Neutral Citation: [2016] IEHC 533

THE HIGH COURT

[2014 No. 284COS]

IN THE MATTER OF LARAGH CIVILS LIMITED (IN VOLUNTARY LIQUIDATION)

AND IN THE MATTER OF THE COMPANIES ACT 1963 – 2013

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

AND IN THE MATTER OF SECTION 56 OF THE COMPANY LAW ENFORCMENT ACT 2001

BETWEEN

MICHAEL FITZPATRICK

APPLICANT

AND

GERARD CONNAUGHTON and ANN-MARIE CONNAUGHTON

RESPONDENTS

JUDGMENT of Mr. Justice David Keane delivered on the 9th September 2016

Introduction

1. This is an application for a declaration of restriction against the second named respondent under s. 150 of the Companies Act 1990, as amended.

Background

2. Laragh Civils Limited ("the company") was incorporated on the 27th April 2010. During its brief existence, the company carried on the business of civil engineering contractors. On the 14th August 2012, the first respondent certified to the Companies Registration Office that, at an extraordinary general meeting on the same date, the members of the company had resolved to wind it up. By resolution made at a meeting of the company's creditors, also on the 14th August 2012, the applicant was appointed liquidator.

3. Then and at all other material times, the two directors of, and shareholders in, the company were the respondents, a married couple, each of whom was appointed director with effect from the 27th April 2010, the date of the company's incorporation.

4. On the 27th May 2014, the applicant certified that, on the 14th August 2012, the date of his appointment, the company was insolvent in that it was unable to pay its liabilities as they fell due for payment.

5. On the 25th January 2013, the applicant furnished a report on the conduct of the respondent directors to the Director of Corporate Enforcement who received that report on the 28th January 2013. On the 30th April 2013, the Office of the Director wrote to inform the applicant that he was not relieved of his obligation under s. 56(2) of the Company Law Enforcement Act 2001 to apply to this court for the restriction under s. 150 of the Companies Act 1990 of each of the respondent directors.

6. By motion filed on the 20th May 2013, the applicant sought various reliefs against the first named respondent only. The first named respondent did not enter an appearance in response to that motion. On the 1st July 2013, this Court (*per* Cooke J.) made orders in the following terms:

> (i) That four separate payments made by the company to the first respondent on the 21st December 2011, the 22nd December 2011, the 17th March 2012 and 30th April 2012, amounting in total to €76,200 were a fraudulent preference of the first respondent over the company's creditors and were invalid;
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> (ii) That the said payments in the said amount were a disposal of the company's property the effect of which was to perpetrate a fraud on its creditors;
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> (iii) That the first respondent was liable to repay the said sum to the applicant as liquidator of the company;
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> (iv) That the first respondent was further liable to pay to the applicant as liquidator of the company the further sum of €98,055, pursuant to provisions of s. 298 (2) of the Companies Act 1963, as amended, whereby the Court is empowered to examine the conduct of a director and compel him contribute such sum to the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or other breach of duty as the court thinks just.
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> (v) That, pursuant to the provisions of s. 297A (1) of the Companies Act 1963, as amended, the first respondent, as a person knowingly a party to the carrying on of the business of the company with intent to defraud creditors of the company, was declared personally responsible for certain debts of the company amounting to the sum of €265,282; and
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> (vi) That the first respondent was liable to repay the said sum to the applicant as liquidator of the company.

7. The present application is brought by motion issued on the 14th June 2014, originally made returnable for the 28th July 2014. The application was heard on the 27th April 2015.

8. On that date, I made a declaration of disqualification as a company director against the first named respondent under s. 160 of the Companies Act 1990, as amended ("the 1990 Act"), for a period of five years, being satisfied that the jurisdictional requirements of s. 160 (2) (b), (c) and (d) had been established and that, on the evidence before me, that respondent's past conduct makes him presently unfit to act in that, or any related, capacity as envisaged under that section. Although the first named respondent had not entered an appearance in response to the application against him, I was satisfied, on the evidence adduced at the commencement of the application, that he had been properly served with the originating notice of motion, and accompanying motion papers, in accordance with the Rules and the previous orders of this Court.

