the appellant's case - which O'Malley J. rejected - was that the Minister had created a false market in ILP shares in the months leading up to July 2011 such that the share price was artificially depressed, thus affecting the value of the shareholding.

85. The term "false market" was described by one of the appellant's expert witnesses, Professor Azarmi, as "unusual, sudden, significant moves in the share price, which are not caused by inherent changes in the business or in the market, but by external rumours or announcements." While Professor Azarmi accepted that the ILP share price had declined in line with other Irish banks and financial stocks, there were, he suggested, unusual significant movements in the share price at the end of March 2011 and the beginning of April 2011.

86. These movements can be summarised as follows. First, on the 28th March, 2011 the share price was stable during the day's trading at about 74 cents. Second, on the 29th March rumours started circulating about a possible takeover by the State and dilution of the shareholding. The share price closed that day at 40.5 cents. Third, on the 30th March the share price was suspended on the stock exchange until the 1st April. Fourth, on the 31st March 2011 the €4 bn. capital raising requirement was imposed. The Minister made a statement referring to the likelihood that the Government would acquire a majority stake. Finally, on the 1st April 2011 trading was reopened and the price dropped to 11 cents, before recovering to 16.7 at the close.

87. Professor Azami contended that the dramatic collapse in the share price was caused by the rumours and the Minister's announcement, and not by any inherent changes in the business or the market over these few days. The capital requirement was not, he said, an inherent change in the business but rather by reason of what he described as "a unique imposition of a drastically new business paradigm".

88. The Minister responded by saying that the market could not be described as false if it was based on clear, verified information such as that disclosed to shareholders. The EGM circular gave to the shareholders relevant and accurate information as to the rationale for the proposed investment by the Minister and the risks to shareholders if the EGM resolutions were not approved. Mr. Moran pointed out on behalf of the Minister that the company was obliged both by legislation and by the rules of the Irish and London Stock Exchanges to disclose price sensitive information to the shareholders. When such information is disclosed, the market typically reacts by adjusting the price.

89. If there were sudden price movements during the period from the end of March 2011 through into early April 2011 this is probably not unconnected with the fact that – as the respondents' witness were in turn all anxious to stress – it became clear after the BlackRock stress tests were published at the end of March that a further €4bn. was needed to ensure that the Bank met appropriate capitalisation requirements and that this would also involve the sale of the company's profitable Irish Life entity. This must all have come as quite a disappointment to the shareholders who, based on ILP's prior public statements on this issue, would presumably have been holding out for better news. But as various witnesses for the respondents stated, this could not be regarded as a false market.

The relative contributions of the Minister and the shareholders
90. Mr Skoczylas has maintained - both in the High Court and on appeal - that the shareholders must be seen as having contributed 36% of the required capital, but they were left with only 0.8% of the shareholding. Putting it another way, he says that the Minister provided five times the amount of capital and got 130 times the existing number of shares. It has been suggested that the recapitalisation could have been achieved in a fairer way. The method suggested by Mr Skoczylas in the course of the hearing in the High Court was a split of the shares such that the existing shareholders would have got 7% and the Minister 93% of the equity.

91. Mr Moran said that the applicants' calculation "defies common sense". He pointed out that if it were correct, and that 36% of the equity should be apportioned to the shareholders, the Minister would have been at an immediate loss of €816m. (35% of the State investment) upon making the investment. This figure comes from the fact that on the 23rd June 2011 (the day by reference to which the Minister's price was fixed) the shares were worth 7 cents each and the market capitalisation was €19m. The Minister's contribution of €2.3 bn. would bring this to €2.319 bn. 64% of that sum would be €1.484 bn.

92. In the alternative, if 64% of the equity was worth €2.3 bn. after the State investment, then the shareholders' hypothetical 36% would have to have been worth €1.3 bn. The last time ILPGH had been worth €1.3 bn. was in November 2009. To attribute the sum of €1.3 billion to the shareholders would be to imply a share price 67 times the price on the 23rd June 2011.

93. The respondents also submit that the value put on the Minister's holding by the applicants ignored the reality that the company continued to lose money and its capital has been eroded accordingly. The total provision for credit losses, as of mid-2013 was €3.6 billion, which exceeded the (conservative) Financial, Management and Policy Review ("FMPR") (*i.e.*, in effect the stress test exercise) estimate of €3.4 billion by the end of 2013. It was suggested that based on the information currently available, it was expected that the Minister would never recover a significant proportion of his investment in ILP.

94. It should perhaps also be noted that for European accounting ("EUROSTAT") purposes, €800m. of the €2.3 billion was immediately written off and added to the Government's debt. The concept of the share-splitting exercise was not accepted by the respondents, as they maintain that in the circumstances that would be to give the shareholders a gift. The calculation made by the Minister as to the number of shares to be allotted to him was based on the amount of money that had to be put into the company and the price to be paid (taking into account the discount). The shareholders ended up with the same number of shares that they had before the intervention, although, obviously, not the same percentage of the company.

95. Mr. Cook also agreed that none of the new capital was contributed by the shareholders. He says that the €1.1 bn. from the sale of Irish Life was the result of the bank (not ILPGH and not the shareholders of ILPGH) converting an asset (shares in Irish Life) into another asset (cash). The LME was an exercise in reducing the bank's debt to subordinated bond and note holders - the latter suffered losses of up to €1bn. The contingent capital was coming from the Minister. The €243m. was a dividend from the bank's subsidiary.

The failure to recapitalise the bank by the July 31st deadline
96. All of the respondents' witness were emphatic that the failure to effect the recapitalisation of the Bank by July 31st would, in all probability, have been disastrous. Again, it is not necessary to dwell on this in view of the clear findings of fact made by O'Malley J. to which I will shortly come. It is perhaps sufficient to mention briefly the evidence of Mr. Cook and that of Professor Phillip Lane, the then Whately Professor of Political Economy at Trinity College, Dublin. Professor Lane is now, of course, the current Governor of the Central Bank.

97. Mr. Cook's evidence was blunt: he stated that if the recapitalisation deadline imposed by the Central Bank had not been met, the bank would have failed. This was because the bank would have been obliged to announce to the market the fact that it had not met the deadline. The resulting loss of confidence on the part of depositors would in turn have caused a run on the bank and its immediate forced liquidation. As a separate problem, its licence could have been revoked, suspended or cancelled. This would, *inter alia*, have constituted an event of default in relation to €9bn. worth of notes issued by the bank. The trustee for the note holders would then have been likely to call for repayment, which would not have been possible.

98. Mr. Cook calculated that the liquidation of the bank would have left the State exposed to €13.08bn. in relation to guaranteed retail deposits, €2.8 bn. corporate deposits covered by the ELG, €8.13bn. for noteholders covered by the ELG and €2.11bn. to the Central Bank in respect of the ELA guaranteed by the Minister in March 2011. This total figure would have come to €26.12 bn.

99. Professor Lane's evidence was simply that in the spring and summer of 2011, various factors were intensifying the euro crisis. The Greek programme was proving inadequate and that member state required further assistance. The markets had lost confidence in Portugal, which had also negotiated a programme in May 2011. There were increasing concerns about Spain and Italy. In these circumstances it was imperative for financial stability in the euro area and the European Union as a whole that Ireland should successfully adhere to the timeline set down for the recapitalisation of its banks. A failure to implement the plan could have thrown into doubt the commitment of the Irish government in relation to the banks, thereby potentially causing difficulties with bank funders in other States. The fulfilment by Ireland of its Treaty obligations would have been called into question.

100. All of this evidence was exhaustively examined and considered by O'Malley J. in her first (and, indeed, the second) judgment. Her critical findings are summarised at para. 41.2 of the first judgment:

> "(i) From 2008 onwards, ILP along with other Irish banks became increasingly reliant upon State and EU financial support. As time went by and the financial turmoil of those years did not resolve, the efforts of the Irish Government to support the banks did not succeed in convincing the markets of either the banks' viability or the State's capacity to continue supporting them.
>
> (ii) By late 2010 it was apparent that there was a serious threat to the financial stability of the State, in significant part due to the State's commitments to the banks.
>
> (iii) The State's guarantees in respect of ILP amounted to €26 billion.

