Neutral Citation: [2014] IEHC 278

THE HIGH COURT

[2011 No. 207 COS]

IN THE MATTER OF NOXTAD LIMITED (IN LIQUIDATION) AND IN THE MATTER OF SECTION 150 OF THE COMPANIES ACTS 1990 AND SECTION 56 OF THE COMPANY LAW ENFORCEMENT ACT 2001

BETWEEN

DAVID VAN DESSEL

APPLICANT

AND

JAMES EDWARD ESMONDE AND PATRICK O'TOOLE

RESPONDENTS

JUDGMENT of Ms. Justice Finlay Geoghegan delivered on the 26th day of May 2014.

1. The applicant is the Official Liquidator of Noxtad Ltd. ("the Company"), having been so appointed by order of the High Court made on 30th May, 2011, on a petition presented by the Revenue Commissioners on 1st April, 2011.

2. The Liquidator brings this application following a report made to the Director of Corporate Enforcement pursuant to s. 56 of the Company Law Enforcement Act 2011, and not having been relieved of his obligation to bring the application.

3. The Liquidator seeks declarations pursuant to s. 150 of the Companies Act 1990 (as amended) in respect of each of the respondents.

4. The Company was incorporated on 23rd December, 1996. The respondents have each been directors of the Company since January 1997, and were directors at the date of commencement of the winding up. It is not in dispute that the Company is insolvent. The Liquidator has made clear that he accepts that the respondents acted honestly in relation to the conduct of the affairs of the Company. The factual issues which he puts before the Court raise serious questions as to whether the respondents can satisfy the Court that they acted responsibly as directors of the Company. The Liquidator is of the view that they did not do so and had expressed that view, along with the relevant facts in four affidavits. The second named respondent, Mr. O'Toole, has sworn five affidavits in response on his own behalf and setting out facts on behalf of the first named respondent, Mr. Esmonde.

5. The matters of concern raised by the Liquidator for consideration by the Court fall under the following headings:

> (i) The failure of the Company to file statutory returns and audited accounts in breach of s. 125 of the Companies Act 1963;
>
> (ii) the failure to file Revenue returns and the build up of substantial liabilities to the Revenue;
>
> (iii) the delay in placing the Company into liquidation and
>
> (iv) the failure to assist the Liquidator.

6. Prior to considering these matters and the respondents' explanations, I propose setting out the applicable law about which there was no real dispute.

7. Section 150 of the Companies Act 1990, insofar as relevant, provides:

> "150.—(1) The court shall, unless it is satisfied as to any of the matters specified in subsection (2), declare that a person to whom this Chapter applies shall not, for a period of five years, be appointed or act in any way, whether directly or indirectly, as a director or secretary or be concerned or take part in the promotion or formation of any company unless it meets the requirements set out in subsection (3); and, in subsequent provisions of this Part, the expression 'a person to whom section 150 applies' shall be construed as a reference to a person in respect of whom such a declaration has been made.
>
> (2) The matters referred to in subsection (1) are—
>
> > (a) that the person concerned has acted honestly and responsibly in relation to the conduct of the affairs of the company and that there is no other reason why it would be just and equitable that he should be subject to the restrictions imposed by this section, or
> >
> > . . ."

8. The issue for the Court is whether it can be satisfied that the respondents each acted honestly and responsibly in relation to the conduct of the affairs of the Company, as directors, and that there is no other reason why it would be just and equitable that either should be subject to the restrictions imposed by s. 150 of the Act of 1990.

9. The facts, as stated, to not raise any issue as to the honesty of either of the respondents. Further, whilst the Liquidator has raised the issue of an alleged failure by the respondents to assist him in the winding up which could, in certain circumstances, constitute an "other reason" why it would be just and equitable to make a declaration of restriction, I am not satisfied on the facts

that the alleged non-cooperation is of an order which would so justify.

