THE HIGH COURT

2006 No. 132 COS

IN THE MATTER OF METAFILE LIMITED
AND IN THE MATTER OF THE COMPANIES ACTS, 1963 – 2005
AND IN THE MATTER OF AN APPLICATION UNDER
SECTION 213(f), 213(g)

BETWEEN/

COLMAN GARVEY

PETITIONER

AND
METAFILE LIMITED

RESPONDENT

Judgment of Miss Justice Laffoy delivered on 20th December, 2006

The factual background

1. Metafile Limited (the Company) was incorporated on 26th October, 1995. The objects for which it was established are set out in Clause 2(1) of its memorandum of association, which contains a number of components. First, the Company was established to carry on all or any of the businesses of –

> "… manufacturers, designers, importers, exporters, buyers, sellers (whether by wholesale or retail), storers, warehousers, distributors and suppliers of and dealers in goods and articles of every description (whether consumable or otherwise) and whether for domestic, industrial, commercial or agricultural use …"

2. Secondly, it was authorised to carry on a comprehensive range of specified businesses. In order to illustrate how comprehensive that range was, it is only necessary to record that, while it did not include the business of candlestick maker, it did include the businesses of butchers and bakers in addition to hairdressers and glaziers. Thirdly, it was authorised to carry on any business which might seem to the Company capable of being conveniently carried on in connection with the previously mentioned businesses or calculated directly or indirectly to enhance the value or render more profitable any of the Company's properties or rights. Fourthly, it was authorised to carry on the business of property investments and dealers in property (whether real or personal) of every description. Although this fact was not alluded to in the course of the submissions by counsel, it is obvious that the Company was incorporated as a shelf company rather than with a specific enterprise in mind.

3. A Shareholders' Agreement was entered into on 6th December, 2000 between the persons who had subscribed for ordinary voting and non-voting shares in the Company, including the petitioner, who, at the time, was the holder of 60 ordinary voting 'A' shares, and Maurice Coveney (Mr. Coveney), who was then the holder of 240 ordinary voting 'A' shares and also non-voting 'B' shares. The type of business which the Company was to embark on was set out in Clause 4.02 of the Shareholders' Agreement as follows:

> "The business of the Company shall be the manufacturing and production and sale of various steel products to include fire escapes, stairways, fire exits, industrial approach tables, heavy duty motorised conveyors, spectacle blinds, piping spools, vessels, trays, passenger handling facilities and such other activities as shall be agreed upon between the parties hereto from time to time and all other business the Company is empowered to carry out by virtue of its Memorandum of Association."

4. The Shareholders' Agreement, in Clause 4.05, contained provisions under which, in the event of a shareholder wishing to dispose of all of his shares other than to certain designated family members, the other shareholders would have a right of pre-emption at an agreed price or, alternatively, at market value as fixed in accordance with the provisions set out therein. Clause 5.01 dealt with the consequences of a shareholder having gone through the procedure outlined in Clause 4.05 and within the period of three months after the expiration of the time frame allowed for such procedure being unable to dispose of his shares to any outsider: that shareholder and the other shareholders should co-operate in taking the Company into voluntary liquidation and appointing an independent liquidator with a view to a disposal of the assets of the Company and distribution of the proceeds of sale.

5. The Company never carried on the type of manufacturing business envisaged in the primary objects set out in a memorandum of association and in the Shareholders' Agreement. An associated company (using that term in a non-technical sense), Carrig Engineering Services Limited (Carrig), carried on the business of mechanical engineering contractors. The shareholders and the proportion of shares held by them in the Company and in Carrig were identical. The Company was the owner of the factory premises and the other fixed assets from and with which Carrig conducted its business. Mr. Coveney has averred that this structure was adopted to avail of a BES Scheme.

6. According to the petitioner, tensions between him and the other members of the Company developed as long ago as May, 2003. In June, 2003 he invoked the provisions of Clause 4.05 of the Shareholders' Agreement. However, the process provided for in Clause 4.05 and Clause 5.01 was not followed through.