(iv) In entering in to the Programme for Support in November 2010, the Irish State entered into binding legal commitments to the European Commission, the European Central Bank and the International Monetary Fund, including a commitment to recapitalise viable Irish banks.

(v) As part of the Programme, the Central Bank committed itself to carry out a Prudential Capital Assessment Review (PCAR) and a Prudential Liquidity Assessment Review (PLAR) and to determine the capital needs of the banks on the basis of the results.

(vi) The PCAR and PLAR results were published on 31st March 2011.

(vii) The State was legally committed to ensure recapitalisation in line with the reviews by the 31st July 2011.

(viii) The Governor of the Central Bank then directed ILP to raise regulatory capital in the sum of €4 billion. This direction was binding on ILP and was not the subject of any legal challenge. The direction was made by the Central Bank in its capacity as independent regulator.

(ix) On the balance of probabilities, the required capital could not have been raised from private investors.

(x) On the balance of probabilities, the required capital could not have been raised from existing shareholders.

(xi) On the balance of probabilities, failure to recapitalise by the deadline would have led to a failure of the Bank, whether by reason of a run on the Bank by depositors, revocation of its licence, a call for repayment of the various Notes, a cessation of funding under the ELA scheme or a combination of some or all of these possibilities.

(xii) The failure of ILP would, as a matter of probability, have resulted in a complete loss of value to the shareholders.

(xiii) The failure of ILP would, as a matter of probability, have had extreme, adverse consequences for the Irish State, whether by reason of a run on the Bank and subsequent calls on the State guarantee of up to c. €26 billion, the contagion effects in relation to the other banks, a full or partial withdrawal of funding to the State under the Programme for Support for non-compliance with its terms, sanctions imposed under the Treaty, or a combination of some or all of these possibilities.

(xiv) The adverse consequences for the State would, as a matter of probability, have worsened the threat to the financial stability of other Member States and of the European Union.

(xv) The decisions by the State to invest in the recapitalisation was made in fulfilment of its legal obligations and in the interests of the State's financial system, the citizens of the State and the citizens of the European Union.

(xvi) The State decided to recapitalise ILP by way of a subscription by the Minister for Finance for ordinary shares in the sum of €2.3 billion, contingent capital in the sum of €0.4 billion, and a "stand by" investment of €1.1 billion. The price to be paid per share was €0.06345, a discount of 10% to the middle market price on 23rd June, 2011. The calculation of the number of shares required to be issued in return for the €2.3 billion resulted in the acquisition by the Minister of 99.2% of the company.

(xvii) The share price on that date was not the result of a false market, as argued by the Applicants. The share price had been falling in any event over the previous number of years, and fell dramatically on publication of the PLAR/ PCAR results. As a matter of probability, this was because the market doubted the ability of the Bank to achieve the required recapitalisation in a way that would be attractive to investors.

(xviii) Part of the plan for the recapitalisation of the Bank involved the sale of its asset Irish Life. The applicants argued that the sale of Irish Life constituted an expropriation of the shareholders of ILPGH. However, this asset belonged to ILP, and not to the shareholders of ILPGH. Its value could not, accordingly, be attributed to those shareholders any more than the liabilities of ILP could have been attributed to them.

(xix) To attribute the value of Irish Life to the shareholders would be to make an unlawful return of capital to the shareholders.

(xx) The paid in share capital of the company was not counted as part of the recapitalisation and has not been taken out of the company by the Minister.

(xxi) A Liability Management Exercise resulted in a significant loss to the subordinated debt holders and contributed significantly to the recapitalisation.

(xxii) The European Commission gave approval under State Aid rules for the recapitalisation of ILP by means of the State investment in the same manner, at the same price and to the same extent as that ultimately carried out on foot of the direction order made by the High Court.

(xxiii) The Irish Takeover Panel granted a waiver of Rule 9 for the purposes of the State investment on the basis of the same proposal. This did not involve any breach of the Takeover Directive.

(xxiv) The Minister's proposal was supported, albeit reluctantly, by the Board of ILP. The Board considered that the Company had no other option available to it in terms of achieving the required recapitalisation. An EGM was called with a view to passing the necessary resolutions.

(xxv) The State's proposal was not accepted by the shareholders voting at the EGM on 20th July, 2011, who wished to explore other potential avenues for the raising of the required capital. The Board was instructed to seek an extension of time for the recapitalisation.

(xxvi) Neither the Minister nor the Governor of the Central Bank was minded to seek such an extension. Having regard to the source of the deadline, an extension would have required the consent of the External Partners and the members of the European Council. (xxvii) The Minister decided to make a Proposed direction order pursuant to the provisions of the

Act.

(xxviii) The Minister informed the Governor of the Central Bank of his intentions and complied with the procedural requirements of the Act in so doing.

(xxix) He informed the Board of ILP of his intentions and complied with the procedural requirements of the Act in so doing.

(xxx) The Governor of the Central Bank communicated his views, which were supportive of the Proposed direction order as being likely to achieve the statutory purposes of the Act.

(xxxi) The chairman of the Board of the Company referred the Minister to the letter he had written after the EGM, outlining the views of the dissenting shareholders.

(xxxii) The application for a direction order was made and granted by the High Court, in accordance with the procedure prescribed by the Act, on 26th July 2011.

(xxxiii) There was no want of candour and no breach of duty to the Court on the part of the Minister or his legal representative in the making of the application.

(xxxiv) One result of the direction order was (as it would have been under the proposal put to the EGM) that the Minister obtained 99.2% of the issued shares of ILPGH. It was therefore necessary to remove the Company's shares from the official lists in Ireland and the United Kingdom. This did not involve any breach of the MiFID Directive.

(xxxv) The Act permits the action taken by the Minister. The docannot be set aside or varied unless the Court finds that his opinion that it was necessary was unreasonable or vitiated by legal error."

The *bona fides* of the appellants
101. Contrary to what was at least hinted at in some of the submissions to this Court, I am perfectly satisfied that the appellants would appear at all times to have acted *bona fide* in defence of their legitimate interests as shareholders. The 2010 Act was, after all, a novel item of legislation which had potentially far-reaching effects. The issues raised arose out of what amounted to a compulsory takeover of a failing bank, albeit a step which, it is not disputed, was one which was entirely necessitated in the public interest.

102. For my part, I do not propose to look behind the circumstances in which each of the appellants acquired their shareholding. Even if the appellants bought into the company at a time when the value of the shares had fallen dramatically, that was their affair. They may have seen value where others did not. In a market economy such as ours, this was a choice which they were perfectly entitled to take. Once, however, they became shareholders they had acquired a bundle of intangible legal rights which were governed in part by the Companies Act 1963 (as it then was) and in part by the provisions of EU law. These property rights qua shareholders are also in principle protected by the provisions of Article 40.3.2 of the Constitution: see, *e.g., Iarnród Éireann v. Ireland* [1996] 3 IR 321. The principal question which is now before the Court can, in essence, be reduced to a consideration of the question of whether these rights were infringed by the provisions of the direction order.

Whether the case is governed by EU law or by national law?
103. During the course of the hearing there was much debate as to whether the present case was governed by EU law or by national law or, perhaps, by a mixture of both. There are certainly aspects of the case that are clearly governed by EU law. Thus, for example, the question of whether the direction order infringed the terms of the Second Company Law Directive (Directive 79/91 EEC) was certainly an issue of EU law which was ultimately determined by the Court of Justice. Contrary, moreover, to the submissions of the applicants, there was equally an obligation imposed by EU law to recapitalise ILP by the 31st July 2011: see Article 1(g) of Council Decision 2011/326/EU (as amended).

