Neutral Citation Number: [2007] IEHC 246

THE HIGH COURT

[2005 No. 350 COS]

IN THE MATTER OF GREENMOUNT HOLDINGS LIMITED (IN LIQUIDATION)
AND IN THE MATTER OF SECTION 150 OF THE COMPANIES ACT 1990 AND SECTION 56 OF THE COMPANY LAW ENFORCEMENT ACT, 2001

BETWEEN

JAMES STAFFORD AS LIQUIDATOR OF THE COMPANY IN THE WITHIN PROCEEDINGS

APPLICANT

AND

ANN O'CONNOR, SEAN CARBERRY, BARBARA CARBERRY, MICHAEL KELLY AND DARRAGH KELLY

RESPONDENTS

Judgment of Mr. Justice Brian McGovern delivered Tuesday 31st July, 2007.

1. This is an application brought by the liquidator of Greenmount Holdings Limited ("the Company") for a declaration that the respondents, being persons to whom chapter 1 of part VII of the Companies Act, 1990 applies, shall not for a period of 5 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 of formation of any company unless that company meets the requirements set out in sub.s (3) of s. 150 of the Companies Act, 1990 (as amended).

2. The company was incorporated on the 11th November, 1994. From the 11th November, 1994 until the 27th July, 2005 the Directors were the first and second named respondent. The first respondent resigned as director on the 12th November, 2004. The third named respondent was appointed a director on the 12th November, 2004. The second and third named respondents resigned as directors on the 27th July, 2005 on which date the second named respondent sold his interest in the company to the fourth named respondent. The fourth named respondent was at the time an undischarged bankrupt. Subsequently the fifth named respondent became a Director.

3. These proceedings only concern the first, second and third named respondents. The fourth and fifth named respondents have already submitted to a restriction order.

4. Background.

The company was incorporated on the 11th November, 1994. The company operated serviced office facility under the trade name "Executive Suites" at the Harcourt Centre, Dublin 2 on a short term licensed basis. The company leased the premises from Damovo. The company had sufficient space to offer 22 offices available for rent at any one time. On the date of the appointment of the official liquidator 17 offices were occupied by licensees or tenants. Three were vacant and two were occupied by companies related to either the first or second named respondent. One of the company's key tenants which occupied seven of the offices on the third floor had given notice to vacate the premises from October, 2005.

5. The company also owned an apartment in the International Financial Services Centre as an investment property. This was sold by the liquidator following his appointment. The company became insolvent and the liquidator was appointed on the 21st September, 2005 pursuant to a petition presented by Damovo Ireland (Limited) on 30th July, 2005

6. For some years prior to the commencement of the winding up relations between the first and second named respondents broke down. The last set of audited accounts filed in the Companies Registration Office was for the year 30th June, 2000. Due to the breakdown of relations between the first and second named respondents no further audited accounts were prepared by the company. The first and second named respondents blamed each other for this. The first named respondent says that she attempted to ensure that books and records were prepared at all times and made every effort to rectify the deficiencies. She said that she employed Farrell Grant Sparks at her own expense in order to bring the books and records up to date prior to her resignation as a Director in November, 2004. From the time it commenced trading the company employed a Book Keeping firm, G.M. Financial Services, to write up the books and financial records on a monthly basis. The company also employed Mr. Gerard T. Murphy to audit the company's accounts. The first named respondent says that in 2002 in emerged that no day to day book keeping was carried out and she was informed that Mr. Gerard T. Murphy refused to accept the figures of Mr. Gerry Doyle, the person responsible for preparing the monthly accounts. For that reason Farrell Grant and Sparks were employed by her to bring the company books up to date. There were disputes between the first and second named respondent over the second named respondent's removal of books and records of the company from the possession of Farrell Grant and Sparks. In mid 2002 the first named respondent discovered that Mr. Murphy had forged her signature on accounts submitted to the Companies Registration Office and to the Revenue Commissioners. She made a complaint to the ICAI which was upheld and Mr. Murphy was severely reprimanded and fined. At a board meeting on the 10th March, 2003 Mr. Murphy was dismissed as auditor of the Company and Oliver Freeney & Company were appointed auditors. A dispute arose as to the level of fees claimed by Mr. Murphy and he refused to hand over the books and records to the new auditors. The first named respondent says that she personally discharged the bill of Farrell Grant Sparks from her own funds and she engaged the services of a former employee of the company to assist in this task.