9. Having heard argument in relation to the application pursuant to s. 150 of the 1990 Act, to restrict the second named respondent

as a company director, I reserved my decision on that aspect of the motion.

10. Before doing so, I ruled *ex tempore* against the second named respondent's submission that the application against her should not be permitted to proceed on grounds of delay.

11. In that regard, it is undoubtedly the position that, having submitted his report to the Director of Corporate Enforcement in January 2013, the applicant failed to comply with the requirement under s. 56(2) of the Company Law Enforcement Act 2001 ("the 2001 Act") that he bring restriction proceedings within five months of that event *i.e*. no later than June 2013. The present motion was not brought until June 2014, some twelve months later.

12. The applicant has averred that, during that period, he was obliged to devote significant time and resources to the pressing claims of fraudulent preference and breach of duty that squarely arose as between the company and the first named respondent. In addition, the applicant has averred that he received no co-operation from the respondents in the conduct of the liquidation. While the second named respondent disputes the applicant's claim that she has failed to co-operate with him, averring that she received no communication from him prior to the issue of the present motion, little turns on the point since, as we shall see, her position is that, despite her status as a director of the company, she had no knowledge of the company's affairs to offer, rendering her professed willingness to co-operate of no practical assistance to the applicant in advancing the liquidation.

13. Indeed, the defence relied upon by the second named respondent is she should be considered to have acted responsibly as a purely passive or token director of her husband's company, entirely uninvolved in, and ignorant of, its management and with no role in its corporate governance. It follows that her defence is not hampered by lapse of time in the way that it might be if she were seeking to make the case that she had acted honestly and responsibly while engaged in the conduct of the company's affairs but was now prejudiced in her efforts to assemble the appropriate witnesses and evidence required to discharge the onus on her to establish that fact due to the applicant's delay in bringing the present application. While any lapse of time prior to trial is prejudicial to a respondent, indeed to any litigant, in as far as it entails a commensurate period of worry or anxiety prior to the determination of that person's rights or obligations, I did not consider that the lapse of time in this case, given the circumstances in which it occurred, was such, in and of itself, as to warrant, much less require, the dismissal of the restriction application against the second named respondent.

14. For those reasons, I ruled that the application should proceed. I also made an order, pursuant to the terms of s. 56(2) of the 2001 Act, extending the time for bringing it.

The issue on the application to restrict the second named respondent

15. The second named respondent does not dispute that the company was unable to pay its debts at the commencement of its winding up. Nor does she deny that she was a director of the company at the material time or that the Director of Corporate Enforcement has not relieved the applicant of the obligation otherwise incumbent on him under s. 56 (2) of the 2001 Act to bring the present application against her in respect of the company.

16. It follows that the Court is obliged to make a declaration of restriction under s. 150 of the 1990 Act in respect of the second named respondent unless satisfied that her position comes within one of the circumstances set out in sub-s. (2) of that section. The applicant accepts that there is no question of any dishonesty on the part of the second named respondent in the conduct of the affairs of the company. The application therefore turns on whether that respondent acted responsibly in that regard, since it is not suggested that there is any other reason why it would be just and equitable to make a declaration of restriction against her.

The evidence

17. Much of the evidence on this application is not in dispute. In addition to what has already been set out above, the following is the position.

18. The applicant has established from his enquiries subsequent to his appointment as liquidator of the company that, at all material times, the first named respondent was the managing director of the company and the person in control of its bank accounts, cheque books, records and finances.

19. In addition to the fraud upon the company's creditors and misfeasance in office of the first named respondent, the applicant has drawn a number of other aspects of the conduct of the company's affairs to the attention of the Court. They include:

(a) A complete failure to keep or maintain proper books, records and accounts in respect of the company's business.

(b) Numerous instances of deliberately misleading entries in the limited books and records that were maintained.

(c) A complete failure to maintain a proper accounting system to monitor the company's financial position.

(d) A complete failure to prepare any accounts whatsoever – whether monthly or quarterly accounts or any trading statements - from the company's commencement of trading in December 2010 to its cessation of trading in August 2012, which failure precluded the respondent directors from forming any sensible view concerning the company's solvency at any time during that twenty month trading period in which, according to the company's statement of affairs, signed on the 14th August 2012 by the first named respondent, the company incurred a deficit of almost €360,000.