104. At the same time EU law, broadly speaking, deferred to national law as to the manner in which the recapitalisation was to be achieved. The 2010 Act was an autochthonous item of legislation enacted by the Oireachtas. Since, moreover, the appellants' main complaints centred on the manner in which the recapitalisation was effected by the provisions of the 2010 Act and the direction order, I consider that the issues which fall to be determined on this appeal are substantially governed by domestic law.

105. As it happens, nothing really greatly turns on whether domestic or EU law provides governs this aspect of the application because the essential challenge in this case is to the proportionality of the direction order and the manner in which the recapitalisation of ILP was carried out. As I hope to show, the scope of review of administrative action on proportionality grounds is essentially no different irrespective of whether the matter is governed by Irish or by EU law. But, as I will also explain below, this Court is bound by the judgment of the Court of Justice in the Art. 267 reference made by O'Malley J.

The economic conditions which prevailed in 2011
106. Few adults who lived through the worst years of the crisis from September 2008 onwards need to be reminded of the litany of turbulent events which unfolded during those grim years. These included the collapse of Lehman Brothers and the bank guarantee (September 2008), the nationalisation of Anglo in January 2009, the ever growing costs associated with the bank bailout, the sovereign bail-out in November 2010, the results of the PCAR and PLAR bank stress tests in March 2011 and the recapitalisation of the banks by the end of July 2011. These events are, in any event, recounted in detail in the affidavit sworn by Mr. Moran.

107. Despite the fact that we now live in happier economic times, the legacy of these events continues to leave a long shadow. I can take judicial notice of this fact, not least given that summary judgment appeals in relation to pre-crisis loans continue to form a staple diet of this Court's work. This puts into perspective a key submission of Mr. Skoczylas to the effect that the crisis – at least so far as it concerned ILP – was really a liquidity crisis rather than a solvency crisis. A key part of Mr. Skoczylas' objections to what was proposed was that the Minister's actions amounted to an over-capitalisation of the bank and that ILP was insolvent "only if the Irish authorities created an artificial state of insolvency based on the artificially high capital requirements that are very different to real capital needs": see the letter to the various defendants sent by Scotchstone Capital on the 17th July 2011. He further maintained that the PCAR/PLAR stress tests were "grossly unrealistic" and "exaggeratedly conservative."

108. There have certainly been instances in economic history where temporary liquidity crises have threatened economic stability. But hindsight has certainly shown that the events of 2008-2011 involved no short term liquidity crisis, but rather a deep and prolonged recession caused in significant part by the fundamental insolvency of the banking sector, both in Ireland and, for that matter,

elsewhere. While it is true that ILP was not exposed to the property development sector, it was nonetheless heavily hit by the fact that many of its mortgages were residential tracker mortgages which proved loss making when interest rates were reduced to their present ultra-low levels.

109. Indeed, further stress tests published under the supervision of the European Banking Authority on the 26th October 2014 showed that while ILP had sufficient shock absorption capacity by reference to these tests, it nonetheless had a €855m. shortfall "under the adverse scenario." The fact that following formal approval by the Commission of the re-structuring plan on 9 April 2015 as compatible with State aid rules (C (2015) 2353 final), ILP was required to raise this additional capital is again a strong indication that this was not simply a liquidity issue or such that it can be said that the capital injection of July 2011 was in some sense an over-reaction to the plight of ILP at the time.

110. It is important to recall, however, that the crisis was in no sense confined to Ireland and that by July 2011 the very survival of the Euro as a currency was under real threat. This was, in essence, the evidence given by Professor Lane in the High Court. This can, in any event, be illustrated by any number of publicly known economic metrics, of which the following examples must suffice. Thus, for example, sovereign bond yields for peripheral countries such as Ireland and Greece were at unsustainably high levels while at the same time Swiss and German short term bond yields were either at or were about to turn negative. Within a space of three years since the onset of the crisis in 2008 the Euro had lost more than a third of its value against benchmark safe haven currencies such as the Swiss Franc.

111. All of these events served to re-inforce the urgency of this crisis and, specifically, so far as Ireland was concerned, the need to take action in respect of ILP. There was, as I have already noted, an obligation under EU law by virtue of the Council Decisions to achieve a recapitalisation of ILP (and, for that matter, the other Irish banks) by the end of July 2011. ILP was thus facing a bank run or insolvency if it was not recapitalised by the end of July 2011. As O'Malley J. succinctly put it in the findings of fact contained in her August 2014 judgment:

> "11. On the balance of probabilities, failure to recapitalise by the deadline would have led to a failure of the bank, whether by reason of a run on the bank by depositors, revocation of its licence, a call for repayment of the various Notes, a cessation of funding under the ELA scheme or a combination of some or all of these possibilities.
>
> 12. The failure of ILP would, as a matter of probability, have resulted in a complete loss of value to the shareholders.
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> 13. The failure of ILP would, as a matter of probability, have had extreme, adverse consequences for the Irish State, whether by reason of a run on the bank and subsequent calls on the State guarantee of up to c. €26 billion, the contagion effects in relation to the other banks, a full or partial withdrawal of funding to the State under the Programme of Support for non-compliance with its terms, sanctions imposed under the Treaty, or a combination of some or all of these possibilities."

112. If ILP failed, the contagion effect on the other Irish banks (all of whom were in a fragile position) and the Irish sovereign would in all probability have been very significant. Just as importantly, the failure of ILP would also have sent shockwaves throughout the European banking sector, with stark implications for banks in other EU Member States, many of whom were also in a parlous and distressed state. Such a failure might even, perhaps, have been imperilled the overall stability of European and Monetary Union itself. The extent, therefore, of the crisis and the nature of the emergency cannot possibly be over-stated.

113. Even, however, in an economic emergency the law is not silent, although under such conditions her voice is, admittedly, at times slightly quieter - even fainter - than is usually the case. In a democratic state based on the rule of law, that voice must nonetheless be sufficiently courageous and powerful to insist on adherence to basic constitutional norms such as due process and the protection of the substance of constitutional rights even if some accommodation for the exigencies of the situation is also understandable and necessary.

114. If it were otherwise, then, as Hardiman J. observed in *Dellway International Ltd. v. NAMA* [2011] IESC 13, [2011] 4 I.R. 1, 289, "the cry of 'emergency' would be sufficient to set all rights aside at the whim of the executive." Hardiman J. continued:

> "Our Constitution makes specific provision for 'war or rebellion'. It is not for the courts to extend these provisions to a situation which is not one of war or armed rebellion. That would require a decision of the people in a referendum, if they thought it necessary or prudent to confer such unreviewable powers on the State. The cry of 'emergency' is an intoxicating one, producing an exhilarating freedom from the need to consider the rights of others and productive of a desire to repeat it again and again."

115. In my view, therefore, the proper approach to the 2010 Act was summed up perfectly by Cooke J. in *Aurelius Capital Master v. Minister for Finance* [2011] IEHC 267 when he said:

> "The measures are justified by the necessity in the public interest of preserving from collapse the banking system and thence the financial and economic stability of the State. That is the rationale and purpose of and justification for the Act. It follows …that the provisions of the Act must, so far as concerned interference with contractual and property rights of members of the public, be construed strictly and applied conservatively while at the same time ensuring that the competence given to this Court is discharged within the terms and conditions of the Act so as to ensure that its preservative and safeguarding objectives are achieved."

The decision of the Court of Justice in the present case

116. The Court of Justice delivered its judgment on the 8th November 2016 on the Article 267 reference which O'Malley J. had made: see Case C-41/15 *Dowling* EU:C: 2016: 836. The Court made it clear (at paras. 50-55 of the judgment) that the making of the direction order was essentially outside the scope of the Second Company Law Directive so that the direction order could not be held unlawful on that account:

> "50. However, as is clear from paragraphs 44 to 48 of this judgment, the direction order is not a measure taken by a governing body of a public limited liability company as part of its normal operation, but is an exceptional measure taken by the national authorities intended to prevent, by means of an increase in share capital, the failure of such a company, which failure, in the opinion of the referring court, would threaten the financial stability of the European Union. The protection conferred by the Second Directive on the shareholders and creditors of a public limited liability company, with respect to its share capital, does not extend to a national measure of that kind that is adopted in a situation where there

is a serious disturbance of the economy and financial system of a Member State and that is designed to overcome a systemic threat to the financial stability of the European Union, due to a capital shortfall in the company concerned.

