THE HIGH COURT

[2014 No. 168 COS]

IN THE MATTER OF THE COMPANIES ACTS 1963-2012 AND IN THE MATTER OF PELKO HOLDINGS LIMITED AND IN THE MATTER OF PELKO LIMITED

JUDGMENT of Mr. Justice Hogan delivered on 28th April, 2014

1. Where it is plain that the petitioning company is unable to pay its debts and that it has a reasonable prospect of survival, in what circumstances – other than misconduct on the part of the officers or lack of candour in the course of the making of the application – should the court decline to exercise its jurisdiction to appoint an examiner to that company under s. 2 of the Companies (Amendment) Act 1990 ("the 1990 Act")? This is essentially the issue which is presented here.

2. There is no doubt at all but that Pelko Ltd. ("Pelko") is insolvent. It is equally clear that, if admitted to examinership, it has a reasonable prospect of survival. The major creditor, Bank of Scotland, maintains that the present application is, however, premature and that the court should decline to exercise its jurisdiction on that ground, not least having regard to the further consideration that the costs of the examinership are likely to be excessive and disproportionate.

The extent of the court's discretion under s. 2 of the 1990 Act

3. Section 2 of the 1990 Act (as amended) provides in relevant part:

> "(1) Subject to sub-section 2, where it appears to the court that –
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> (a) a company is or is likely to be unable to pay its debts, and
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> (b) no resolution subsists for the winding-up of the company, and
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> (c) no order has been made for the winding-up of the company,
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> it may, on application by petition presented, appoint an examiner to the company for the purpose of examining the state of the company's affairs and performing such duties in relation to the company as may be imposed by or under this Act.
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> (2) The court shall not make an order under this section unless it is satisfied that there is a reasonable prospect of survival of the company and the whole or any part of its undertaking, as a going concern.
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> (3) For the purposes of this section, a company is unable to pay its debts if—
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> (a) it is unable to pay its debts as they fall due,
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> (b) the value of its assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities, or
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> (c) section 214 (a) or (b) of the Principal Act applies to the company.
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> (4) In deciding whether to make an order under this section the court may also have regard to whether the company has sought from its creditors significant extensions of time for the payment of its debts, from which it could reasonably be inferred that the company was likely to be unable to pay its debts."

4. It is clear from the language of s. 2(1) and s. 2(2) that the court has no jurisdiction to appoint an examiner save where the essential jurisdictional requirements of these provisions have been satisfied. The Court cannot appoint an examiner save where it is satisfied as to the actual or prospective insolvency of the petitioner (s. 2(1)(a)) and it is positively precluded ("…shall not make an order…") from appointing an examiner (s. 2(2)) unless it is clear that the company (or some part of it) has a reasonable prospect of survival. Subject to this, s. 2(1) is permissive ("…may…appoint an examiner"). Indeed, the contrast between the permissive "may… appoint" in s. 2(1) and the positive prohibition of "shall not" in s. 2(2) underscores the discretionary character of s. 2(1).

5. This very point was made by Fennelly J. in *Re Gallium Ltd.* [2009] IESC 8, [2009] 2 ILRM 11:

> "A petitioner does not, by getting over that threshold, acquire a right to have an order made. I still think it is fair to say that the section confers a "wide discretion" on the court, or alternatively, that the court should take account of all the circumstances. The establishment of *a reasonable prospect of the survival* merely triggers the power, which remains discretionary."

6. It is, I think, nevertheless true to say that in the vast majority of cases the courts have exercised the jurisdiction to appoint an examiner where these threshold requirements have been met. This is doubtless because of the public policy imperative of endeavouring to save as many viable outlets and businesses as possible. Yet it is equally clear that the court has a discretion not to make an order where creditors have been defrauded and where no real prejudice would otherwise be caused to the employees (*Re Missford Ltd.* [2010] IEHC 11) or where there has been a lack of candour on the part of the petitioner (*Re Wogans (Drogheda) Ltd.*, High Court, 7th May 1992, *Re Belohn Ltd. (No.2)* [2013] IEHC 157, [2013] 2 ILRM 407).

7. Nevertheless, the overall tendency of the courts has been to appoint examiners in the light of these policy objectives. As Clarke J. explained in *Re Traffic Group Ltd.[*2007] IEHC 445, [2008] 3 I.R. 253, 261:

> "It is clear that the principal focus of the legislation is to enable, in an appropriate case, an enterprise to continue in existence for the benefit of the economy as a whole and, of equal, or indeed greater, importance to enable as many as possible of the jobs which may be at stake in such enterprise to be maintained for the benefit of the community in which

the relevant employment is located. It is important both for the court and, indeed, for examiners, to keep in mind that such is the focus of the legislation. It is not designed to help shareholders whose investment has proved to be unsuccessful. It is to seek to save the enterprise and jobs.