7. The second named respondent says that in March, 2002 he became concerned with a number of issues which were brought to his attention by the company auditors. These issues concerned the payment by the company of a sum of money to a Polish company in which neither the company nor he had any involvement but in which the first named respondent had an interest. He was also concerned about the withdrawal of monies by the first named respondent from the company's Visa account and the transfer out of the company's bank account of a sum of money on foot of a bank transfer form which purported to contain his signature but he did not sign. As a result of the disagreements between the parties the second named respondent commenced s.205 proceedings.

8. It is clear that the major factor precipitating the insolvency of the company was the diminishing rental income being obtained by the company for the executive suites coupled with a rent review which significantly increased the annual rent which the company was required to pay to the Damovo. After the rent review took place there were also substantial arrears of rent to be paid.

9. It seems that the third named respondent's role in the company was rather passive. She is the wife of the second named respondent and it was suggested that she was appointed as a director to "make up the numbers". For her part she accepts that she played no role in the day to day management of the affairs of the company but she did discuss Company matters with her husband from time to time. She had replaced the first named respondent as director. When the first named respondent resigned as director she was paid by the company the sum of €130,000.00 on foot of an agreement of the 15th November, 2004.

10. The Applicant's Case.

The applicant submits that there are seven issues which the court ought to consider in determining whether the first, second and

third named respondents acted responsibly during their tenure as directors of the company. These are:

> (a) Whether the directors in general and the first and second named respondents in particular, properly functioned as a board of directors and if not, whether any negative consequences were caused to the company by this;
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> (b) Whether the respondents ensured that the company maintained proper books of accounts;
>
> (c) Whether the decision of the first, second and third named respondents to procure the company to purchase the first named respondents share capital in the company for €130,000.00 was a reasonable decision and a transaction that was in the best interest of the company;
>
> (d) Whether the decision of the second and third named respondents to transfer control of the company to the fourth named respondent was a responsible decision;
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> (e) Whether the first named respondents decision to procure the company to issue invoices to the Polish company, Genyslabs, was a responsible decision; and
>
> (f) Whether the third named respondent adequately discharged her duties as a director of the company.

11. The court was referred to the decision of Shanley J. in *Le Moselle Clothing Limited v. Souhali* which set out the criteria which the court can have regard to when considering whether a director acted responsibly during his tenure. At page 352 Shanley J. said:

> "Thus it seems to me that in determining the "responsibility" of a director for the purposes of s. 150(2)(a) the court should have regard to:
>
> > (a) The extent of which the director has or has not complied with any obligations imposed on him by the Companies Act, 1963 – 1990.
> >
> > (b) The extent to which his conduct could be regarded as so incompetent as to amount to irresponsibility.
> >
> > (c) The extent of the director's responsibility for the insolvency of the company.
> >
> > (d) The extent of the director's responsibility for the net deficiency in the assets of the company disclosed at the date of the winding up or thereafter.
> >
> > (e) The extent to which the director, in his conduct of the affairs of the company, has displayed a lack of commercial probity or want of proper standards."

In *Kavanagh v. Delaney (Re: Tralee Beef & Lamb Limited*) (Unreported, High Court, Finlay Geoghegan J. 20th July, 2004) the learned judge stated that at common law directors owe duties to the company which are normally divided into duties of loyalty based on fiduciary principles developed initially by the Courts of Equity and duties of skill and care developed by the common law courts from the in the law of negligence. Finlay Geoghegan said that:

> "Accordingly, it appears to me that when considering the matters referred to by Shanley J….under paragraph (a) the court should have regard not only to the extent to which a director has or has not complied with any obligation imposed on him/her by the Companies Acts but also with duties imposed by common law."

In that case she cited with approval the remarks of Jonathan Parker J. in Re: Barings plc and Others (No. 5) Secretary of State for Trade and Industry the Baker and Others where he said:

> "Each individual director owes a duty to the company to inform himself about [The Company's] affairs and to join with his co-directors in supervising and controlling them."