51. The provisions of the Second Directive do not therefore preclude an exceptional measure affecting the share capital of a public limited liability company, such as the direction order, taken by the national authorities where there is a serious disturbance of the economy and financial system of a Member State, without the approval of the general meeting of that company, with the objective of preventing a systemic risk and ensuring the financial stability of the European Union (see, by analogy, judgment of 19 July 2016, *Kotnik and Others*, C 526/14, EU: C: 2016: 570, paragraphs 88 to 90).

52. That conclusion cannot be called into question by the fact that the direction order could be classified, as claimed by the applicants in the main proceedings, not as a 'judicial measure', but a 'provisional administrative act'. It follows from the two preceding paragraphs that the Second Directive does not preclude, in circumstances such as those at issue in the main proceedings, the adoption of a measure such as the direction order, the nature of the national authority which issued that order being of no relevance in that regard.

53. The above interpretation is in no way irreconcilable with the interpretation adopted by the Court in the judgment of 12 March 1996, *Pafitis and Others* (C 441/93, EU:C:1996:92), contrary to what is claimed by the applicants in the main proceedings. The factors set out in paragraphs 44 to 48 of this judgment distinguish the situation at issue in the main proceedings from the case that gave rise to the judgment of 12 March 1996, *Pafitis and Others* (C 441/93, EU:C:1996:92), the feature of that case being that it concerned the insolvency of a single bank. While the Court held that the Second Directive continues to apply in the case of 'ordinary reorganisation measures' (judgment of 12 March 1996, *Pafitis and Others*, C 441/93, EU:C:1996:92, paragraph 57), the Court did not, however, give a ruling, as the Advocate General observed in point 45 of his Opinion, on extraordinary reorganisation measures, such as a direction order designed to avoid, in a situation where there is a serious disturbance of the national economy and of the financial system of a Member State, the failure of a bank and thereby to maintain the financial stability of the European Union.

54. Further, as ILPGH and ILP and also Ireland have stated in their observations submitted to the Court, the national measures contested in the *Pafitis and Others* case (C 441/93, EU:C:1996:92) had been adopted in the 1986-1990 period and the Court delivered its judgment on 12 March 1996, thus well before the start of the third stage for the implementation of the Economic and Monetary Union, with the introduction of the euro, the establishment of the Eurosystem and the related amendments to the EU Treaties. Although there is a clear public interest in ensuring, throughout the European Union, a strong and consistent protection of shareholders and creditors, that interest cannot be held to prevail in all circumstances over the public interest in ensuring the stability of the financial system established by those amendments (see, to that effect, judgment of 19 July 2016, *Kotnik and Others*, C 526/14, EU: C: 2016: 570, paragraph 91).

55. In the light of the foregoing, the answer to the questions referred is that Article 8(1) and Articles 25 and 29 of the Second Directive must be interpreted as not precluding a measure, such as the direction order at issue in the main proceedings, adopted in a situation where there is a serious disturbance of the economy and the financial system of a Member State threatening the financial stability of the European Union, the effect of that measure being to increase the share capital of a public limited liability company, without the agreement of the general meeting of that company, new shares being issued at a price lower than their nominal value and the existing shareholders being denied a pre-emptive right to subscribe."

117. In its earlier judgment in Case C-526/14 *Kotnik* EU: 2016: 570 the Court of Justice had examined the implications of a Communication (known as "the Banking Communication") issued by the Commission on the 1st August 2013. It was one of a series of such communications issued during the financial crisis and its purpose was to provide guidance on the State aid rules for the financial sector in that context. In December 2013 the Slovenian authorities acting on the basis of legislation intended to implement the Banking Communication, adopted measures for the recapitalisation of certain banks which involved the writing off of subordinate rights. Following an Article 267 TFEU reference which was made by the Slovenian Constitutional Court, the Court of Justice ruled that the Communication was not, as such, binding upon Member States. It merely gave guidance to the Member States regarding the likely manner in which the State aid rules were likely to be applied.

118. The Court noted the central role played by financial services in the economy of the EU, saying (at para. 50):

"… Banks and credit institutions are an essential source of funding for businesses that are active in the various markets. In addition, the banks are often interconnected and a number of them operate internationally. That is why the failure of one or more banks is liable to spread rapidly to other banks, either in the Member State concerned or in other Member States. That is likely, in its turn, to produce negative spill-over effects in other sectors of the economy. "

119. The Court then addressed the question of burden-sharing (at paras. 54-58):

"54. When reviewing the compatibility of State aid measures with the internal market, the Commission could take the view that, as stated in point 15 of the Banking Communication, burden-sharing measures were essential in order that State aid in the banking sector should be limited to the minimum necessary and that any distortions of competition in the internal market should be limited.

55. First, such burden-sharing measures can be understood as being designed to prevent recourse to State aid merely as a tool to overcome the financial difficulties of the banks concerned.

56. Second, the burden-sharing measures are designed to ensure that, prior to the grant of any State aid, the banks which show a capital shortfall take steps, with their investors, to reduce that shortfall, in particular by raising equity capital and by obtaining a contribution from subordinated creditors, since such measures are likely to limit the amount of the State aid granted.

57. To act otherwise would be liable to cause distortions of competition, since banks whose shareholders and subordinated creditors had not contributed to the reduction of the capital shortfall would receive State aid of an amount greater than that which would have been sufficient to overcome the residual capital shortfall. In those circumstances, such aid would not, as a general rule, be compatible with EU law. 58. Moreover, in order to overcome the problem of 'moral hazard', which is linked to the fact that individuals are inclined to engage in risk-taking when the possible negative consequences of so doing are borne by the community as a whole, it is important to ensure that banks are not

encouraged by the possibility of obtaining State aid to have recourse to financial instruments that carry greater risk and are more likely to cause significant losses, the effect of which would be to create serious distortions of competition and to jeopardise the integrity of the internal market."

120. The Court accordingly ruled that the burden-sharing measures in issue did not breach the principle of protection of legitimate expectations. Even if it could have been so established, there was an overriding public interest in ensuring the stability of the financial system while avoiding excessive public spending and minimising distortions of competition.

121. The Constitutional Court had also asked whether these measures had involved a breach of property rights. The Court of Justice responded (at paras. 73-75) by addressing the rights of the shareholders:

> "73. Further, as regards the shareholders of the banks, it must be recalled that, in accordance with the general rules applicable to the status of shareholders of public limited liability companies, they must fully bear the risk of their investments. It follows from recital 5 of the preamble to Directive 2012/30 [the Directive that replaced the Second Directive] that the aim of that directive is to maintain the share capital that constitutes the creditors' security.
>
> 74. Since shareholders are liable for the debts of the bank up to the amount of its share capital, the fact that points 40 to 46 of the Banking Communication require that, in order to overcome a bank's capital shortfall, prior to the grant of State aid, those shareholders should contribute to the absorption of the losses suffered by that bank to the same extent as if there were no State aid, cannot be regarded as adversely affecting their right to property. 75. The scale of losses suffered by shareholders of distressed banks will, in any event, be the same, regardless of whether those losses are caused by a court insolvency order because no State aid is granted or by a procedure for the granting of State aid which is subject to the prerequisite of burden-sharing."