It is as against that background that Costello J. felt [in *Re Seluwke Ltd.*, High Court, 20th December 1991] that the high prospects of saving a significant number of jobs outweighed the lack of candour displayed by the petitioners in *Selukwe*. It is also important to note that, in addition to the lack of candour displayed in *Wogans*, it is clear from the remainder of the judgment of Costello J., in that case that he was also motivated by what he perceived were significant deficiencies in the scheme then under consideration. In addition Costello J. characterised the scheme as one which was in reality a proposal for a new commercial enterprise whereby, in truth, the existing enterprise and existing jobs would have been written off.

It seems to me, therefore, that a court should lean in favour of approving a scheme where the enterprise, or a significant portion of it, and the jobs or a significant portion of them, are likely to be saved. That is not to say that the court should disregard any lack of candour or other wrongful actions. It does, however, seem to me that the courts approach to such matters should take into account the following.

Firstly it needs to be recognised that there may be cases where the wrongful actions of those involved in promoting the examinership are so serious that the court is left with no option but, on that ground alone, to decline to confirm a scheme which would otherwise be in order. It is necessary, as Costello J. pointed out in *Wogans*, to discourage highly wrongful behaviour.

However, in addition it seems to me that the court should consider the extent to which it may be possible (either by virtue of the provisions of the scheme as presented or modifications suggested by the court) to, as it was put by counsel for the petitioners, "neutralise" the effects of any such wrongful actions. The extent to which measures can be put in place to ensure that those who may have been guilty of a lack of candour or other wrongful action do not, themselves, benefit by it, is a factor to which significant weight should be attached. It is important, in my view, that in an appropriate case, examiners should have regard to such factors in formulating schemes for presentation to the court.

Where there is a high level of likelihood that the company can survive with a consequent saving of a significant enterprise and at least a significant proportion of the jobs at stake, the court should lean in favour of confirmation, especially if appropriate remedial measures can be put in place to mark and deal with the consequences of any lack of candour or other inappropriate action on the part of those charged with the management of the company."

8. It is with these principles in mind that I accordingly propose to consider the manner in which this discretion should be exercised.

The background to the application

9. Pelko is a quite typical small and medium enterprise which was incorporated in 1977. The company specialises in the manufacture and supply of high quality office and auditorium seating and furniture. Its clientele typically consists of large institutional purchasers, such as the Health Service Executive, Government Departments, Universities and banks. The company was profitable prior to the economic crash of late 2008. Since then – almost like every SME in the country – it has struggled as the business demand for its products plummeted. It was accordingly necessary for the company to reduce its cost base, reducing from 17 to 11 employees and restructuring its costs base. It managed to make a small profit in 2010 and 2011.

10. In this respect, the report of the independent accountant prepared by Ms. Myra Finnegan is extremely helpful. She has noted these developments and has commented that Pelko is "capable of benefitting from any improved trading improvements upcoming in the Irish market." If, however, an examiner is not appointed, then the likelihood is that the company will be placed into receivership in the not too distant future. The assets of the company are likely to be sold in order to pay down the company's debt and the 11 jobs are likely to be lost.

11. The principal difficulty facing the company remains, however, the unsustainable debt to Bank of Scotland of some €515,000. This is a debt which was generated from the acquisition of leasehold premises in North Wall, Dublin 1 in 2003, which is the company's current manufacturing base. In strictness, the lease has been transferred to Pelko Holdings Ltd. and Pelko itself is a wholly owned subsidiary of Pelko Holdings. There is, however, no formal lease between the two companies and Pelko discharges the payments under the facility letters. The application in relation to Pelko Holdings is made pursuant to s. 4(1) of the 1990 Act as a related company.

12. Bank of Scotland has a first fixed charge over the property, a floating charge over the assets of the companies and a guarantee from Pelko Holdings in respect of Pelko. The difficulty is that following the calamitous decline in commercial property values in recent times the property is now in substantial negative equity. While the property itself has been recently valued at €330,000, this was on the basis that the company had freehold title. A further complication, however, is that although the Circuit Court ruled in 2009 that Pelko could enlarge the leasehold to a freehold on payment of some €11,000, in the event this was not done at the time due to considerable trading difficulties experienced at that stage. If, however, appropriate funds could be found to enlarge the interest to a freehold this would enhance the value of the proprietary interest. At the moment, however, given that all that remains of the balance of a leasehold interest which will expire in 2045, the lease is valued at about €90,000.