(e) The presentation of a statement of affairs to the meeting of the company's creditors that was grossly misleading and untrue, understating the company's deficit by almost €100,000.

(f) The payment by the company of a net annual salary of €23,700 to the second named respondent in 2011, while the company's wages records for that year recorded her gross annual salary as €21,242, suggesting a net annual salary of €15,603.

20. In the two replying affidavits that she has sworn in opposition to the application for a declaration of restriction against her, the second named respondent avers to several matters that she contends are relevant to the central issue of whether she has acted honestly and responsibly in relation to the conduct of the company's affairs.

21. The second named respondent avers that she did indeed work for the company and was paid €300 *per* week. Her pay slips and P60s were 'done by the lady in accounts', though she did not receive them. Her job involved running errands and performing menial tasks. At 'around' that time, the first named respondent was banned from driving and the second named respondent acted as his driver and performed other 'general non-accounting duties.' She ceased working for the company in March 2011 because she had to

look after her seriously ill son. Her lack of knowledge concerning the company and its affairs was contributed to, if not caused by, the breakdown of her personal relationship with the first named defendant and the resulting breakdown in communication between them.

22. The second named respondent goes on to aver broadly as follows. She first learnt of the 'enormous financial difficulties' of the company when she was served with the present motion papers. The first named defendant ran the company alone as he saw fit, as was acknowledged by the applicant in his report to the Director of Corporate Enforcement. Naively and through lack of experience, the second named respondent saw her role in the company as 'a silent one.' She understood that a book keeper was employed to manage the company's books on a day to day basis. It was her 'reasonable expectation' that accountants were to attend to the company's annual accounts and 'that appropriate experts were dealing with matters.' She was not made aware of 'very fast developing and catastrophic events' that befell the company. She does not explain what she understands those fast developing and catastrophic events to have been. She was not aware of demands by the company's creditors for overdue payments.

The law

23. The applicant suggests that the starting point for the Court's consideration of what the requirement to have acted 'responsibly in relation to the conduct of the affairs of the company' entails is the following passage from the judgment of Fennelly J. in the Supreme Court in the case of *Re Mitek Limited; Grace v Kachkar* [2010] 3 I.R. 374 IESC 31 (at para. 79):

> "In one sense, it is obvious that a director must behave responsibly. In order to discharge his duties, he must, in the first instance, inform himself about the business and affairs of the company and about his own duties as director. Circumstances will inform the nature and extent of these duties. Even non-executive directors of companies must be conscious in the times we live in that they cannot be mere cyphers or purveyors of votes at the whim of management. There was a time when even such a distinguished text as Gower's *The Principles of Modern Company Law* (3rd ed. Stevens, London, 1969) could state at p. 549: 'public opinion has come to recognise that directorships are little more than sinecures, requiring, at the most, attendance at occasional board meetings.' The Act of 1990 itself evinces public concern that directorships involve real responsibility and that persons who do not conform at least to some generally acceptable minimum standards either should not, in the public interest, be permitted or should be restricted in regard to future holding of directorships.'

24. In the face of that authority, very able Counsel on behalf of the second named respondent pointed to the uneasiness expressed by Hardiman J. in *Re Tralee Beef & Lamb Ltd: Kavanagh v Delaney et al* [2008] 3 IR 347 at any suggestion that the position of a non-executive director be assimilated to that of an executive one, an approach that Hardiman J. felt might derive some support from the decision of Murphy J. in *Vehicle Imports Ltd (in liquidation)* (Unreported, High Court, 23rd November 2000) which, in turn, had adopted the exposition of the duties and responsibilities of a company director set out by Jonathan Parker J in *Re Barings plc et al (No 5); Secretary of State for Trade and Industry v Baker et al (No 5)* [1999] 1 BCLC 433.

25. However, it seems to me that the question in each of those cases concerned the permissible degree of delegation of specific tasks and functions – whether by a board of directors generally or by a specific director in particular - that is consistent with the responsibilities or duties of each as such. In that context, it is perfectly understandable that Hardiman J. was wary of any suggestion of a 'one size fits all' answer to that question, contrasting the position of the 'vast corporation' the subject of the *Barings* case and the 'small meat company in rural Ireland run effectively by one man' in *Tralee Beef & Lamb*. The appellant in the latter case was a non-executive director of the company concerned, having been appointed to that role at the instance of a company which managed funds that had been invested in it under a business expansion scheme.