122. In effect, therefore, the Court found that the protection of property rights could not preclude a burden-sharing requirement as a condition to the grant of State aid. The Court then went on to consider whether the provisions of Articles 29, 34, 35 and 40 to 42 of Directive 2012/30 precluded burden sharing conditions. (These provisions effectively replicate the provisions of the Second Directive dealing with an increase or reduction in share capital upon which the appellants rely). The Court then said (at paras. 87 *et seq.*):

> "The background to Directive 2012/30 is the attainment of freedom of establishment in the internal market, and its principal objective is the protection of the interests of shareholders and others. The directive is intended to reassure investors that their rights will be respected throughout the internal market by the governing bodies of the companies in which they have invested, particularly when a company is formed and when its share capital is increased and reduced. Consequently, the measures provided for by Directive 2012/30 in order to guarantee that protection relate to the normal operation of public limited liability companies. By contrast, the burden-sharing measures involving both shareholders and subordinated creditors constitute, when they are imposed by the national authorities, exceptional measures. They can be adopted only in the context of there being a serious disturbance of the economy of a Member State and with the objective of preventing a systemic risk and ensuring the stability of the financial system. Contrary to what is claimed by the applicants in the main proceedings, Directive 2012/30 does not preclude measures relating to share capital being adopted, in certain specific circumstances, such as those mentioned in the Banking Communication, without the approval of the company general meeting. That interpretation cannot, moreover, be called into question by the judgment of 12 March 1993 *Pafitis and Others* (C-441/93, EU:C:1996:92). In that judgment, the Court interpreted Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent (OJ 1977 L 26, p. 1), in the context of a dispute characterised by the insolvency of a single bank, whereas, in the main proceedings, the burden-sharing measures that are the subject of points 40 to 46 of the Banking Communication are envisaged as a prerequisite for the grant, to banks faced with a capital shortfall, of State aid intended, in an exceptional context of a national economy being affected by a serious disturbance, to overcome a systemic financial crisis capable of adversely affecting the national financial system as a whole and the financial stability of the European Union."

123. It is clear from these paragraphs (and the corresponding paragraphs in Dowling) that the judgments in *Kotnik* and *Dowling* have essentially superseded what have been termed as the earlier Greek bank cases. Those bank cases - which dated from the 1990s - all concerned various attempts to provide State aid to a variety of ailing Greek banks and, in essence, the Court of Justice ruled that all such attempts were unlawful.

124. Thus, for example, in C-441/93 *Pafitis* the Court of Justice had previously stated (at paras. 38-41):

> "38 …it must be pointed out, first, that the Second Directive is intended… to coordinate the safeguards which are required by Member States of companies or firms …with a view to making such safeguards equivalent and protecting the interests of members and others. The Second Directive thus seeks to ensure a minimum level of protection for shareholders in all the Member States.
>
> 39 That objective would be seriously frustrated if the Member States were entitled to derogate from the provisions of the directive by maintaining in force rules - even rules categorized as special or exceptional - under which it is possible to decide by administrative measure, separately from any decision by the general meeting of shareholders, to effect an increase in the company' s capital…..
>
> 40 For those reasons, the Court has thus already held that Article 25(1) of the Second Directive precludes the application of rules which, being designed to ensure the reorganization and continued trading of undertakings that are of particular importance to the national economy and are in an exceptional situation by reason of their debt burden, allow an increase in capital to be decided upon by administrative measure, without any resolution being passed by the general meeting…."

125. Yet as both Advocate General Wahl and the Court pointed out in the present case, the circumstances of these Greek cases were very different to those under consideration in the present case. They all concerned *unilateral* attempts to provide state aid to *individual* banks at a time which long pre-dated the creation of the Euro. While these banks were, admittedly, of importance to the Greek economy, the failure of those banks did not pose a systemic risk to the European economy and nor could they have imperilled the future of the Euro-system which then lay in to the future. Nor were the cases decided against a background where there was a specific obligation imposed by a binding Council decision that required the recapitalisation of these institutions by a Member State by a particular date.

126. While the European Court does not, as such, adhere to a formal system of precedent and even if, admittedly, earlier decisions such as *Pafitis* might have been regarded as providing some support for the appellants' case, it is nonetheless clear from the judgments in both *Kotnik* and *Dowling* that these earlier Greek cases must be taken as having been distinguished and held not to be applicable to the very different recapitalisations at issue in the present case. One way or another, however, as this Court has recently pointed out, we cannot look behind the decision of the Court of Justice given pursuant to an Article 267 TFEU reference in these very proceedings: see *Danqua v. Minister for Justice (No.2)* [2017] IECA 20, [2017] 3 I.R. 192.

127. We must accordingly take the judgment of the Court of Justice as we find it. That Court has clearly ruled that the directions order did not amount to a violation of either Article 8, Article 25 or Article 29 of the Second Directive even if it provided for an increase in the provision of share capital to the company without the express consent of the shareholders. Irrespective of what might have been said earlier in *Pafitis* or the other Greek bank cases dating from this period, the Court of Justice has now given an authoritative and final determination on this issue of EU law which is averse to the contentions of the appellants. As it is that decision which binds this Court, it follows that the appellant's endeavours in this appeal to re-open or to re-interpret the decision of the Court of Justice must accordingly fail.

128. The very fact, however, that the direction order was held not to amount to an ex ante breach of EU law does not in *itself* mean that it cannot be held to be disproportionate or unreasonable by reference to Irish administrative law rules: see, *e.g.,* the decision of the Supreme Court to this effect in *Duff v. Minister for Agriculture* [1997] 2 I.R. 22.

The nature of the direction order

129. It is next necessary to consider the nature of the direction order of the 26th July 2011. On that day the Minister applied to and obtained from the High Court an order under the 2010 Act directing ILP to allot up to €3.8bn. of shares to him. Portions of the direction order had immediate effect and nullified the effect of many of the resolutions passed at the EGM at the behest of the appellants. The Minister invested €2.7bn. in exchange for shares once the direction order took effect.

130. The Minister acquired the shares at a price of 6.36 cents. This represented a 10% discount to the market share price of the 23rd June 2011, which was the last date before the circular for the EGM for the 20th July 2011 was circulated. As it happens the share price on the 25th July 2011 – *i.e.*, the day before the direction order – was just 5 cents.

131. While it is true that the direction order was formally confirmed by an ex parte order made by the High Court under the terms of the 2010 Act, it would have to be acknowledged that it was in substance an administrative order made by the Minister, albeit one which was judicially confirmed. This, indeed, was the very point which had previously been made by Fennelly J. in earlier interlocutory appeal concerning the joinder of the parties, *Dowling v. Minister for Finance* [2013] IESC 58:

> "The direction order, it is true, was technically made by the Court. However, in reality the Court was endorsing the proposed direction made by the Minister and it is the correctness of the Minister's actions, not those of the Court, which are in issue."

132. An *ex parte* order of this kind cannot permanently affect the legal rights of the parties affected without giving a prior opportunity to be heard: see, *e.g., DK v. Crowley* [2002] IESC 66, [2002] 2 I.R. 712. This very point had also been made by Fennelly J. in the interlocutory appeal which I have mentioned and by O'Malley J. in her judgment under appeal.

133. It must also be accepted that the direction order amounted, in effect, to a compulsory take-over of the bank by the Minister, albeit one which was necessitated in the public interest. It is important to state that none of the parties to this appeal disputed this proposition.

134. In principle, therefore, in these circumstances, the appellants were constitutionally entitled to receive something close to full value for their shareholding. As Denham C.J. said in *Rafferty v. Minister for Agriculture & Food* [2014] IESC 61, a case concerning the entitlement of a farmer to receive compensation for the true value of the slaughter by agents of the Minister for Agriculture of his sheep flock as a precautionary measure to stop the spread of foot and mouth disease:

> "A person who has been compulsorily deprived of his or her property or property interests by the State is entitled, in principle, having regard to the constitutional protection of property rights from unjust attack, to compensation for the total loss caused or resulting as a consequence of compulsory deprivation of those interests. As the case law of this Court, including those cited above, indicates there are circumstances in which it may be, for legitimate reasons, constitutionally permissible to limit the compensation to an amount less than the total loss including consequential loss. *Any such exception would be subject to strict scrutiny by the courts as to the legitimacy of the grounds limiting full compensation for loss actually sustained, and subject also to the principle of proportionality.*" (emphasis supplied)

135. These comments also have relevance so far as the scope of judicial review of the directions order is concerned, a topic to which I now propose to turn.