7. In early 2005 the petitioner went off on a different tack. He threatened to bring petitions to this Court in relation to both the Company and Carrig seeking relief under s. 213 and s. 205 of the Companies Act, 1963 (the Act of 1963). By a settlement agreement dated 3rd March, 2005 (the Settlement) the petitioner, on the one hand, and Carrig, the Company and Mr. Coveney, on the other hand, agreed to settle all their disputes and differences on terms, including the following:

> (a) the petitioner acknowledged that his employment with Carrig had ceased on 28th February, 2005 and Carrig agreed to pay him the sum of €30,000 by way of compensation for the termination of his employment;
>
> (b) the petitioner agreed to transfer his entire shareholding in Carrig and the Company to those companies for a total consideration of €126,000;
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> (c) the petitioner resigned as a director and secretary of the Company and Carrig; and
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> (d) the Settlement was conditional on the closing of a then pending sale by the Company of its premises in accordance with a contract for sale dated March, 2005, and, in the event that such sale should not be completed by 15th June 2005, the Settlement should be null and void save that Carrig should pay to the petitioner the sum of €30,000 by way of

compensation for the termination of his employment.

8. The sale by the Company was not completed on 15th June, 2005, so that the provisions of the Settlement, other than the provision for payment of €30,000 by Carrig to the petitioner, became defunct.

9. On 16th June, 2005 the petitioner issued a demand pursuant to s. 214 of the Act of 1963 to Carrig for payment of the sum of €30,000 due to him. The demand was not met. The petitioner then presented a petition to this Court on 27th July, 2005 to have Carrig wound up by the court. On 24th August, 2005 a winding up order was made by Herbert J. on foot of a petition (2005 No. 284 COS).

10. As regards the Company, a sale of the factory premises was subsequently completed. The only asset the Company now has is the proceeds of that sale. The Company has no employees and it does not trade. It is solvent and has no creditors.

11. On 20th February, 2006 an extraordinary general meeting of the Company was held on the petitioner's requisition at which the petitioner proposed that the Company be wound up by way of a members' voluntary winding up and that Mr. Carl Dillon FCA be appointed liquidator. While the majority of the votes cast (61.5%) supported the resolution to wind up, that majority fell well short of the 75% majority required to pass the necessary special resolution under the Act of 1963. Following that meeting, the petitioner's solicitors wrote to the Company's solicitors advising that a petition would be brought if the directors of the Company did not take steps to convene and extraordinary general meeting for the purpose of its winding up within fourteen days. The directors did not oblige.

12. This petition was issued on 13th April, 2006.

13. The current position is that, on my calculations, the petitioner owns 42.9% of the issued voting shares of the Company. Mr. Coveney is a director of the Company and, on my calculations, he is the holder of 21.9% of the issued voting shares in the Company.

The petition and the response thereto

14. The petitioner brings the petition as a contributory of the Company. He has invoked paragraphs (f) and (g) of s. 213 of the Act of 1963, as amended. However, it was made clear in the petition and on the hearing of the petition that the sole basis on which the petitioner was grounding his entitlement to relief was that there has been a failure of substratum consequent on the winding up of Carrig and the sale of the factory premises by the Company.

15. The petition has been resisted by the Company primarily on the basis that there has been no failure of substratum. In response to the petition, Mr. Coveney, the managing director of the Company, averred that the Company wishes to continue to trade with a view to suing the petitioner for alleged breach of his fiduciary duties to the Company. Mr. Coveney's affidavit contains a litany of actions alleged to have been taken by the petitioner which he contended support his claim that the petitioner breached his fiduciary duties to the Company. While it would not be appropriate to express any view on those allegations on the basis of mere affidavit evidence, I do not consider it inappropriate to comment that there is a lot of substance in the response of the petitioner that, if the alleged breaches deposed to by Mr. Coveney were in fact true, the cause of action in relation to them would rest with Carrig, which is in liquidation, not with the Company. In any event, apart from its avowed intention to pursue the petitioner for the alleged breach of fiduciary duty to the Company, Mr. Coveney has averred that he and his fellow directors have yet to decide how the Company will proceed from hereon with the benefit of the proceeds of sale of the "main asset".