26. Whatever the variation in the level of permissible delegation may be between different sorts of director in various kinds of company, and that point has yet to be definitively considered, it is difficult to see how any director – executive or non-executive - can escape any of the following basic responsibilities: first, to inform himself or herself about the nature of his or her duties as director; second, to acquaint himself or herself with the affairs generally of the company concerned; and third, to exercise appropriate supervision or oversight at board level in respect of the execution or discharge of whatever tasks or functions have been properly and appropriately delegated to others.

27. More fundamentally, in my view the present case raises the issue of 'abdication of responsibility', rather than that of 'delegation of responsibility.' I did not understand Counsel on behalf of the second named respondent to argue other than that, on the evidence before the Court, the second named respondent was a 'token' or 'passive' director who agreed to assume that position at the behest of her spouse, the first named respondent and did not purport to discharge any responsibility whatsoever thereafter in relation to any aspect of the conduct of the company's affairs or the supervision of that conduct.

28. As long ago as 1984, in *Re Hunting Lodges Ltd* [1985] ILRM 75, Carroll J. stated:

> "The day has long since passed since married women were classified with infants and persons of unsound mind as suffering from a disability in so far as responsibility for their acts was concerned, or since a married woman could escape responsibility on the grounds that she acted under the influence of her husband. Mrs Porrit cannot evade liability by claiming that she was only concerned with minding her house and looking after her children. If that was the limit of the responsibilities she wanted, she should not have become a director of the company or, having become one, she should have resigned.
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> Any person who becomes a director takes on responsibilities, particularly where there are only two. The balance sheet and profit and loss account and director's report for each year should have been signed by her. A director who continues as a director but abdicates all responsibility is not lightly to be excused. If she had reasonably endeavoured to keep abreast of company affairs and had been deceived (and there is no such evidence) it might be possible to excuse her."

29. At the hearing of the application, Counsel for the second named respondent submitted, with disarming directness, that the Court should simply prefer and apply the very different approach of Palmer J. in the Supreme Court of New South Wales decision in *Southern Cross Interiors Pty Ltd & Anor. v Deputy Commissioner of Taxation &Ors*. [2001] 188 ALR 114. Having considered that submission carefully, I am satisfied that I cannot do so for a number of reasons.

30. The first and most obvious is that, as Parke J. pointed out in *Irish Trust Bank Ltd v Central Bank of Ireland* [1976]7] ILRM 50 and Clarke J. reiterated in *Re Worldport Ireland Ltd* [2005] IEHC 189, as a matter of judicial comity, a judge of first instance should normally follow the decision of another judge of the same court unless there are substantial reasons for believing that the initial judgment was wrong. In this instance, I believe that the analysis of Carroll J. in *Re Hunting Lodges* was correct and that the decision of Palmer J. in *Southern Cross Interiors* is readily distinguishable from the present case.

31. The latter decision does indeed, at first glance, appear to encapsulate a starkly different approach to the question of the degree of responsibility in relation to the conduct of a company's affairs borne by a 'token' or 'passive' director who agrees to act as such due to 'the ties of affection', when compared to that assumed by company directors generally. The passage from that judgment upon which the second named respondent relies is the following (at para. 137):

> "I hold that Mrs Clark accepted appointment as a director of [the company] with no understanding of all of the duties and responsibilities which that office entailed. That lack of understanding was not due to any fault on her part. Her husband failed to explain to her anything of the responsibilities which directorship involved and did not suggest that she seek advice of further information. She accepted the appointment at his request because of the trust and confidence which she had in him, believing, at his suggestion, that the appointment was only a formal requirement. She did not participate in the management of the company because she did not believe that she was required to do so. That belief was induced by her husband's statements at the time he requested her to become a director and by his subsequent conduct in not discussing the company's affairs with her. She acted upon that belief because of the trust and confidence she placed in her husband and because she thought that he was knowledgeable in such matters. Nothing was brought to her attention during her directorship which should have put her on enquiry as to [the company's] financial position or as to her responsibilities as director."