The scope of review

136. As I have already noted, s. 11 of the 2010 Act provides that the High Court may set aside the directions order if the applicant can show that the opinion of the Minister under s. 7(2) was unreasonable or was vitiated by error of law. In effect, therefore, at least so far as this application is concerned, s. 11 provides for a form of statutory judicial review akin to what might be termed the standard common law Ord. 84-style judicial review. I propose, therefore, to deal with the present case in the light of the principles established and developed in common law judicial review and the test of reasonableness found there in respect of this s. 11 application.

137. Given the nature of the direction order and its clear implications for the appellants' constitutional rights, it is plain that the "no evidence" test set out in *O'Keeffe v. An Bord Pleanála* [1993] 1 IR 39 would be ineffective to secure these constitutional rights: see, *e.g.*, *Holland v. Governor of Portlaoise Prison* [2004] IEHC 208, [2004] 2 I.R. 575, *Clinton v. An Bord Pleanála* [2007] IESC 19, [2007] 4 IR 701, *Meadows v. Minister for Justice* [2010] IESC 3, [2010] 2 I.R. 201, *Efe v. Minister for Justice* [2011] IEHC 214, [2011] 2 I.R. 798 and *N.M. (DRC) v. Minister for Justice* [2016] IECA 217, [2016] 2 I.L.R.M. 369. If the State (through its judicial arm) is required by Article 40.3.2 of the Constitution to respect and vindicate these property rights as far as practicable, that test is not satisfied by a simple consideration of whether there was evidence by which the direction order could be sustained.

138. This is perhaps best illustrated so far as the present case is concerned by the Supreme Court's decision in *Clinton*, a case where the applicant had challenged the validity of a compulsory purchase order which had been confirmed by An Bord Pleanála. In his judgment Geoghegan J. rejected the argument that the *O'Keeffe* "no evidence" test should govern this application, saying ([2007] 4

IR 701, 723):

> "It is axiomatic that the making and confirming of a compulsory purchase order to acquire a person's land entails an invasion of his constitutionally protected property rights. The power conferred on an administrative body such as a local authority or An Bord Pleanála to compulsorily acquire land must be exercised in accordance with the requirements of the Constitution, including respecting the property rights of the affected landowner (*East Donegal Co-Operative Ltd. v. The Attorney General* [1970] I.R. 317). Any decisions of such bodies are subject to judicial review. It would insufficiently protect constitutional rights if the court, hearing the judicial review application, merely had to be satisfied that the decision was not irrational or was not contrary to fundamental reason and common sense."

139. The same is true here. It might, for example, be difficult to demonstrate that the fixing of an acquisition price well below market value was irrational or contrary to fundamental reason (in the restricted *O'Keeffe* sense of that term). But that could not be – and is not - the test required by Article 40.3.2 so far as the protection and vindication of the applicants' property rights is concerned. As Denham C.J. said in *Rafferty*, any departure from the principle of market compensation would have to be subject to the principle of strict scrutiny and the principles of proportionality.

140. To that extent, therefore, I would, if necessary, go further than O'Malley J. insofar as she placed any reliance on the *O'Keeffe* test in adjudicating on the reasonableness and proportionality of the directions order. In any event, it is clear from the modern post-*Meadows* case-law that the guiding test in cases of this kind where administrative decisions materially impact on constitutional rights is in substance the proportionality test articulated in *Heaney v. Ireland* [1994] 3 I.R. 593.

Proportionality analysis

141. The classic *Heaney* analysis as articulated by Costello J. ([1994] 3 I.R. 593, 607) is that where a constitutionally protected right is restricted by legislation (or, as I would add, by administrative decision such as the direction order in the present case), the restrictions must:

> "(a) be rationally connected to the objective and not be arbitrary, unfair or based on irrational considerations;
>
> (b) impair the right as little as possible, and
>
> (c) be such that their effects on rights are proportionate to the objective."

142. The application of the first limb of the *Heaney* test cannot really be in dispute. As Cooke J. pointed out in *Aurelius Capital Master*, the 2010 Act and the power granted thereunder to make a directions order were based on the rational objective of saving the banks – and, by extension, the wider economy – by measures designed at once both to stabilise the banking system and to re-capitalise it.

143. The second limb of the test ("…impair the rights as little as possible….") cannot, however, quite literally mean what it says. Given that, as *Heaney* shows, we have borrowed the concept of proportionality from the Canadians, the comments of MacLachlin J. (at para. 160) in *RJR-MacDonald Inc. v. Canada (Attorney General)* [1995] 3 S.C.R. 199 are rather in point:

> "…..As the second step in the proportionality analysis, the government must show that the measures at issue impair the right of free expression as little as reasonably possible in order to achieve the legislative objective. The impairment must be "minimal", that is, the law must be carefully tailored so that rights are impaired no more than necessary. The tailoring process seldom admits of perfection and the courts must accord some leeway to the legislator. If the law falls within a range of reasonable alternatives, the courts will not find it overbroad merely because they can conceive of an alternative which might better tailor objective to infringement….On the other hand, if the government fails to explain why a significantly less intrusive and equally effective measure was not chosen, the law may fail."

144. A similar point had been made by Murray C.J. in *Meadows* ([2010] 2 I.R. 701 at 723):

> "I am of the view that the principle of proportionality is a principle that may be applied for the purpose of determining whether, in the circumstances of a particular case, an administrative decision may properly be considered to flow from the premises on which it is based and to be in accord with fundamental reason and common sense. In applying the principle of proportionality in this context I believe the Court may have regard to the degree of discretion conferred on the decision-maker. *In having regard to the degree of discretion a margin of appreciation should be allowed to the decision-maker in choosing an effective means of fulfilling any legitimate policy objectives.*" (emphasis supplied)

145. It is clear from these comments that some flexibility must necessarily be allowed to decision makers, not least in cases of this kind where the decision in question had large scale macro-economic implications and where it was required to be taken urgently and against the background of an acute emergency.

146. In a submission to the Minister for Finance on the 17th June 2011 ILP expressed concerns about the proposed capital injunctions. It feared that it might lead to the over-capitalisation of the bank and the dilution of the existing shareholders. The deadline of the 31st July 2011 furthermore restricted capital raising alternatives. I LP accordingly proposed alternative structures, with a placing range in the region of €0.30 to €0.75:

> "Shareholders could be offered pre-emption over the ordinary share issuance by the Irish State.
>
> • Given scale of capital required in order for shareholders to "follow their money", unlikely to attract significant take up.
>
> • However, would potentially alleviate some of the negative perception around value migration from existing shareholders to the State.
>
> • The 31 July deadline would still be met. Shares could be offered back to existing shareholders post 31 July deadline for capital injection (given timetable pressure in issuing Prospectus prior to 31 July) - precedents are Lloyds and RBS (October 2008) issuance.
>
> • Claw back offer to existing shareholders would require limited documentation under ESM.

• All or part of State Investment currently structured as ordinary shares could be structured as a B share investment (similar to RBS).

• Potential to determine an exit price for the B shares such that in the event of overcapitalisation (i.e. stress scenario envisaged under PCAR does not materialise) the company could undertake a targeted buyback of a specific class of shares as economic conditions improve.

• RBS' non-preemptive issuance of B shares in December 2009 was structured in this way (whereby the exit price of the B shares was equal to the entry price), but incurred a coupon (which may not qualify for CT1 capital under Basel 3 rules).

• Instead, B shares could have a pre-determined buy-back price based on an assumed per annum return for the State."

147. In the end, the direction order of the 26th July 2011 did not provide for any of these things. Its failure to do so is really at the heart of the present proportionality challenge and, for that matter, the present appeal. The appellants maintain that the Minister could have:

(i) provided for a pre-emptive offer by shareholders;

(ii) provided for a "B" shares option by which in the event that it transpired that ILP was overcapitalised as market conditions recovered, these shares could have been bought back by the company and

(iii) purchased the shares at the pre-PCAR/PLAR review price of March 2011.