16. The Company contended that it would not be just and equitable that it be wound up on foot of this petition. It was submitted on its behalf that there are other avenues open to the petitioner to realise the value of his shareholding. That argument does not carry much weight, given the petitioner's experience when he invoked Clause 4.05 of the Shareholders' Agreement in 2003 when, he contended, Mr. Coveney did not engage with him or make any serious effort to assist in realising his shares, and given also the outcome of the Settlement.

The core issue

17. It seems to me that the core issue on this petition is whether there has been a failure of substratum.

Failure of substratum: the law

18. As is pointed out in Courtney on *The Law of Private Companies*, 2nd Edition, at para. 25.087, since the advent of the ability to alter a company's objects clause, the failure of a substratum ground as a basis for a petition to wind up the Company has become somewhat anachronistic. That point is enforced where, as here, the objects clause has been drafted in the broadest possible terms. In fact, I have not been referred to any Irish case in which that ground was relied on.

19. In *Re Kitson & Co. Ltd.* [1946] 1 All E.R. 435, Lord Greene M.R. rationalised the substratum ground in the following passage of his judgment at p. 438:

> "It must be remembered in these substratum cases that there is every difference between a company which on the true construction of its memorandum is formed for the paramount purpose of dealing with some specific subject-matter and a company which is formed with wider and more comprehensive objects. I would explain what I mean. With regard to a company which is formed to acquire and exploit a mine, and, accordingly, if the mine cannot be acquired or if the mine turns out to be no mine at all, the object of the company is frustrated, because the subject matter which the company was formed to exploit has ceased to exist. It is exactly the same way with a patent, as, in the well known *German Date Coffee* case. A patent is a defined subject matter, and, if the main object of a company is to acquire and work a patent and if it fails to acquire that patent, to compel the shareholders to remain bound together in order to work some other patent or make some unpatented article is to force them into a different adventure to that which they contracted to engage in together; but, when you come to subject matter of a totally different kind like the carrying on of a type of business, then so long as the company can carry on that type of business, it seems to me that prima facie at any rate, it is impossible to say that the substratum has gone."

20. In that case, Kitson & Company had been incorporated in 1899. The first object set out in its memorandum of association was to acquire and take over as a going concern a business known as "Kitson & Company" and all or any of its assets and liabilities. Its second object was to carry on the business of locomotive engine manufacturers, iron founders etc. As a matter of construction, Lord Greene held that the main and paramount object of the company was to carry on an engineering business of a general kind, and the memorandum did not limit that paramount object or restrict the contemplated venture of the shareholders to the carrying on of the business of Kitson & Co. Although the business of Kitson & Co. which had been acquired 46 years previously was sold in 1945, it was held that this did not amount to a destruction of the substratum of Kitson & Company Limited. The Court of Appeal dismissed the

petition to wind up.

21. The decision in the *Kitson* case was distinguished by the Chancery Division of the English High Court in *Re Perfectair Holdings Limited* [1990] BCLC 423. There are undoubtedly similarities between that case and this case. The company which it was sought to liquidate was a holding company which held property. The business was carried out through a wholly-owned subsidiary which traded out of that property. In order to resolve a dispute between the shareholders, it was agreed that one faction would purchase the shares of the subsidiary, the holding company would sell the property and then the holding company would be put into liquidation. The shares in the subsidiary were sold in accordance with the agreement, as was the property of the holding company. Thereafter the assets of the holding company consisted of cash. One faction sought to have the holding company wound up. This was resisted on the basis that it had a pending action for damages against the subsidiary and that the prosecution of this claim constituted a justification for keeping the holding company in existence. Having referred to the *Kitson* case and *Re Taldua Rubber Company Limited* [1946] 2 All E.R. 763, Scott J. stated (at p. 434):