10. The issue on the facts set out in the affidavits is only whether the Court can be satisfied that the respondents each acted responsibly in relation to the conduct of the affairs of the Company. The proper approach of the Court to determining this question where no issue is raised as to the honesty of the directors, following the review of the relevant law by Fennelly J. in *Mitek Holdings Ltd. and the Companies Acts* [2010] IESC 31, [2010] 3 I.R. 374, and earlier decisions, has been set out by me at paras. 13 to 15 inclusive of the judgment I delivered in the matter of *Derbar Developments Ltd. (In Liquidation)* [2012] IEHC 144, and subsequently repeated in Abington Doors [2014] IEHC. I do not propose setting it out in full again in this judgment. Suffice to say for the facts of this application that the Court must look at the entire tenure of the respondents as directors; the Court must be careful not to judge the actions of the respondents with the benefit of hindsight; and the Court should consider the extent to which the directors have displayed a lack of commercial probity or want of proper standards, particularly in the period leading up to the making of the winding up order or after it became or should have become apparent that the Company was insolvent. The Court must also have regard to the extent to which the respondents have not complied with obligations imposed on them as directors by the Companies Acts 1963 to 2012.

11. Counsel for the respondents referred me to what I stated in judgment delivered in the matter of *Digital Channel Partners Ltd. (In Voluntary Liquidation)* [2004] 2 I.L.R.M. 35, at pp. 40 to 41, which is relevant to the admitted use made of monies due to the Revenue Commissioners for the Company's cashflow:

> "There are, I think, two ways of looking at the failures to make tax returns. The failures to make tax returns are clearly in breach of the relevant Taxes Acts. Similarly, the failure to make the payments are in breach of the Taxes Acts. The mere fact that a company is in breach for, as in this case, a relatively limited period will not of itself, it seems to me, indicate that the directors of the company have acted either dishonestly or irresponsibly in such a way as to preclude my concluding that overall they acted responsibly and honestly in relation to the conduct of the affairs of this company. Unfortunately and inevitably where companies are under significant financial pressure, this may occur.
>
> It appears to me that in relation to tax liabilities there must be something more than a limited failure over a period to indicate that the directors have acted irresponsibly. This has been put in a number of different ways and certainly insofar as there may be evidence that there either has been selective distribution or selective payment of liabilities of a company or indeed a total disregard of obligations to the Revenue, or even a decision to effectively seek to use taxation liabilities for the purpose of financing a company, that of itself will normally be indicative of the fact that directors have been acting at least irresponsibly."

12. Counsel for the respondents submitted that on the facts herein, in applying the above criteria to the admitted failures to make payment to the Revenue Commissioners, that it should not give rise to a refusal by the Court to find that the respondents had acted responsibly whilst directors of the Company.

Assessment and Conclusion

13. It is not in dispute that the Company failed to file statutory returns and audited accounts in breach of s. 125 of the Companies Act 1963. Such failures resulted in the Company being struck off the Registrar of Companies in 2000, then being restored in 2002, and being struck again and restored in 2005. Whilst relevant, they are not determinative and there were, in those periods, other relevant positive facts put before the Court in relation to compliance with statutory obligations, including the filing of tax returns and discharge of Revenue liabilities until February 2010. The Liquidator has deposed that the Company failed to file an annual return made up for the year ending 30th September, 2010, or to file audited accounts for the year ending 30th September, 2010, which is not disputed. Whilst relevant, this failure, of itself, given that the petition was presented on 1st April, 2011, would not preclude the Court from finding that the respondents acted responsibly as directors.

14. The real issues of concern for the Court are the respondents' approach to Revenue liabilities in 2010/2011, and the continued trading of the Company in 2011, and consequent increase in trade liabilities.

15. The trading of the Company is unusual. Mr. O'Toole deposes that the Company was incorporated for the purpose of the purchase, ownership and hire of machinery for use in the construction industry; that it did not commence trading until 2002, and only became involved in the hotel business in 2006.

16. The Company traded the Carlton Abbey Hotel in Athy from January, 2010 until three weeks prior to the commencement of the winding up. The background to its doing so is complex, and on the affidavits, there appear to be some discrepancies in the details of the explanations as to precisely what occurred prior to 2010. However, such details are not relevant to the admitted trading from January, 2010 until April 2011, which is the relevant period for the matters which have to be determined in this application.

