



THE COURT OF APPEAL

**Irvine J.
Sheehan J.
Mahon J.**

Record No. 2014/889

[Article 64 Transfer]

Mary and Joseph O'Brien Developments Limited (In Liquidation)

Plaintiff/Appellant

- and -

Robert Sobol and Mary O'Brien Sobol

1st and 2nd Defendants/Respondents

- and -

Anthony Allen

3rd Named Defendant/Respondent

Judgment of Ms. Justice Irvine delivered on the 9th day of May 2016

1. Core to this appeal are the circumstances in which a judge having jurisdiction in a matter ought to make an order pursuant to s. 390 of the Companies Act 1963 requiring a company that is a plaintiff in litigation to provide security for the costs of a defendant in that action.

2. Section 390 provides that:-

"Where a limited 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 defence, require sufficient security to be given for those costs and may stay all proceedings until security is given."

Relevant background facts

3. On 17th December, 2012, the High Court (Murphy J.) made an order that the plaintiff company ("the company"), the appellant in this appeal, provide security for the costs to be incurred by the third named defendant/respondent ("Mr. Allen") in defending these proceedings, in default of which the same would be stayed. Later, by order dated 16th May, 2014, the Master of the High Court measured the said security in the sum of €74,800 inclusive of VAT. It is as against that order that the company now appeals. In this regard it is perhaps relevant to note that the company has, pursuant to an order of the Supreme Court made on 25th July, 2015, lodged a sum of €10,000 in court to secure Mr. Allen's costs on this appeal.

Factual background

4. The appellant was a property development company that was placed in voluntary liquidation on 12th April, 2012, following a meeting of its creditors. The first and second named defendants were directors and shareholders of the company which, from its statement of affairs of 12th April, 2012, would appear to have been wholly insolvent on that date, in that it reported a deficit of some €2.9m.

5. Mr. Allen had earlier been an employee of the company and in 2009 had instituted proceedings against his employer and the first and second named defendants in respect of the alleged non payment of certain wages and bonus payments. Those proceedings were compromised and by order of the High Court of 28th February, 2012, (Hedigan J.) Mr. Allen obtained a joint and several judgment against the company and the first and second named defendants for a sum of €200,000 together with his costs, the same to be taxed in default of agreement. Notwithstanding repeated demands for payment, the said sum remains outstanding.

6. It later came to Mr. Allen's attention that the first and second named defendants were the registered owners of two apparently unencumbered properties ("the properties"). The properties are those comprised in folios 92684F and 92687F for the County of Galway. As a result, he registered his judgment as a mortgage against the aforementioned lands on 21st March, 2012, and thereafter commenced proceedings seeking to have his judgment mortgage declared well charged thereon.

7. On 20th April, 2012, the company's liquidator, Mr. Conor O'Boyle, through his solicitors advised Mr. Allen that the properties against which he had registered his judgment were properly the property of the company and were not the lawful property of the first and second named defendants. The basis for his claim was advised in that letter; namely, that the company had advanced to the first and second named defendants the sum of €492,500 towards the purchase of the properties on the company's behalf. Thus, he maintained that the company had an unregistered burden on the lands at the time Mr. Allen registered his judgment as a mortgage. Alternatively, he maintained that the properties were held by the first and second named defendants on a resulting or constructive trust for the company.

8. On 9th August, 2012, the company commenced the within proceedings for the purposes of obtaining from the Court, *inter alia*, a declaration that Mr. Allen's judgment mortgage dated 21st March, 2012, was subject to the company's prior unregistered burden on the said folios.

9. Following an exchange of correspondence, wherein he informally sought security for his costs of defending the company's proceedings, Mr. Allen issued a motion on 14th November, 2012, seeking a court order to that effect.

10. In his affidavit sworn on 12th November, 2012, Mr. Allen, having set out the relevant background to the proceedings, asserted

that the company was hopelessly insolvent as was clear from the accounts presented to the creditors meeting of 12th April, 2012. He argued that there was no evidence to support the existence of the unregistered burden or trust contended for by the liquidator and that the proceedings were an effort to frustrate the proceedings he had instituted to have his judgment mortgage declared well charged on the properties. As a matter of law he maintained that even if the company should satisfy the Court as to the existence of an unregistered burden of the nature proposed by the liquidator, this could not oust his legal charge which has been registered in accordance with s. 6 of the Judgment Mortgage Ireland Act 1850.

11. In response, the liquidator maintained first, that the third named defendant had failed to demonstrate that the company would be unable to pay his costs in the event of him successfully defending the proceedings. Secondly, he asserted that Mr. Allen had failed to establish by credible evidence that he had a *prima facie* defence to the proceedings. Finally, he maintained that even if the Court was satisfied as to the first two matters, there were special circumstances which would justify the Court refusing the relief sought. In this regard he relied upon an assertion that Mr. Allen's conduct, while a manager of the company, had caused or contributed to the company's perilous financial state.

