Neutral Citation [2016] IEHC 660

THE HIGH COURT

[2014 No. 3011 S]

BETWEEN

ORCA FINANCIAL LIMITED

PLAINTIFF

AND

BALLYCRAG DEVELOPMENTS LIMITED

DEFENDANT

JUDGMENT of Mr. Justice Eagar delivered on the 17th day of November, 2016

Relief claimed
1. By notice of motion dated 19th October, 2015 the defendant in these proceedings seeks an order pursuant to s. 52 of the Companies Act, 2014 and/or pursuant to O. 29 of the Rules of the Superior Courts directing the plaintiff to furnish security for costs of these proceedings.

Section 52 of the Companies Act, 2014
2. Section 52 provides:

> "Where a company is plaintiff in any action or other legal proceeding, any judge having jurisdiction in the matter, may, if it appears by credible testimony that there is reason to believe that the company will be unable to pay the costs of the defendant if successful in his or her defence, require security to be given for those costs and may stay all proceedings until the security is given."

The legal principles
3. In *Connaughton Road Construction Limited v. Laing O'Rourke Ireland Limited* [2009] IEHC 7, Clarke J. quoted *Interfinance Group v. K.P.M.G. Peat Marwick* (Unreported, Supreme Court, Clarke J., 13th January, 2006), setting out the central test for security for costs applications:

> "(1) In order to succeed in obtaining security for costs an initial onus rests upon the moving party to establish:
>
> (a) that he has a prima facie defence to the plaintiff's claim, and
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> (b) that the plaintiff will not be able to pay the moving party's costs if the moving party be successful."
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> "(2) In the event that the above two facts are established, then security ought to be required unless it can be shown that there are specific circumstances in the case which ought to cause the court to exercise its discretion not to make the order sought.
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> In this regard the onus rests upon the party resisting the order. The most common examples of such special circumstances include cases where a plaintiff's liability to discharge the defendant's costs of successfully defending the action concerned flow from the wrong allegedly committed by the moving party or where there has been delay by the moving party in seeking the order sought.
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> The list of special circumstances referred to is not of course, exhaustive.""

This Court notes that the onus of proof lies on the defendant to prove the first and second limb of the test, and if these are established, the onus of proof switches to the plaintiff to establish that special circumstance exist, that ought cause the court to exercise its discretion not to grant the application for security for costs.

4. In *Ochre Ridge Limited v. Cork Bonded Warehouses Limited and Port of Cork Company Limited* [2000] IEHC 96 O'Neill J. stated:

> "Mr. Cregan submits that the Court must look forward to that point in time and determine whether at that point in time the Plaintiffs will on the balance of probabilities be unable to pay the costs of the successful Defendant.
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> […]
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> I accept the correctness of Mr. Cregan's submissions, that the appropriate time in respect of which the Court must determine inability to pay, is the point in time where the Defendant seeking security has been successful in his defence."

5. This Court is mindful of the rights of persons, or companies to litigate, and has regard in this light to the dicta of Hogan J. in *CMC Medical Operations Limited (In Liquidation) trading as Cork Medical Centre v. the Voluntary Health Insurance Board* [2015] IECA 68. In dealing with the statutory power to direct security for costs Hogan J. states:

> "As the Supreme Court itself made clear in that case, such a discretionary power must be exercised in accordance with fundamental constitutional principles and respect the essence of constitutional rights.
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> The administration of justice is committed to the judicial branch of government by Article 34.1 of the Constitution. Access to justice is, accordingly, an indispensable feature of the constitutional order so that no "unnecessary monetary obstacle should be placed in the path of those who seek access to the courts"."

6. Security for costs applications serve a legitimate aim and purpose, in enabling the courts to engage in a balancing of the right of a plaintiff to litigate a claim, and the right of a (potentially) successful defendant not to be left without remedy. However, the Supreme

Court has recognised that security for costs applications if granted, may, if fixed at too high a sum, lead to a situation where a defendant "may be able to defeat an honest and substantial claim because the plaintiff cannot find the necessary security" (*Thalle v. Soares* [1957] I.R. 182. The courts must be mindful of the potential of the application to be used oppressively, so as to stifle a genuine claim.

