Neutral Citation: [2014] IEHC 187

THE HIGH COURT

[2012 No.254 COS]

IN THE MATTER OF GERDANDO LIMITED (IN LIQUIDATION)

AND IN THE MATTER OF SECTION 150 OF THE COMPANIES ACT 1990

AND IN THE MATTER OF SECTION 56 OF THE COMPANY LAW ENFORCEMENT ACT, 2001

BETWEEN:

PETER DOHERTY

APPLICANT

AND

KARL DONOHOE, RUTH DONOHOE AND EDITH DONOHOE

RESPONDENTS

JUDGMENT of Mr. Justie Barrett delivered on the 1st day of April, 2014

1. This is an application for a restriction order under s. 150 of the Companies Act 1990, as amended, in respect of each of Mr. Karl Donohue, Ms. Ruth Donohue and Ms. Edith Donohue. The key issue arising in the case is the extent to which directors may be held liable in law when they rely on the advices and services of professional advisors.

2. Mr. Karl Donohue, Ms. Ruth Donohue and Ms. Edith Donohue were directors of Gerdando Limited at the date of commencement of its winding-up. Gerdando was incorporated on 2nd November, 1995. It was the proprietor of two 'Eddie Rocket's' restaurants in County Dublin. Gerdando sublet its lease in one of the restaurant premises to an operations company that is also in liquidation at this time. The liquidator of Gerdando has suggested in his affidavit evidence that there were two main reasons for the company's insolvency. The first was the failure of the operations company to pay rent to Gerdando during 2009. The second was a 'reorganisation' in 2008 of the corporate arrangements through which the restaurants were operated by the Donohues, the legitimate intention underpinning this reorganisation being that each restaurant business should be owned and operated by a separate company. It is claimed that this reorganisation was done in breach of the Companies Acts and the fiduciary duties of the Donohues as directors in that it entailed a distribution that was allegedly done in breach of s. 45 of the Companies (Amendment) Act 1983.

3. Under s. 150 of the 1990 Act, the court must grant the declarations sought in these proceedings unless satisfied that any of a variety of circumstances identified in s. 150(2) pertain, the relevant circumstances in this case being that each of the Donohues, insofar as application is made in respect of him or her, acted (a) honestly and (b) responsibly in relation to the conduct of the affairs of Gerdando and (c) there is no other reason why it would be just and equitable that an order under s. 150 should issue. In the course of the proceedings before the court it became apparent, and the court finds, that there is no issue as to the honesty of any of the Donohues and, apart from the issue of whether they acted responsibly in relation to the conduct of the affairs of Gerdando, there is no other ground on which a s. 150 declaration should issue against any of them. Thus the only substantive issue that survives for the court to consider, from a s. 150 perspective, is whether the Donohues acted responsibly in relation to the conduct of the affairs of Gerdando, in particular as regards the reorganisation that was effected in 2008.

4. Under the 2008 reorganisation, the undertaking of Gerdando was transferred to a company called Terenure Restaurants Limited, in return for which the latter company issued shares to Mr. Karl Donohue and Ms. Ruth Donohue in the same proportion as their shareholdings in Gerdando. This form of transaction is sometimes called a 'three-party swap' and, if done in accordance with the law, represents a tax efficient method of corporate reorganisation. As mentioned, it has been suggested that the 2008 reorganisation involved a breach of s. 45 of the 1983 Act. It is not necessary for the court in deciding the application now before it to decide whether in fact a breach of s. 45 occurred. Instead, for the reasons stated above, the court needs merely to decide whether the Donohues acted responsibly in effecting the reorganisation in the manner that they did. To this end, Mr. Donohue avers in his affidavit evidence that:

> *"As appears from the foregoing, the Respondents [the Donohues} sought to restructure the business ...but the manner in which that restructuring took place was devised by the Company's professional advisers. They also took steps to give effect to the Transaction ....The Applicant asserts ...that the other directors and I did not concern ourselves to ensure that the requirements of the Companies Acts were complied with. Neither I nor the other directors are experts in accountancy, tax law or company law. It is true that we sought to reorganise our companies in the most tax efficient manner possible. In order to do so, we engaged the services of appropriate experts to advise on all aspects of the Transaction. I say and believe that it was reasonable for us to assume that those experts were aware of all of the legal implications of the Transaction, that they would bring such implications to our attention and that they would structure the Transaction in such a way as to ensure compliance with all relevant legal obligations. If it is the case that the Transaction contravened provisions of the Companies Acts, that was never our intention and did not, I say and believe, arise as a result of any lack of honesty or responsibility on my part or on that of the Second or Third Named Respondents."*

5. It is perhaps worth noting in passing that an independent report of 29th June, 2012, produced, at the behest of the respondents, by Hughes Blake, a prominent firm of accountants, concludes in effect that the reorganisation done in February 2008 did not contravene s. 45 of the 1983 Act. The liquidator, however, contends the contrary to be true. The fact that such a *bona fide* divergence of opinion can arise between professional people greatly weakens, if it does not in fact completely undermine, the contention that, when it came to the reorganisation, any of the Donohues, none of whom are expert in law, accounting or taxation, failed to act responsibly in relation to the conduct of Gerdando's affairs.