It is said that because the Minister failed to do some or all of these things, the appellants' constitutional rights qua shareholders were impaired to a greater extent that was necessary, thereby failing the second limb of the *Heaney* proportionality test.

148. It is, I suppose, true to say that the Minister could perhaps have done some or all of these things but, as MacLachlin J. observed in her judgment in *RJR MacDonald*, these must be reasonable alternatives. Or, to use the language of Article 40.3.2, the obligation to vindicate these rights is qualified by considerations of practicability. And, in the desperate circumstances of July 2011, there were a great many things which were not practicable.

The failure to offer the ILP shareholders pre-emption rights
149. One may start by looking at what in many ways is the appellants' strongest card, namely, the failure to offer the shareholders pre-emption rights. One could, I think, make a cogent theoretical case that the failure to do this was disproportionate. After all, pre-emption rights had been offered to shareholders in the case of some of the UK bank rescues from this period, the case of RBS being a case in point, and in this jurisdiction, pre-emption rights had just been offered in the case of Bank of Ireland shareholders. Moreover, a successful pre-emptive offer – whether by a rights issue or a placing – would have necessarily reduced the State's exposure, thereby easing – if only marginally – the heavy burdens which bank recapitalisation entailed for taxpayers.

150. Yet it must be accepted that this theoretical case is entirely undermined by the realities which then prevailed in July 2011. The unchallenged evidence was that the Minister had been informed by ILP that there was limited interest in pre-emption among the shareholders, many of whom were small retail investors. A pre-emptive offer would have required ILP to prepare a prospectus and dispatch this to some 135,000 shareholders and then gauge the take-up of the offer. Mr. Cook estimated that this process would take at least two months, when the reality was that ILP was but days away from disaster if the 31st July 2011 deadline was not met. In that respect the position of ILP was appreciably different from that of Bank of Ireland which, as Mr. Moran pointed out, had managed to secure significant outside investment and which was to be the sole domestic banking institution to have avoided nationalisation.

151. A further consideration is that a pre-emptive offer would have been disproportionately expensive. It was estimated that the cost of such an offer when underwritten by the State would have been in the order of some €100m. (or perhaps even more), when compared with the value of the original shareholder's interests which were estimated to be some €19m. on 23 June 2011. Nor is there any evidence at all that the appellants themselves would have been prepared to advance the significant sums required to protect their financial interests via a pre-emptive offer.

The B share option
152. The second possibility was the "B" shares option. This would have involved an essentially passive investment by the State in the company, albeit doubtless one providing for an interest coupon. The critical feature, nevertheless, of this option was that it denied the Minister the right to share in any upswing in the market valuation of the company as the existing shareholders would have been given the right to buy out that investment as and when (if ever) the company's financial state improved.

153. There was, admittedly, a prospect that that it would ultimately transpire that ILP would turn out to have been over-capitalised, but given the evidence, the Minister was perfectly entitled to take the view that this prospect was essentially a remote one. Even with the benefit of hindsight nothing has emerged which has disturbed the accuracy of the PLAR and PCLAR stress tests and the consequential necessity to raise large sums of capital.

154. Painful though it may be to say so, any realistic assessment of the financial circumstances of ILP in July 2011 revealed a failing bank whose demise was, absent extensive State support, perhaps no more than days away. The appellants have strongly urged that ILP simply faced a short term liquidity problem which, with some forbearance and *some* State support, it could have traded through. One might wish that that were so, but all the established evidence points otherwise.

155. In these circumstances, the State was entitled to seek a reasonable return on its investment. Indeed, so desperate in fact was the parlous state of ILP that, as O'Malley J. noted in her first judgment and as I have already noted, some €800m. of the €2.3bn. investment had to be immediately written off as a loss for the purposes of the accountancy rules applied by Eurostat, the EU's official statistics agency. It must also be recalled that the Commission's Banking Communication had previously stated in this context that "the Member State concerned should in principle receive rights, the value of which correspond to their contribution to the recapitalisation." That proposition does not, of itself, determine the reasonableness of the State's decision not to take the B share option, but it nonetheless does show the banking and commercial context in which the State made its investment, and to which it was entitled to have regard. Had the State agreed to the B shares option proposal, it would not have received rights "the value of which correspond to their contribution to the capitalisation", because the State would have covered the exposure to the liabilities of ILP, but with no right to share in any recovery of the market value of the company in the event that this were ever to occur,

something which, of course, was far from certain in July 2011.

156. I accept, of course, that the Banking Communication was, as the Court of Justice observed in *Kotnik*, simply non-binding guidance so far as the State aid rules were concerned. It is also true to say that simply because a particular administrative decision was found not to violate the State aid rules, this does not mean that the validity of the underlying decision cannot be examined by the domestic courts by reference to national law principles. This, indeed, has already happened in the long-running *BUPA* case where the risk equalisation scheme promulgated for health insurance purposed by the Minister for Health was held not to infringe the State aid rules by the Court of First Instance (now General Court), but where the scheme itself was ultimately found by the Supreme Court to be *ultra vires*: see *BUPA International Ltd. v. Health Insurance Authority* [2008] IESC 42, [2009] 1 I.L.R.M. 81. But even making all due allowance for this, the principles contained in the Banking Communication nonetheless contain much good sense and reflect standard company law thinking in this jurisdiction to the effect that the law will give priority to the needs of creditors at the expense of the shareholders. These principles can, I think, be applied by analogy to the issues of reasonableness of the Minister's decision to make an investment in an ailing bank and to preserve at least some hope value should the value of the bank improve in time.

157. One might accordingly ask: what prudent investor would ever have agreed to make such a significant investment in a failing bank so heavily dependent on ELA support and in respect of which debt markets were closed without at least receiving an assurance that it could participate in the "upside" were the market value of the company ever to recover? Posed thus and leaving aside for one moment the obvious observation that no prudent investor would actually have invested in ILP in July 2011, the question nonetheless really answers itself.

Whether the share price paid was artificially low

158. There remains the question of whether the price which was actually paid for the shares was artificially low. As I have already observed, given what in effect was the compulsory nature of the take-over of the company, it is clear from the decision in Rafferty that the appellants are entitled to something close to the full market value of their shares or, in this instance, for the diminution of that shareholding by reason of the massive and non-premptive acquisition of shareholding by the Minister.

159. There is, however, one important difference between the present case and *Rafferty*. In the latter case the plaintiff was the entirely innocent farmer whose sheep holding had been slaughtered on a prophylactic basis in the public interest in order to stop the spread of foot and mouth disease. It is true that the direction order made here was also made in the public interest, but the plain fact of the matter was that the bank was failing and without this State investment it would – as O'Malley J. expressly found in her first judgment – in all probability have collapsed within days, leading in that situation to a total loss of shareholder value. In a market economy such as ours shareholders cannot realistically expect to be compensated by the State for what amounts, objectively, to a poor investment decision. As I have already observed, these were also the sentiments expressed by the Court of Justice in *Kotnik*, even if these comments were admittedly made in the context of State aid.

160. The very fact, therefore, that the shareholders were required to suffer a 10% reduction on the then prevailing share price immediately prior to recapitalisation as part of this burden-sharing cannot be regarded in these particular circumstances as some *ex ante* violation of their property rights as protected by Article 40.3.2. This is because although the company was being compulsorily acquired – and the intrinsic value of the appellant's shareholding massively diluted by reason of the Minister's acquisition of over 99% of the company through the unilateral extension of the company's shareholding – unlike cases such as *Rafferty*, the dominant consideration nonetheless must be that without that compulsory investment the bank was within days of being wound-up and the probable loss of the entirety of all shareholder value.

161. In truth, the appellants do not *as such* seriously contest the 10% deduction. Their real objection is that the price at which the Minister acquired his shares was not at levels which prevailed in respect of ILP shares *prior* to the announcement of the PCAR/PLAR results at the end of March 2011. This is because a key critique of the price paid by the Minister for the shares which has been advanced by the appellants was that the State respondents had created a false market in respect of the ILP share price. As I have noted elsewhere, this arguments rests on the premise that there had been unusual share dealings in the ILP share price in late March and early April 2011. But, as O'Malley J. found in her judgment, it is far more likely that these price dealings reflected the digestion by the market of the results of the stress tests which had just been published at the end of March.