7. However, the position of plaintiff *companies* [this Court's emphasis] subject to moving parties' security for costs applications raises unique considerations for this Court. The Court has regard to the fact that the plaintiff company enjoys limited liability. Hogan J. made the point in *CMC Medical Operations Limited (In Liquidation) trading as Cork Medical Centre v. the Voluntary Health Insurance Board* [2015] IECA 68 that litigation brought by limited companies is different in principle to litigation brought by private individuals. Within this context, unless security is ordered, there is a risk that plaintiff companies may use limited liability as a shield, causing defendants to "face the threat of expensive litigation", where costs may be irrecoverable. Hogan J. took the view that the main aim of the jurisdiction conferred then by s. 390 of the 1963 Companies Act was to balance the risk of the potential abuse of limited liability against the right of access to the courts.

8. Hogan J. continued:

> "It is true that Clarke J. suggested in his judgment in Connaughton Road Construction Ltd. v. Laing O'Rourke Ireland [2009] IEHC 7 that where, prior to the alleged wrongdoing, the plaintiff company had no significant net assets, it would need to establish that "in the absence of the wrongdoing alleged, it would have acquired net assets sufficient to enable it to discharge the defendant's costs in the event that the defendant were successful" in order to avoid an order for security for costs under s. 390 of the 1963 Act.
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> The effect of this test appears to be that an impecunious plaintiff company may face an order for security for costs even where the plaintiff could demonstrate that it would otherwise have a good cause of action. If, for example, the company has a deficit of €40,000 and the costs of the proceedings have been estimated at €60,000, does this mean that it should face an order for security for costs under s. 390 of the 1963 Act unless in that example it could show that it is likely to recover more than €100,000 damages? I cannot help thinking that as the application of s. 390 of the 1963 Act in this manner could effectively stifle otherwise valid claims, the Connaughton Road test itself may have to be re-visited in the light of the constitutional considerations I have just mentioned."

In the same case, Mahon J. stated:

> "A court should be slow to take any step which has the effect of curtailing litigation or unduly restricting the constitutional right of access to the courts. The requirement that a party effectively defending an application for security for costs should be expected to delve unduly deeply into complex matters which constitute the subject matter of the litigation itself may produce this result."

The facts

9. In this case, the plaintiff company commenced proceedings by issuing a summary summons seeking the payment of €698,000 in respect of fees relating to the plaintiff's sourcing and raising loan funding to assist with the purchase and development of sites for residential homes, on behalf of the defendant (or special purpose vehicles owned and controlled by the defendant). Following the exchange of affidavits in the context of a notice of motion seeking summary judgment before the Master, the Master by consent ordered that the action be adjourned for plenary hearing and directed the plaintiffs to file a statement of claim which was delivered on 9th July, 2015. On 3rd September, 2015 the defence was lodged by the defendant, denying that the defendant owed the plaintiff the sum as set out in the statement of claim, and denied the existence of agreements.

10. Counsel on behalf of the plaintiff conceded that a prima facie defence had been made out by the defendant. In these circumstances the first leg of the central test is established - the defendant company has established a prima facie defence to the plaintiff's claim.

11. The second burden on the defendant is to show that the plaintiff will not be able to pay the moving party's costs if the moving party is successful in defending the claim.

12. The plaintiff company's activities can be summarised as follows: it provides financial advice and products to companies and individuals, and it assists in sourcing and raising investment capital for commercial purposes. The defendant company is a construction company engaged in the purchase and development of residential sites. The relevant affidavits are that of Kieran Wallace filed 19th October, 2015, the affidavits of Stephen Byrne and James O'Hanlon both filed 30th November, 2015, the second affidavit of Kieran Wallace, dated 22nd December, 2015 and the supplemental affidavit of James O'Hanlon filed on 17th February, 2016.

13. Kieran Wallace is a well known accountant in KPMG. He said that he had examined the financial returns filed by the plaintiff company with the Companies Registration Office for the financial years ended 31st December, 2012 and 31st December, 2013. He believes that there are limited funds available to the plaintiff which would not be sufficient to satisfy any order for costs in the event that the plaintiff's claim failed. He has been informed that the costs of any proceedings are likely to be between €150,000 and €200,000. Exhibited with his affidavit is the independent auditor's report to the directors pursuant to s. 18 (3) of the Companies (Amendment) Act, 1986 by Avid Partners, Chartered Certified Accountants, dated 31st December, 2012.

14. In relation to the 2012 accounts, Avid Accountancy indicate the following: "accounts are prepared on a going concern basis which assumes that the company will continue in existence for the foreseeable future with no intention to liquidate or significantly curtail its activities within the next 12 months. While the global economic downturn has impacted on the business with a curtailment of profits reported in the previous 2 years and a trading loss in the current financial year the business continues to be supported by the financial institutions in terms of working capital and senior debt finance. Having considered the financial position outlined above and the near global financial uncertainty, the continuity of the business is dependent on returning to and maintaining a sufficient level of profitable trading to meet the debts and obligations as they fall due and the continued financial support of the financial institutions." It also notes the bank overdraft and loan facilities as secured by personal guarantees from the directors.