She also referred to three general proposition which Jonathon Parker J. derived from earlier authorities. These are as follows:

> "(i) Directors had, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company's business to enable them properly to discharge their duties as directors.
>
> (ii) Whilst directors were entitled (subject to the articles of association of the company) to delegate particular functions to those below them in the management chain, and to trust their competence and integrity to a reasonable extent, the exercise of the power of delegation did not absolve a director from the duty to supervise the discharge of the delegated functions.
>
> (iii) No rule of universal application can be formulated as to the duty referred to in (ii) above. The extent of the duty and the question whether it has been discharged, depended on the facts of each particular case, including the director's role in the management of the company."

12. The applicant contends that the respondents failed to properly function as a board of directors. There is no doubt that this is true as, unhappily, differences arose between the first and second named respondents which led to litigation and also lack of communication. I am satisfied that the company failed to maintain proper books and records as required by s. 202(1) of the Companies Act, 1990. The last audited accounts prepared in respect of the company were for the year ending 30th June, 2000. While draft accounts were prepared for succeeding years ending 30th June, 2001, 2002 and 2003 these accounts were not approved.

13. As a result of the failure to keep proper books of account it was not possible at any time after the 30th June, 2000 to enable the financial position of the company to be determined with reasonable accuracy.

14. The respondents do not deny that audited accounts were not prepared between 2001 and 2004 and that proper books of account were not kept but seek to explain why this was so. The first and second named respondents maintain that it was due to the ongoing disputes between them that it was not possible to have the accounts prepared. It is not possible for this court to determine which of the respondents is personally responsible for the failure to ensure that the company produced audited accounts after the year ending 30th June, 2000 and the failure to maintain proper books of account. The applicant argues that the directors are under an individual

and collective duty to supervise the company's affairs and that the respondents were in breach of that duty.

15. The sale of the first named respondents shares to the company.
The applicant contends that this decision was irresponsible and not in the best interest of the company because the company was insolvent at the time. Furthermore, the applicant contends that at the time of the transaction the company had inadequate distributable reserves to fund the payment. The agreement to pay the sum of €130,000.00 was made on the 15th November, 2004. The applicant contends that there was substantial trading loses at that time and that a review of the company's trading operations between 31st July, 2003 and November, 2004 would have shown further trading loses. On the 27th July, 2004 the company's landlord raised an invoice in the sum of €167,424.54 for back rent for the period 8th May, 2003 to 8th August, 2004 following on a rent review becoming operative. This raised serious questions as to the company's ability to continue trading. The respondents say that they got expert advice on the matter. The first named respondent says that she had legal advice from Messrs. William Fry and the second named respondents says that he obtained independent legal advice from Messrs. Arthur P. McLean & Company, William Fry Solicitors and Gerard T. Murphy and Oliver J. Freeney & Company. At no stage did any of these professionals call into question whether or not the company had sufficient reserves and cash in the back to finance the buy back of shares. The second respondent points out that in fact Mr. Pauraic Ward of Oliver Freeney & Company stated on the 5th November that:

> "The company will have sufficient reserves and cash at Bank to finance the buy-back of the shares."

The second named respondent points out that the liquidator has not taken steps to recover the sum of €130,000.00.

16. "Abandonment" of the Company by the second named respondent.
On the 27th July, 2005 the second named respondent sold his interest in the company to the fourth named respondent €1.00. The fourth named respondent was an undischarged backrupt. At this time the company was engaged in a long running dispute with its landlord Damovo (Ireland) Limited regarding the rent arrears due. It appears as the fourth named respondent was an undischarged backrupt he asked his son, the fifth named respondent to become a director of the company. Cleary the fourth named respondent could not be appointed a director as he was an undicharged bankrupt but the applicant contends that he was a shadow director of the company. Furthermore significant sums of rent under the terms of the rental review had accrued. The company's auditors were due to be paid and the company was having difficulty selling the apartment which was an investment property. The applicant argues that the company was insolvent and the second named respondent acted in an irresponsible way in disposing of the company in this matter. The second named respondent complains that the applicant as looking at the transaction with the benefit of hindsight and that he is not permitted to do this. See *Business Communications Limited v. Baxster* (Unreported, High Court, Murphy J. 21st July, 1995). In an affidavit sworn on the 14th December, 2006 the second named applicant says that:

> "I say that in mid July, 2005 I commenced negotiations with Mr. Michael Kelly, a personal friend of mine for many years. I knew that Mr. Kelly had been made a bankrupt but was informed by Mr. Kelly and believed that he was in the process of being discharged from bankruptcy. I say that Mr. Kelly volunteered Damovo the landlord of the leasehold premises, and reported to me that he believed he could negotiate a deal with Damovo which would lead to a long term survival of the company. As my relationship with Damovo had become strained, due to many continued attempts to settle the arrears of rental issue and the company's continual inability to make a capital payment, I believed that it would be preferable if Mr. Kelly took over the negotiations on the company's behalf and consequently I transferred by shareholding to Mr. Kelly's son for €1.00 and both my wife, Barbara Carberry and I resigned as directors. Subsequently I was informed by Mr. Kelly and believed that he had negotiated a deal with Damovo but later he informed me that Damovo had resiled from their position, he believed due to communications which had been made to Damovo by Mrs. O'Connor."

17. The position of the third named respondent is that she appears to have been a passive director who was appointed to replace the first named respondent. The applicant maintains that as a director she had a duty to take all steps to preserve the assets of the company for the benefit of the creditors.

18. Issuing of invoice to Genyslabs.
It is alleged that the first named respondent had an interest in Enterprise Holdings, a business in Warsaw, Poland which operated serviced offices. It is contended by the applicant that the company facilitated a client at Enterprise Holdings to evade tax, without the knowledge of the second named respondent. The client in question was Genyslabs which did not want to deal directly with the Polish company but required an agreement with an EU based company for tax purposes. The applicant alleges that this request was facilitated by the first named respondent by issuing, or causing to have issued, through the company, a rental agreement for signature by the directors of Genyslabs together with invoices for rent of an office in Warsaw which it did not own. No corresponding licence agreement was put in place between Enterprise Holdings and the company nor, where invoices received from Enterprise Holdings. The invoices were issued to Genyslabs by the company and were not recorded by the company in its books or records and the applicant contends that this transaction was entered into purely for the benefit of the first named respondent's other business interests. The first named respondent refutes the allegation and points out that the applicant has never produced the alleged false invoices or any evidence that they issued.

19. Findings and Conclusions.
Having regard to the authorities which have been opened to me I determine the responsibility of the respondents as follows:-

> (i) I find that the respondents failed to maintain proper books of account as required by s. 202 of the 1990 Act and failed to file audited accounts beyond the 30th June, 2000. I accept that the first and second named respondents were in dispute with each other for this period and that it is not possible for the court to resolve the issues between the parties in this motion. There is sufficient evidence from the first and second named respondents to establish that they were making some attempts to regularise the situation and that their attempts to do so were impeded by the disputes between them and the litigation brought under s. 205 of the Companies Acts. In the circumstances I do not find sufficient grounds to make a restriction order with regard to the first and second named defendants on this issue. It seems to me that the third named respondent was only a director for a short period of time (14th November, 2004 – 25th July, 2005) and while she was in breach of her duties to the company I am satisfied that she was not is a position to alter events in the circumstances that arose and I make no order restricting her on the basis of this ground.
>
> (ii) While I am satisfied that the respondents failed to properly function as a board of directors I make no order restricting them in connection with that failure for the reasons set out at paragraph (i) above.
>
> (iii) 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.

(iv) I am satisfied that at the time when the second named respondent took a decision to sell the shares in the company to Michael Kelly for €1.00 the company was insolvent. Although the third named respondent had a legal responsibility in regard to this decision it seems that effectively she was not part of the decision and the evidence suggest that the decision was made by the second named respondent. Accordingly I make no order restricting the third named respondent in respect of that action.

(v) However I find that the action of the second named respondent in disposing of the shares of the company in those circumstances and to an undischarged bankrupt was irresponsible and militated against an orderly winding down of the company's affairs in circumstances where the company was no longer viable. I find that in taking such action the second named respondent acted in a manner which would amount to a "lack of commercial probity". On that basis I make a restriction order in respect of the second named respondent in the terms of paragraph 1 of the notice of motion for a period of 5 years.

(vi) I am somewhat concerned about the allegation against the first named respondent concerning the issuing of false invoices to Genyslabs. If this allegation were proved it is obviously a serious matter. However it is denied by the first named respondent and the evidence in respect of the allegation is not sufficient to enable me to make a restriction order against the first named respondent on that account.