32. The significant point of distinction between the two cases is that *Southern Cross Interiors* does not address the question whether the relevant respondent there had 'acted responsibly in relation to the conduct of the affairs of the company' at issue in that case. Plainly, she hadn't. Instead, it addresses the quite different question of whether the respondent had a 'good reason' for failing to participate in the management of the company, which question forms the test in that jurisdiction for the application of a statutory defence to a claim by the tax authorities for an indemnity against the directors of a company, in the face of a claim by the liquidator of that company for a rebate, as an 'unfair preference', of a payment that the company had previously made to those authorities.

33. It was just such a claim for an indemnity in *Southern Cross Interiors* that, in the view of Palmer J. on the facts presented, brought into play long established legal principles, such as that of unconscionability, whereby a person may be excused from the legal consequences of his or her acts where the terms of the relevant bargain are so lop-sided or so unjust as to be contrary to good conscience, and which prompted a discussion of the manner in which the potential incurring of any such liability by an unsuspecting or incautious spouse had recently acquired in that jurisdiction the provocative tag of 'sexually transmitted debt.'

34. The question addressed in the context of the defence available to the relevant respondent in *Southern Cross Interiors* was not whether she had acted responsibly as a director of the company concerned but, rather, as the passage quoted above demonstrates, whether, in failing to do so, she was ever conscious of those responsibilities. It is the former question, not the latter one, that the Court is required to address under s. 150 of the 1990 Act (and, in respect of more recent cases, under s. 819 of the Companies Act 2014).

35. One further point must be made about the decision of the Supreme Court of New South Wales in *Southern Cross Interiors*. It is that Palmer J. prefaced the paragraph of his judgment quoted above with the observation that it would be 'a comparatively rare case in which a wife is able to establish such a defence on the facts.' I take that to imply that unsupported assertions of inexperience; naivety; lack of awareness of the responsibilities of company directorship; trust and confidence in a spouse who describes the appointment as a formality and who says that the management of the company may be left entirely to him; and so forth, would be closely scrutinised by the courts in that jurisdiction when required to adjudicate on any assertion of the statutory defence.

36. In my view, such close scrutiny is particularly necessary where a court is presented - as this Court has been in a significant number of s. 150 applications subsequent to the decision in *Southern Cross Interiors* - with bare recitals on oath by respondents who have acted as 'token directors', borrowing, in whole or in part, or closely paraphrasing, the precise language that Palmer J. used when giving an example of the kind of circumstances in which a spouse may have 'good reason' for not participating in the management of a company. Such terse averments are then invariably used, as they have been in this case, in support of the contention that the respondent concerned has acted responsibly in relation to the conduct of the relevant company's affairs by playing no part whatsoever in the conduct of those affairs or in the supervision of that conduct.

37. As the Court of Appeal recently confirmed in the case of *Director of Corporate Enforcement v. Walsh* [2016] IECA 2, it would be contrary to the whole notion of proper corporate regulation to exonerate token directors from liability or relieve them from restriction on the basis of the passive nature of their role. To limit the test for irresponsibility to cases where the evidence demonstrates, in addition, "some real moral blameworthiness" by reference to the decision of Carroll J. in *Re Hunting Lodges*, would be to conflate the test for fraudulent trading under s. 297 of the Companies Act 1963 (which was at issue there) with that for irresponsible conduct under s. 150 of the 1990 Act or, as is now the position, under s. 819 of the Companies Act 2014 ('the 2014 Act').

38. Against that background, insofar as the decision of O'Neill J. in *Re Lynrowan Enterprises Ltd* (31 July 2002, unreported, High Court) [2002] 7 JIC 3119 cannot be reconciled with the earlier decision of Carroll J. in *Re Hunting Lodges* (or the subsequent decision of the Court of Appeal in *Director of Corporate Enforcement v Walsh*), I must decline to follow it as a decision reached *per incuriam*. The apparent acceptance by the Court in that case of the proposition that a *de jure* director of a company who takes no part whatsoever in the affairs of a company, and is not expected to do so, is not thereby irresponsible in relation to the conduct of the affairs of the company, appears to have occurred in circumstances where the decision in *Re Hunting Lodges* was not drawn to the Court's attention; it was certainly not cited in the Court's judgment, which is more particularly concerned with the role of another respondent in that case as a *de facto* or shadow director.