15. The affidavit of Stephen Byrne filed on 30th November, 2015 sets out the following. The shares in the plaintiff company are held on an equal basis by John Molloy and Stephen Byrne. He states that given the nature of the service offered and the closely held ownership structure of the plaintiff company, there is no commercial sense or necessity in the company recording and then retaining

large end of year profits. The directors of the plaintiff company withdraw the majority of any profits made by the plaintiff company. He also states that the amount withdrawn is decided after consultations made on a quarterly basis between the directors and Avid Partners Accountants and Business Advisors. He further makes the point that these assessments of the plaintiff's liabilities are undertaken in a thorough and conservative manner as *it is imperative* [this Court's emphasis] that the company, as a Central Bank authorised entity, remain solvent. The plaintiff is authorised by the Central Bank to act as an insurance and reinsurance intermediary, an investment business firm, an investment product intermediary and a mortgage intermediary. He exhibits a copy of the authorisation certificate granted by the Central Bank to the plaintiff. He further says that the authorisation granted by the Central Bank to the plaintiff to act in this capacity is monitored continuously and reviewed annually following the submission of the plaintiff's annual accounts to the Central Bank. He says that great care is taken to ensure that the plaintiff is in a position to meet its liabilities as they fall due. He further says that the plaintiff is aware that it will need to make provision for the payment of the defendant's legal costs in the event that it is unsuccessful in the present proceedings.

16. He further states that the plaintiff company has strong existing revenue streams and that it is expected that the plaintiff's trading performance will improve significantly in the coming year.

17. He states that a more accurate appraisal of the financial position of the plaintiff is offered by Mr. O'Hanlon, than that of Mr. Wallace. Mr. Byrne says that the plaintiff's net current liabilities position as shown in the abridged financial statements for the year ended 31st December, 2014 arose due to a number of term loan facilities expiring, and that he and his fellow director are currently involved in negotiations to restructure the repayment of such loan facilities over a longer period. The directors are confident that these negotiations will have a positive result. It is expected that the plaintiff's position in relation to net current assets and liabilities will improve significantly in the near future. He also states that the plaintiff has strong and increasing revenue streams in the sum of €188,000 due to be paid in relation to insurance business written by the plaintiff, while the plaintiff further expects to continue to receive its regular new business income of approximately €70,000 per month. The plaintiff is also expecting a once-off fee of €338,000 which is due by March, 2016 and the plaintiff intends to form a cash reserve from these funds which would cover any potential costs liability. He says that in the unlikely event that the plaintiff is made liable for the defendant's costs prior to March, 2016, the cash reserves will be in place, and the plaintiff would look to sell a portion of, or an entire book of its recurring business which, as outlined above, is of considerable value.

18. The next relevant affidavit was that of James O'Hanlon who said he is an accountant and managing director of Avid Partners, Accountants and Business Advisers Ltd. who are the *independent* [this Court's emphasis] auditors of Orca Financial Limited. He exhibits his report of the summary financial review in November, 2015. He emphasised again that the plaintiff is a broker and retail intermediary regulated by the Central Bank of Ireland. He affirmed that the company receives and transmits orders in certain financial products. He said that in relation to goodwill, the qualifying goodwill was written down by the carrying value by €300,000 in 2014. He said that the existing renewable book for the plaintiff is currently in the region of €156,000 per annum, placing an extra valuation of €936,000 on the renewable book of the plaintiff. Based on this valuation, the uplift in the market would increase the net asset position by €276,000. This valuation excludes the valuation on the non-recurring income of the plaintiff which, on an annual basis, is in excess of €744,000 based on the current annual income of the plaintiff being €888,000 as reported in the financial statements for the year ended 31st December, 2014.

19. The company's net current liabilities position arose due to a number of the term loan facilities being out of contract and therefore, the term loan facilities were required to be disclosed as current liabilities within the financial statements. The company directors are in ongoing negotiations to restructure such loan facilities over a longer term, which is expected to result in the company returning to a positive position in relation to net current assets/liabilities in the foreseeable future.

20. In conclusion, he says it is his opinion that the plaintiff company is in a healthy financial position and will be capable of meeting an order for costs in the amount previously put forward by the defendant's solicitors.