17. The first named respondent is a builder and the second named respondent a solicitor. It appears that in 2004, they purchased lands in Athy with the intention of constructing a new hotel. They jointly borrowed €7 million from Bank of Scotland Ireland ("BOSI"), secured, *inter alia*, by Personal Guarantees and provided €3 million of their own personal funds. The intention was to lease the hotel to a management company to obtain capital allowance benefits from the rental income arising therefrom. The hotel was built, overseen by Mr. Esmonde. Mr. O'Toole deposes that their then tax advice was to lease the hotel to an existing company which would then lease the hotel to a management company. The Company was chosen as the existing company as it was not then active, and it then appears to have leased the hotel to a company, Carlton Athy Hotel Ltd. which was managed by the Carlton Group. This occurred in 2006, and the hotel commenced trading under the management of the Carlton Group. This continued until the end of 2009. Between 2006 and 2009, the Company's role in relation to the hotel was as landlord. Mr. O'Toole has deposed that the respondents were not involved in day-to-day management at that time. It is not expressly stated that the respondents were also directors of Carlton Athy Hotel Ltd but it appears they may have been. Even if they were, the Court is not considering their conduct as directors of that company. However, their knowledge of what occurred during the period when Carlton Athy Hotel Ltd. traded the hotel is relevant to their conduct as directors of the Company from January, 2010 to April, 2011.

18. Mr. O'Toole, at para. 6 of his affidavit sworn on 4th July, 2013, has deposed:

> "In 2009, the Revenue were owed €430,000 by Carlton Athy Hotel Ltd., as we understand that payments to the Revenue were sacrificed in order to pay other creditors. The position was unsustainable and it was by mutual agreement that the lease was terminated."

19. It further appears from Mr. O'Toole's affidavit that BOSI, which was the lender to the respondents (and, presumably, had security over the hotel) engaged Horwath Bastow Charleton ("HBC") to carry out an independent review of the trading history of the hotel and

to establish whether it was a viable business. HBC reported in November 2009, and a copy of their feasibility study was exhibited. The trading history in that review relates, not to the Company, but rather, Carlton Athy Hotel Ltd. which traded the hotel business until the end of 2009. Whilst Mr. O'Toole deposes that the review indicates that the respondents had introduced personal funds to "the Company", and that the amount due and owing in 2009 to them stood at approximately €1 million, that appears to be rather a reference to Carlton Athy Hotel Ltd. which was then trading the hotel. The review also indicated a potential increase in total revenue during 2010, and that if savings were made on costs, including savings in payroll, a positive EBITDA (earnings before interest, tax and amortisation) of €354,000 could be achieved.

20. The review, at p. 38, stated:

> "9. Balance Sheet Review
>
> In 2008, Trade creditors were €577,315. This was reduced to €496,884 in 2008 (sic). Currently creditors total €267,280. Almost 60% of trade creditors are over 90 days. The level of trade creditors is in line with a hotel of its level. Although the creditor situation is stretched, there is no risk of suppliers not delivering orders.
>
> The Revenue are owed €430k and it is the payments to the Revenue that have been sacrificed to pay other creditors.
>
> The Directors introduced personal funds to the company over the last few years to assist with the payment of creditors. The amount owing to the promoters stands at €1m."

It must be recalled that whilst the above review does not relate to the Company, the respondents were aware of it prior to January 2010 and in particular how payment of trade creditors had been made. From Mr O'Toole's affidavit they appear to be the persons who introduced personal funds and were owed the €1million.

21. It appears that subsequent to this review, in consultation with BOSI, it was decided that the Company would take over the trading of the hotel and that the respondents, as directors of the Company, would manage the business of the hotel. The respondents employ a financial controller, Mr. Morrow, who, it is deposed, was responsible for the day-to-day management of the business, and the first named respondent held a meeting on a weekly basis with Mr. Morrow and the second named respondent, every second week. A hotel manager was also employed.