> "It is not clear that either of the companies involved in the two cases was, so to speak, a partnership company such as the company in the present case undoubtedly was. But nevertheless I accept the general principle set out in those cases. The memorandum of any company to which the loss of substratum argument as a ground for winding up is to be applied must be construed. If when construed there are some commercial activities that the company is capable of discharging consistently with its memorandum and if some members of the company want that commercial activity to be pursued by the company, *prima facie* at least, there is no more to the case than that, the just and equitable ground will not have been made out.
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> Of course, if three-quarters or more of the shareholders want the company wound up, they do not need to come to court and ask for a winding up order. They can put the company into voluntary winding up by means of a resolution passed at a general meeting."

22. However, Scott J. stated that the case before him had features which distinguished it from the two cases to which he had referred. He found that it had been common ground ever since the sale of the subsidiary that the holding company would never again engage in any commercial activity whether by way of holding assets or subsidiaries with a view to profit or by way of carrying on business on its own account. On the basis of those facts, he stated as follows (at p. 345):

> "So this is a case where, although the company stands possessed of a substantial amount of cash and has the money to go back into commercial activity if the majority so desires, that is not the position. The majority does not so desire. Even since the conclusion of the 'heads of agreement' the majority has been content and perhaps determined to get in all the assets of the company, realise all the assets, have them reflected in cash and wind up the company. All of that, in my judgment, is a process of liquidation.
>
> Counsel for the respondents said, and correctly said, that the sale of property and the bringing of actions is part of the normal business of an incorporated company. So it is. The sale of property and the prosecution of actions is for all companies, I would think, a legitimate ancillary purpose, ancillary to its principal objects. A trading company litigates to get in debts. It litigates for a variety of other reasons for the purpose of enhancing or protecting its principal object, its trading activity. A holding company does likewise for the purpose of protecting its assets that it holds for profit. The distinction between cases like that and the present case is that it is not for the purpose of any trading object that the assets of Holdings were being realised, that the action against Perfectair is being prosecuted. All of this has taken place and is taking place for the purpose of liquidation."

23. Referring to the second paragraph in the above passage, counsel for the petitioner submitted that the position is the same here. In my view, it is not. When the Settlement was entered into, while the only asset of the Company was already in the course of being sold, it was clearly envisaged that the petitioner's stake in both Carrig and the Company would be bought out. Taking the Settlement at face value, it was not envisaged that either Carrig or the Company would be wound up. Subsequently, Carrig was wound up at the instigation of the petitioner with a view to recovering the debt owed by it to him. Here the sale of the Company's asset and the winding up of Carrig were not part of an arrangement under which the Company was ultimately to be wound up. Accordingly, in my view, the position here is not analogous to the situation with which Scott J. was dealing and there is no basis for adopting the approach he adopted on the facts of this case.

Conclusions

24. The resolution of the core issue turns on the construction of the shareholders' contract with the Company and *inter se*.

25. As a matter of construction of the memorandum of association of the Company, whether standing alone, or read by reference to clause 4.02 of the Shareholders' Agreement, the paramount purpose for which the Company was incorporated was to carry on a manufacturing business of a general kind. The fact that the members carried on a mechanical engineering contractor's business through the medium of Carrig does not take from the fact that the Company can carry on the type of manufacturing business envisaged in its memorandum. That being the case, in my view, it cannot be said that the substratum has gone. Indeed the Shareholders' Agreement expressly provided for the Company carrying on such other activities as should be agreed between them from time to time and all other business which the Company was empowered to carry out under its Memorandum of association.

26. On the basis of that conclusion, the petition must be dismissed. I must come to that decision, notwithstanding a strong sense that there is no element of common sense or commercial reality behind the stance which the Company has adopted.

Order

27. There will be an order dismissing the petition.