39. I am reinforced in that view by a consideration of the following passage from the judgment of Cooke J. in the more recent case of *Mannion v Connolly & Anor* [2013] IEHC 544 concerning the position of a respondent director who, while "not indifferent" to the proper management of the Company, became a co-director of the company with her husband only to fulfil the legal requirement for two directors:

> "It is well settled, however, that inactivity or non-involvement on the part of a director is no answer to an application for restriction under s.150. An individual who accepts a position of director of a company even if only to fulfil the legal requirement must accept the responsibilities and potential consequences that go with it. A director who has played no part whatsoever in the conduct of the affairs of an insolvent company cannot claim to have acted responsibly in relation to them."

40. There is one feature of this case that has given me pause in applying the law as I have just identified it. That is the subsequent commencement in force of the 2014 Act, abolishing the minimum two director requirement under s. 174 of the Companies Act 1963 and replacing it with a single director requirement under s. 128 of the new Act.

41. This was foreshadowed in Courtney, *The Law of Companies*, 3rd ed. (Dublin, 2012) in which, at p. 898, having addressed the decision in *Southern Cross Interiors*, the learned author expressed the view that 'rather than operate as a defence to negligently acting as a second statutory director, the fact that some spouses are prevailed upon to meet a statutory minimum of two directors should instead cause us to consider whether private companies should be required to have two directors.' Indeed, the Company Law Reform Group, of which Dr Courtney was the chairman, in its First Report of the 31st December 2001 (para. 11.8.7), had recommended the relevant change on the basis that the practice of appointing a second 'token' director serves 'only to devalue and trivialise the office of director of a company'.

42. While it is possible to speculate that, had the relevant provision of the 2014 Act been in force at the material time, the second named respondent might never have been called upon to accept appointment as a director of the company and might never have done so, the reality is that it was not then in force and she did accept appointment as a director of the company. I cannot approach this case on the basis of the law as it is now but rather I am constrained to deal with it on the basis of the law as it stood at the material time.

43. The submission was made on behalf of the second named respondent that it would be 'unjust and inequitable' to restrict her from 'being involved in business', because of her particular personal circumstances. Those circumstances are asserted to be that her home has been repossessed; that she has separated from her husband who is undergoing a process of bankruptcy in Scotland; and that she is a qualified foot health practitioner who would like to set up a small business, as such, to support herself and her young son, which – she contends - would 'necessitate' setting up a limited company through which that business could operate.

44. There are three fundamental difficulties with that submission, quite apart from the failure of the second named respondent to provide any evidence beyond her own bare averments to corroborate any of the assertions of fact that underpin it. The first is that it assumes that the Court has a discretion, irrespective of any failure on her part to establish that she acted responsibly, to refrain from making a declaration of restriction against her on *ad misericordiam* or other grounds. The Court has no such discretion. Where an application is brought in the appropriate circumstances and where the defences in s. 150(2) are found not to apply, the making of a restriction order is mandatory; so much is clear from the decision in *Business Communications Ltd v Baxter and Parsons* (21 July 1995, unreported) HC, Murphy J.

45. The second difficulty is that the submission equates a declaration of restriction under s. 150 of the 1990 Act with a 'restriction on being involved in business.' A declaration of restriction under s. 150 of the 1990 Act, now s. 819 of the Companies Act 2014, does not restrict a person from being involved in business. In essence, it restricts the person concerned from being a director of a private limited company with an allotted share capital of less than €100,000. It does not prevent a person from being a director of a private limited company that meets that share capital requirement. More significantly for the second named respondent, in view of her straitened financial circumstances as she describes them, it does not restrict a person from engaging in business in partnership, or as a sole trader or as an employee of another individual, partnership or company.

46. The last observation leads directly to the third difficulty, which is that the second named respondent has done nothing to explain, much less corroborate, her assertion that she can only work as a foot health practitioner through the medium of her own private limited company.

Conclusion

47. For the reasons I have given, in circumstances where the second named respondent has failed to establish a defence under s. 150(2) of the 1990 Act, the Court is obliged to make the appropriate declaration of restriction under s. 150(1) of that Act against the second named respondent and I will do so.