22. Mr. O'Toole has fairly deposed that between January, 2010 and April, 2011 that the majority of the discussions focused on the implementation of promotional programmes for the development of the hotel and the assessment of whether the Company's business was continuing to grow. At para. 11 of the affidavit of 4th July, 2013, Mr. O'Toole deposes:

> "During this period, insufficient attention was being given to the issues of cashflow and Revenue liabilities, which continued to accrue during this period. Mr Morrow had responsibility for making Revenue returns and during this time, I understood that the Company's tax returns were being filed. I do acknowledge that I was aware that monies due to the Revenue were being used to assist the hotel's cashflow. While recognising that this practice should not have been allowed to develop, I say that we genuinely believed in the hotel's viability and we believed at the time that we would be able to trade our way out of these difficulties and ultimately discharge all Revenue liabilities."

23. The facts, which are not disputed, in relation to Revenue returns and liabilities in this period are as follows:

> (i) In respect of VAT from 1st March, 2010, only €2,000 was remitted to the Revenue, leaving a liability of €183,877.94 to the Revenue for the 14-month period prior to liquidation.
>
> (ii) In respect of PAYE, with the exception of August 2010, returns were made and payments made up to 30th September, 2010. However, thereafter, payments were not made and some returns not made, resulting in a PAYE liability of €118,690 (of which portion was estimated due to lack of returns) at the date of commencement of the winding up.

24. In November 2011, the Revenue Commissioners served a notice pursuant to s. 214 of the Companies Act 1963, on the Company.

25. The Liquidator, in his affidavits, has identified from management accounts what he contends to have been a significant increase in the Company's trade creditors from €102,401 at 31st May, 2010, to €277,105 at the date of his appointment. He also refers to an increase from €152,709 as at 31st March, 2011, to the sum of €277,105 at the date of cessation of trade which was approximately five days prior to his appointment. Whilst Mr. O'Toole has attempted to explain the latter increase by reference to credit periods, it appears to me that there was, as a matter of probability, a significant increase in trade creditors in the months leading up to the commencement of the winding up.

26. Mr. O'Toole, whilst recognising the improper failure to make Revenue payments on an ongoing basis, has attempted both to justify the use of monies collected for the Revenue and the continuing trade of the Company, partly by reference to the firm belief that the Company could trade out of its difficulties by reference, *inter alia*, to increases in wedding bookings, and also the continuing discussions with BOSI and reports being made to HBC. He also specifically refers to an unexpected loss of trade during the very bad weather period in December, 2010.

27. Regrettably, it does not appear to me, taking those matters into account that on the undisputed facts that the Court could be satisfied that the directors acted responsibly in the last year of trading of the Company in continuing to trade the Company, effectively by using VAT collected from March 2010, and subsequent to October 2010, PAYE deducted from employees' wages. The context in which the Court must view the actions of the respondents includes the fact that the Company took over the trading of the hotel in January 2010, following the review by HBC of the trading of the hotel by Carlton Athy Hotel Ltd. in which, as Mr. O'Toole very fairly acknowledges, HBC had clearly set out that "[t]he Revenue are owed €430k and it is the payments to the Revenue that have been sacrificed in order to pay other creditors". Hence, the Company was commencing to trade a hotel business where, to the knowledge of the respondents, as directors of the Company, the prior company which traded the hotel had effectively only been able to continue paying trade creditors by using monies due to the Revenue Commissioners.

28. It appears an inescapable conclusion from the facts put before the Court that the respondents made a decision to use VAT and PAYE collected or deducted and due to the Revenue Commissioners for the purpose of financing the continued trading of the Company during a significant period prior to the presentation of the petition to wind it up. The service by the Revenue Commissioners of a s. 214 notice in respect of debts the Company was unable to pay must have made the respondents aware that the Company was insolvent. The Court, hence, in accordance with the views expressed previously in *Digital Channel Partners Ltd*. cannot be satisfied,

on all the facts put before the Court that the respondents, in determining that the Company should continue trading the hotel, and using monies collected for the Revenue to enable it to do so, acted responsibly in relation to the conduct of the affairs of the Company, even when considered in the context of their entire tenure as directors of he Company.

29. Accordingly, the Court is obliged by the mandatory terms of s.150 of the Act of 1990 to make the declaration of restriction, as sought.