13. Ms. Finnegan has further identified the problem with a sale is that Pelko are likely to be left with a substantial residue of debt to Bank of Scotland, along with the removal of Pelko from its current trading base. Pelko have, however, also located two other possible sites to which they might be able to move. She considers that that the companies have a reasonable prospect of survival provided in particular that the debt of Bank of Scotland and the other creditors are either partially written down or otherwise re-structured.

14. Here it may be observed that the loan from the Bank of Scotland expired as long as ago as 26th January 2013 and is presently in operation outside of agreed terms. The Bank "agreed to bear with the position" until 31st March 2014, subject to certain conditions. These conditions included the conversion of the leasehold interest to freehold title and the sale of the property at an auction of (largely distressed) properties at a reserve acceptable to the Bank. Moreover, the payments which the company has been able to pay have been interest only, with no reduction in the capital.

15. The other major creditor is the Revenue Commissioners who have adopted a neutral stance on this application. They are owed at least the sum of €37,520 in terms of arrears of taxes, but the full sum due may indeed be closer to €52,000. It was indicated to me that absent the protection of the Court, these sums would be regarded as immediately payable by Revenue, something which Pelko would presently be unable to do. It was, however, open to company to apply to Revenue for a staged payments option. Given, however, the acute cashflow problems which Ms. Finnegan has identified, even this option is likely to be problematic for the company.

16. While to their credit, Bank of Scotland has preserved with this SME company, the blunt reality is that the company is already insolvent, whether this is approached on either a balance sheet or, indeed, a cash flow basis. It cannot, therefore, be said that the application for examinership is premature, not least given that, as counsel for the petitioner, Mr. Gorman noted, noted, s.2(1)(a) provides that the jurisdictional threshold is satisfied simply where it appears to the court that the company "is likely to be unable to pay its debts." It is clear from the report of Ms. Finnegan that this situation is imminent, if, indeed, it has not already come about. One might add that s. 2(4) expressly empowers the Court to have regard to the forbearance shown by creditors. Here there has been significant forbearance shown by Bank of Scotland and (to an admittedly lesser degree) by the Revenue Commissioners.

17. These are all factors which strongly argue for the appointment of an examiner. Even if the company could trade for a few more weeks, the end result is more or less inevitable. Given that some restructuring of the company's debt is necessary, it is better that this should be done now in the course of an examinership while the company still has some prospects of survival, rather than at some later stage when any reserves of lingering goodwill and forbearance on the part of creditors might have been exhausted and the risk of disorderly collapse was all the greater.

18. Indeed, it may be fairly be observed that the real objection to the examinership in the present case on the part of the Bank is not untypical on the part of secured creditors, namely, a general dislike of the process. It places their security in jeopardy and the costs of the examinership must often in practice be indirectly borne by the secured creditors. These are, of course, understandable concerns, but they are not a reason in themselves which would justify the court refusing to make an order under s. 2 of the 1990 Act on general discretionary grounds if all jurisdictional conditions are satisfied and it was otherwise appropriate to do so. If the process of examinership is thought to be excessively burdensome or otherwise unfair to the rights of secured creditors, then the question of any reform of the 1990 Act is one which should be addressed to the Oireachtas and is not a matter for the courts.

Conclusions

19. In conclusion, therefore, it is clear that Pelko is a company which is insolvent and which is either presently unable to pay its debts as they fall due or, at least, will be shortly in a position where it will be unable to do so. It is plain from the report of the independent accountant that it has a reasonable prospect of survival if certain debt re-structuring takes place.

20. While it is true that a petitioning company is not entitled to the appointment of an examiner as of right under s. 2 of the 1990 Act even if the jurisdictional requirements are satisfied, here this step is appropriate, as the speedy appointment of an examiner mitigates the risk of a disorderly collapse were this necessary re-structuring to be delayed. There are, in any event, no real countervailing factors of substance which would justify the court declining to make such an order on general discretionary grounds. The mere fact that the secured creditors generally dislike this process given that they will often fare better with the appointment of a receiver at the time of their own choosing is not in itself a factor which would justify the court refusing to make the order sought.

21. In the event, therefore, I will appoint an examiner in respect of both Pelko and Pelko Holdings.