21. The second affidavit of Kieran Wallace was sworn on 22nd December, 2015 and makes some observations upon a review of the abridged accounts at 31st December, 2014. He quoted as follows:

> i. Orca recorded a repayment loss of €8,890 in 2014.
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> ii. The company's largest asset is purchased goodwill and that according to Mr. O'Hanlon it was written down by an additional €300,000 in 2014 to take account of guidelines issued by the Central Bank regarding qualifying goodwill for investment intermediaries.
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> iii. The company had current net liabilities of €468,000 in 2014, reduced however from €526,734 in 2013 and he says that a company cannot operate with negative working capital for an extended period of time because the company will not be able to meet payments of certain liabilities if additional funds are not sourced.

22. The approach adopted by the plaintiff sets out how Orca would discharge an order for costs if one was made against the company before and after March, 2016. However, the Court notes that it is presently November, 2016.

23. Mr. Wallace indicates that no details on the company's projections, or how such projections have been prepared, have been provided. Further, he opines that no meaningful details were provided to him relating to Orca's historical trading performance. In these circumstances he is not in a position to undertake his own review on the basis of the abridged accounts available. He says that Mr. O'Hanlon, who has far greater access to information than he does concerning the company, has not provided any meaningful assessment of the company's trading performance. He criticises Mr. O'Hanlon for placing a speculative value on the company's assets, an assessment he would have expected to be undertaken by an experienced company valuations expert, and not the company's auditor.

24. Finally, of relevance is the supplemental affidavit of James O'Hanlon sworn on 7th February, 2016, in which he takes issue with Mr. Wallace querying the amortisation of the value of the goodwill held by the plaintiff in 2014. He states that standard accountancy policy is to amortise goodwill held by a company on the basis that such goodwill has a useful economic life of 20 years. However, he notes that the directors of the plaintiff company should have reduced the value of such goodwill by a further €300,000 in addition to the standard 20 year amortisation, to ensure compliance with the accelerated amortisation requirements for investment intermediaries and with s. 22 of the Central Bank (Supervision and Enforcement) Act, 2013.

25. He also criticised Mr. Wallace for outlining that an expression of interest may be made by a private individual who may purchase a number of shares in the plaintiff company – he viewed this as an irrelevance. He states that in relation to Mr. Wallace's averment, there is nothing to be gained from a consideration of the plaintiff's performance for the year ending 31st December, 2009. He states

that a consideration of the plaintiff's performance in this current period better predicts future trading results, more so than considering the period of 2010 – 2014. The plaintiff company in that period, in common with the vast majority of commercial enterprises was effected by the unprecedented domestic and global economic collapse.

26. This Court is required to estimate whether the plaintiff company would be able to discharge the costs of proceedings, should the defendant be successful.

27. This case is not likely to finish before October, 2017. The Court, in exercising its discretion, notes the comments of O'Neill J. in the *Ochre Ridge Limited v. Cork Bonded Warehouses Limited and Port of Cork Company Limited* [2000] IEHC 96, that this Court must look forward to the relevant point in time where the defendant at the close of legal proceedings, *may* (this Court's emphasis) have been successful in his defence, and determine whether at the point in time, the plaintiff will be able to furnish payment for costs.

28. Mr. Wallace appears to this Court to be doing the opposite of what he is supposed to do. He makes assumptions about the company's performance and the exercise he carries out is an incomplete one. The affidavit of Mr. Wallace does not contain his view as to the income streams of the plaintiff company in the future (this Court's emphasis).

29. The plaintiff company is solvent and required to be so by Central Bank rules.

30. The authorisation granted by the Central Bank to act as an insurance and reinsurance intermediary, an investment business firm, an investment product intermediary and a mortgage intermediary, is monitored continuously by the Central Bank and is reviewed annually.

31. The onus of course is on the defendant to show that the plaintiff would not be able to pay the costs. The Court is also conscious of the comments made by Hogan J. in *CMC Medical Operations Limited (In Liquidation) trading as Cork Medical Centre v. the Voluntary Health Insurance Board* [2015] IECA 68 in which he said:

> "Such a discretionary power must be exercised in accordance with fundamental constitutional principles and respect the essence of constitutional rights.
>
> The administration of justice is committed to the judicial branch of government by Article 34.1 of the Constitution. Access to justice is, accordingly, an indispensable feature of the constitutional order so that no "unnecessary monetary obstacle should be placed in the path of those who seek access to the courts"."

In all the circumstances of this case in exercising discretion, the Court does not accept that the defendant has proved that the plaintiff will not be able to pay the moving party's costs if the moving party is successful in its defence.

32. In those circumstances this Court refuses to direct that the plaintiff furnish security for costs of these proceedings.