162. It is, moreover, hard to see how the laying bare of the true financial position of ILP in the aftermath of this large-scale FMPR exercise conducted by a specialist international consultancy company (BlackRock) could be said to have created a false market in ILP shares. As I have already stated, it is far more likely that the sharp falls in the ILP share price which occurred thereafter reflected the market's assessment that the true scale of the company's difficulties had not been fully priced into the share price. If the company was facing the task of raising €2.3bn. from external sources by the end of July 2011 in circumstances where debt markets were closed to it and where no obvious well-resourced external investor was available, it is scarcely surprising that the share price was continuing to fall as that deadline loomed.

163. For these reasons, I like, O'Malley J., would reject the argument advanced by the appellants to the effect that the Minister had created a false market in ILP shares and that this artificially depressed the ultimate price paid by the Minister for these shares.

164. The final argument advanced by the appellants was that the share price did not reflect the true level of the contribution made by the shareholders. Specifically, it was said that the shareholders had already contributed significantly through the ultimate sale of Irish Life to the Minister for some €1.1bn. and, more particularly, that the share price paid did not reflect at all the value of the Irish Life asset. I think the simple answer to this latter point to be found in standard company law principles, namely, that a particular shareholder has no rights *in specie* to any particular item of property of the company. As Kenny J. famously said in *Attorney General v. Jameson* [1904] 2 I.R. 644 at 671:

> "No shareholder has a right to any specific portion of the company's property, and, save by and to the extent of, his voting power at a general meeting of the company, cannot curtail the free and proper disposition of it."

165. This point was also well expressed by Courtney, *Law of Private Companies* (Dublin, 2016) at 447:

> "Where the company holds property, it holds it in its own right and its shareholders have no right to or interest in its assets."

166. It follows that Irish Life was an asset of ILP (or, perhaps, more strictly, ILP General Holdings plc). Critically, however, it did *not* belong to the shareholders and nor can it be said that ILP in its various corporate structures held Irish Life on some form of trust for those shareholders. The net result of this is that it cannot be said that Irish Life was owned in some way – directly or indirectly – by the shareholders. Nor does it follow that through this sale of Irish Life the shareholders can be said to have contributed an asset

towards the company's liabilities, so that to that extent they had burden-shared already.

167. In these circumstances, I cannot say that the price paid by the Minister for the acquisition of these shares was not close to the market price which then prevailed. It is true that the price was at a 10% deduction to premium, but in the circumstances I have described where all shareholder value would otherwise have been lost and where no other reasonable prudent investor would have this investment, this deduction cannot be seen as an appreciable interference with property rights. Even if it were, it is clear that the substance of the appellants' constitutional rights were fully respected in the circumstances.

Conclusions
168. In summary, therefore, I would conclude as follows:

169. First, this Court cannot look behind the judgment of the Court of Justice in *Dowling* insofar as it was concluded that the making of the direction order was essentially outside the scope of the Second Company Law Directive, so that the direction order could not be held unlawful on that account. Irrespective of what might have been said earlier in *Pafitis* or the other Greek bank cases dating from this pre-Euro period, the Court of Justice has now given an authoritative and final determination on this issue of EU law in the present case which is averse to the contentions of the appellants. As it is that decision which binds this Court, it follows that the appellant's endeavours in this appeal to re-open or to re-interpret the decision of the Court of Justice must fail.

170. Second, as the appellants' challenge in the present appeal centred on the *manner* in which the recapitalisation was effected by the provisions of the 2010 Act and the direction order made thereunder, it follows that the proportionality and reasonableness of these measures is in essence governed by domestic law rather than by EU law. I would regard that the power to set aside a direction order on grounds of reasonableness or error of law contained in s. 11 of the 2010 Act in effect provides in statutory form for judicial review of an administrative decision such as the High Court ordinarily enjoys in standard Order 84 proceedings.

171. Third, the direction order must be regarded as amounting, in substance, to a compulsory take-over of the Bank by the Minister, albeit one which was necessitated in the public interest. In principle, therefore, the appellants were constitutionally entitled to receive something close to full value for their shareholding.

172. Fourth, given the nature of the direction order and its clear implications for the appellants' constitutional rights, it is plain that the "no evidence" test set out in *O'Keeffe* would be ineffective to secure these constitutional rights.

173. Fifth, so far as any proportionality analysis conducted by reference to the *Heaney* test is concerned, it cannot be said that the failure to offer the shareholders pre-emption rights was unreasonable in the circumstances. The unchallenged evidence was that the Minister had been informed by ILP that there was limited interest in pre-emption among the shareholders, many of whom were small retail investors. A pre-emptive offer would have required ILP to prepare a prospectus and dispatch this to some 135,000 shareholders and then gauge the take-up of the offer. It was estimated that this process would take at least two months, when the reality was that ILP was but days away from disaster if the 31st July 2011 deadline was not met. In that respect the position of ILP was appreciably different from that of Bank of Ireland which had managed to secure significant outside investment and which was to be the sole domestic banking institution to have avoided nationalisation.

174. Sixth, a further consideration is that a pre-emptive offer would have been disproportionately expensive. It was estimated that the cost of such an offer when underwritten by the State would have been in the order of some €100m. (or perhaps even more), when compared with the value of the original shareholder's interests which were estimated to be some €19m. on 23 June 2011. Nor is there any evidence at all that the appellants themselves would have been prepared to advance the significant sums required to protect their financial interests via a pre-emptive offer.

175. Seventh, nor can it be said that the failure to offer a B shares option was unreasonable. This would have involved an essentially passive investment by the State in the company, albeit doubtless one providing for an interest coupon. The critical feature, nevertheless, of this option was that it denied the Minister the right to share in any upswing in the market valuation of the company as the existing shareholders would have been given the right to buy out that investment as and when (if ever) the company's financial state improved.

176. There was, admittedly, a prospect that that it would ultimately transpire that ILP would turn out to have been over-capitalised, but given the evidence, the Minister was perfectly entitled to take the view that this prospect was essentially a remote one. Painful though it may be to say so, any realistic assessment of the financial circumstances of ILP in July 2011 revealed a failing bank whose demise was, absent extensive State support, perhaps no more than days away. In these circumstances, the State was entitled to seek a reasonable return on its investment.

177. It must also be recalled that the Commission's Banking Communication had previously stated in this context that "the Member State concerned should in principle receive rights, the value of which correspond to their contribution to the recapitalisation." Yet had the State agreed to the B shares option proposal, it would not have received rights "the value of which correspond to their contribution to the capitalisation", because it would simply have meant that the State would have covered the exposure to the liabilities of ILP, but with no right to share in any recovery of the market value of the company in the event that this were ever to occur, something which, of course, was far from certain in July 2011.

178. Finally, I would reject the argument that, having regard to the evidence, the State had somehow created a false market in ILP shares or that the shareholders did not receive what, in substance, was fair value for their existing shareholding by reason of the State's investment. This is because although the company was being compulsorily acquired – and the intrinsic value of the appellant's shareholding massively diluted by reason of the Minister's acquisition of over 99% of the company through the unilateral extension of the company's shareholding – unlike cases such as *Rafferty*, the dominant consideration nonetheless must be that without that compulsory investment the bank was within days of being wound-up and the probable loss of the entirety of all shareholder value.

179. In these circumstances I find myself coerced to conclude that the direction order satisfied the substance of the appellants' constitutional rights, even if that order also provided for a form of burden sharing by the shareholders.

180. It follows, therefore, for all of the reasons that neither the Minister's opinion as reflected in the directions order or the actions which he took by virtue of that order has been shown to be unreasonable in law. It follows, therefore, that the appellants are not entitled to the relief sought and, specifically, the order sought pursuant to s. 11 of the 2010 Act setting aside the direction order.

181. In these circumstances, therefore, I would dismiss the appeal.