Principles to be applied in section 150 applications
6. There is, if anything, a possible surfeit of judicial guidance on the criteria that are relevant to determining a s. 150 application. An early but significant contribution was made by Shanley J. in *La Moselle Clothing Limited (in liquidation) v. Soualhi* [1998] 2 I.L.R.M. 345, his observations having since been described by Hardiman J. in *In the Matter of Tralee Beef & Lamb Limited* [2008] 3 I.R. 347 at 358, as being, at least at that time, of "near canonical status". Shanley J.'s observations had previously been affirmed and expanded upon by the Supreme Court in *Re Squash (Ireland) Ltd* [2001] 3 I.R. 35, the court holding, *inter alia*, that it is important, in a s. 150 application, to have regard to the entire tenure of an individual as director of a company. Notably, in the context of the present proceedings all of the alleged wrongdoing springs from or otherwise relates to a single, albeit significant, event in Gerdando's history, namely the reorganisation of February 2008.

7. In his judgment in *La Moselle*, Shanley J. had, at p. 11, mentioned that the extent to which a director has or has not complied with the Companies Acts is a relevant factor when determining a s. 150 application. In the High Court decision in *Kavanagh v. Delaney* [2005] 1 I.L.R.M. 34 at 41, Finlay Geoghegan J. suggested that compliance by a director with the common law obligations of a director is also a relevant factor. In his above-mentioned judgment in what is now sometimes referred to as the *Tralee Beef* case, Hardiman J., at 358, indicated that he did not disagree with this 'amplification' by Finlay Geoghegan J., though he was concerned that no injustice should be wrought in that case as a result of the amplification being sounded therein for the first time. In truth it is somewhat difficult to see how a director could be held to have acted responsibly where he or she has complied with the Companies Acts but is in breach of his or her common law duties, though equally it is difficult offhand to see how a director could breach his or her common law duties where he or she is not guilty of any breach of, or exposed to any penalty under, the detailed and comprehensive code established by the Companies Acts. Be that as it may, the jurisprudence appears in any event to have further evolved, with Fennelly J. signalling in *Re Mitek Holdings Ltd* [2010] 3 I.R. 374 at 396 that it is important not to adopt a formulaic, standardised, 'tick the box' approach to determining s. 150 applications. Thus Fennelly J. emphasises "*the need to identify the issues that are important in the particular case*" and then continues:

> *"I would not be disposed to limit the matters to which regard should be had or to substitute standardised judicial criteria for the general words of the statute."*

8. Section 150 enjoins the court to have regard to whether an affected person has acted "*honestly*" and "*responsibly*" and also to consider whether there is any other reason why it would be *"just and equitable*" that a s. 150 order should issue. All of the quoted terms bear their ordinary meaning. As mentioned above, there are no 'honesty' or 'just and equitable' grounds arising in this case. In deciding whether the Donohues have acted responsibly the court may of course have regard to their obligations as directors, to general commercial practice and to prior case-law but perhaps more to anchor than to determine any decision of the court as to the responsibility or otherwise of their respective actions.

Reliance on professional advice
9. To what extent may a director of a small company be held liable for breaches of important but highly technical provisions of the Companies Acts in circumstances where that director is not expert in accountancy, tax or company law and has sought appropriate advice in relation to a proposed transaction from suitably qualified professional advisers and entrusted due completion of that transaction to them?

10. In *Coyle v. Callanan* [2006] 1 I.R. 447, a s. 150 application was made in respect of two directors of a company that had acted in breach of the financial assistance provisions contained ins. 60 of the Companies Act, 1963. O'Leary J. refused to make the declarations sought on the basis that the defendants had received express and specific legal advice that a breach of s. 60 did not arise from the transaction in issue in those proceedings. Per O'Leary J., at 451:

> *"The court was astonished to be supplied with an affidavit by the solicitor to the company ...indicating that while he raised the share purchase issue with the first respondent, his advice was that the proposed scheme was not contrary to s.60 of the Act of 1963. In looking at issues from time to time the best of legal advisers will overlook a problem. The court would understand such a lapse. What is more difficult to accept is that a solicitor having applied his mind to the issue would conclude that the scheme was not contrary to s.60. The court, however, accepts that the advice as described was tendered and though the matter was couched in terms of some doubt the basic advice appears to have been that the scheme was legal. That advice was wrong but the first and third respondents are entitled to rely on it for the purposes of defeating this application though not necessarily in proceedings under other enactments which operate on the basis of strict liability."*

11. In *Stafford v. O'Connor* [2007] IEHC 246, another s. 150 application, McGovern J. took a not dissimilar view where professional advice sought and tendered had not been against the completion of the transaction in issue in those proceedings. Per McGovern J., at 13:

> *"I am not entirely convinced that the company was solvent or had adequate distributable reserves to make the decision to purchase the first named respondent's share capital in the company for £130,000.00 a responsible decision. However there appears to have been some good reasons why she should be bought out in view of the long standing disagreements between her and the second named respondent. In any event I am satisfied that the respondents obtained proper professional advice in the matter and that this advice did not go against the completion of the transaction. In the circumstances I make no restriction order in relation to the respondents in respect of that issue. "*

12. English case-law also offers some relevant precedents. Thus, in *Re McNulty's Interchange Ltd. & Anor* (1988) 4 B.C.C. 533, an application by a receiver for the disqualification of the respondent as director of a limited company, Browne-Wilkinson V.-C. states at 535 that:

> *"The official receiver says that although Mr. McNulty was not aware that the company was insolvent when it was continuing to trade, he says that he ought to have been aware it was. I reject that allegation on the evidence before me. The evidence is that he was throughout advised by professional financial advisers. To suggest that somebody in those circumstances, who relies on the advisers, is in some way acting improperly, because he does not appreciate that his advisers is wrong, seems to me untenable."*

13. A perhaps slightly less 'director-friendly' precedent is offered by the case of *Re Ortega Associates Ltd (in liq.)* [2007] EWHC 2046, an application for the repayment of certain monies to a company. The English High Court was confronted with a situation in which a director had been advised by a solicitor to go along with the sale of a business in order to avoid committing an offence under the UK's proceeds of crime legislation. Per Deputy Judge Livesey, at para. 36:

"The fact that a director has taken advice will be a relevant and important factor to be taken into account when determining the validity of an allegation against him that he has acted in breach of his duties."

14. The general thrust of the above case-law suggests that where a director, acting in good faith, seeks comprehensive professional advice of suitably qualified advisors and in good faith acts in accordance with such advice as is tendered, that will generally suffice to prevent such director from later being the subject of a s. 150 or like order. Perhaps the only caveat to this broad principle is that where the courts are dealing with a director who is professionally qualified or who directs a large or quoted enterprise, more exacting standards of behaviour will typically be applied than those which fall to be applied in the instant case where the court is dealing with enterprising but professionally unqualified individuals who doubtless are competent in their own field of endeavour but who are not expert in matters of law, tax or accounting. For these last directors the above case-law suggests that it suffices that they seek to do what is right, that they entrust their legal, tax and accounting affairs to the care of suitably qualified professionals, and that they seek to conform fully with such advices as are tendered to them. Were the contrary to apply the result would be absurd. A director of a small enterprise who, as here, was unskilled in law, tax or accounting and who enlisted suitable professional assistance to ensure that his or her enterprise acted in compliance with applicable law and regulation would nonetheless suffer very serious sanction in the event of non-compliance. Were a director to suffer so, a question would surely arise as to whether there was any advantage to engaging professional advisors if the law was effectively going to set the value of their advices at nought. Moreover, the person who sought such advice would be placed in an impossible situation in which, despite a lack of knowledge of applicable law and regulation, he or she would have to contemplate and raise queries regarding every possible breach of laws or regulations about which he or she knew little or nothing. When a person engages a solicitor to transfer a piece of property to another, the solicitor is not given an exemption from liability in negligence if such person does not raise detailed legal queries in relation to the substance of the transfer deed. When a person consults a doctor, the law does not establish an exemption from liability in negligence for such doctor if his or her patient does not test the correctness of any such diagnosis as the doctor may proffer. When, as here, a director of a small company requests of suitably qualified professionals that they complete a certain transaction with the clear intention that the transaction be done in compliance with applicable law and regulation then, it seems to follow from the above case-law, that when a want of compliance is later identified such director ought not to be the subject of a s. 150 or like order, at least absent other circumstances which suggest him or her to be somehow blameworthy. In this case there are no such other circumstances arising.

Additional grounds raised

15. Certain further ancillary issues concerning the transaction were also raised in the pleadings. Thus questions were raised as to whether the distribution that was effected as part of the transaction matched the details in the transaction documentation, whether a particular inter-company loan formed part of the undertaking of Gerdando, and whether the assets of Gerdando were fully accounted for in the transaction. In his affidavit evidence the first-named respondent offers what appear on their face to be reasonable answers to the questions posed. There were inadvertent errors in the transaction documentation, there was what seems ostensibly valid reason to view the inter-company loan as part of Gerdando's undertaking, and certain errors in the accounting can it seems be remedied now without much ado. All of these additional issues appear to the court to be subject to the same legal vulnerability which it considers to afflict the entirety of these proceedings, namely that in giving effect to the transaction the respondent small-company directors, being unskilled in tax, accounting or law, relied in good faith on advice that was sought in good faith from, and tendered by, suitably qualified professional advisers. Thus the court does not consider that any of these ancillary issues, whether viewed in themselves or in the context of all of the issues raised, requires that a s. 150 order be forthcoming.

Refusal of declaration

16. For the reasons stated above, the court is not satisfied that it is required to make an order under s. 150 of the Companies Act, 1990, in respect of any of Mr. Karl Donohue, Ms. Ruth Donohue or Ms. Edith Donohue, and declines to do so.