12. The first and third of the aforementioned arguments are not pursued by the company on this appeal. Accordingly, it is unnecessary for the Court to engage with them save to say that both claims were little more than bald assertions and that each was wholly unsupported by any credible evidence. In particular, insofar as the liquidator made allegations of professional wrongdoing against Mr. Allen whilst employed by the company, it seems to me highly unlikely that the company and its directors would have consented to judgment in his favour for €200,000 in 2012 if there was even a modicum of truth in that allegation.

13. As to the company's submission that Mr. Allen had failed to establish a *prima facie* defence to the company's claim, the liquidator exhibited a letter of loan sanction addressed to the company dated 20th August, 2007, in order to demonstrate that Allied Irish Bank had loaned the company a sum of €502,000 to enable it purchase, for investment purposes, the properties the subject matter of these proceedings. He also exhibited the company's bank statement showing that this loan remained outstanding to the bank as of the date of his appointment. Accordingly, he maintained that the first and second named defendants had no entitlement to register these properties in their own name.

14. In support of his assertion that Mr. Allen had failed to demonstrate a *prima facie* defence to the company's claim he referred to what he understood to be the legal effect of the facts deposed to in his affidavit. It was his understanding that Mr. Allen's judgment mortgage, not being a charge created on land for valuable consideration within the meaning of s. 68(3) of the Registration of Title Act 1964, was subject to the company's prior unregistered burden. In further support of the company's entitlement to the declaration sought in the proceedings the liquidator relied upon letters which he had received from the first and second named defendants consenting to the orders sought by the company in the proceedings.

Judgment of the High Court

15. Having considered the submissions of the parties and the evidence before him, Murphy J. expressed himself satisfied that Mr. Allen had established that the company would be unlikely to be in a position to pay his costs should he succeed in his defence. He also appears to have been satisfied that there were no special circumstances which would justify the Court failing to grant the relief sought once it was satisfied that Mr. Allen had established a *prima facie* defence to the proceedings.

16. It is not terribly clear from counsels' agreed note of the judgment of the High Court judge as to precisely what he considered to be evidence of Mr. Allen's defence to the proceedings. It is clear that he placed some weight upon the fact that Mr. Allen had obtained a lawful judgment against the company and had validly registered that judgment as a mortgage against the properties. It seems reasonable to infer from his judgment that he considered that the validity of the company's claim depended upon proof of all of the matters referred to by the liquidator in his affidavit and that these were matters which would ultimately affect the priority to be attached to Mr. Allen's judgment mortgage. In other words the High Court judge appears to have taken the view that as of the date of the application the only party with evidence of a charge over the lands was Mr. Allen and that until such time as the company proved that it had a prior unregistered burden, Mr. Allen should be considered to have a *prima facie* defence to the claim.

Submissions of the parties

17. Mr. Kennedy B.L. on behalf of the company submits that the High Court judge erred in law in concluding that Mr. Allen had demonstrated the existence of a *prima facie* defence to the company's claim. First, he submits that in circumstances where the first and second named defendants have agreed to consent to the relief sought in the plenary summons, it is inevitable that any defence that Mr. Allen may seek to advance must fail. Secondly, he maintains that Mr. Allen has not satisfied the burden of proof required of a defendant seeking security for costs, in that he has not referred to any evidence upon which he might rely at the trial to defend the company's claim to a prior unregistered burden on the properties. In this regard he relies upon the fact that Mr. Allen did not file any replying affidavit to contest the averments made by Mr. O'Boyle in his affidavit and that in such circumstances there was no evidence before the Court upon which the High Court judge was entitled to rely for the purposes of concluding that he had established a *prima facie* defence to the proceedings. Finally, he submits that a number of the matters relied upon by Mr. Allen in support of his application are irrelevant. The first of these is Mr. Allen's assertion that on the date of the creditor's meeting no mention was made of the fact that the properties were owned by the company and the second being Mr. Allen's complaint that there was no note or memorandum to support the company's claim to a prior unregistered burden.

18. Mr. Treanor B.L. on behalf of Mr. Allen submits that the High Court was correct to conclude that Mr. Allen had demonstrated that the company was hopelessly insolvent and unlikely to be in a position to discharge his costs should he successfully defend the proceedings. Likewise, he submits that the High Court judge was correct when, having regard to all of the matters on affidavit, he granted the relief sought under s. 390. He rightly concluded that his client had done nothing wrong. Mr. Allen had obtained a judgment and lawfully registered it as a mortgage against the properties. There could be no disputing the lawfulness of his judgment mortgage and his entitlement, in due course, to obtain an order declaring that judgment mortgage well charged on the properties. He submits that the High Court judge did not err in law in concluding that his client had established a *prima facie* defence to the proceedings. The company had yet to prove, by way of evidence, the existence of the unregistered burden which it contends for and his client would dispute that evidence. Counsel submits that, balancing the rights of the parties and in particular having regard to the potential prejudice to his client should the relief sought be refused, this Court should uphold the findings of the High Court judge.

Legal Principles

19. The principles governing the proper interpretation of s. 390 of the Act are not in dispute. These have been rehearsed in many recent decisions including that of Clarke J. in *Connaughton Road Construction Ltd v. Laing O'Rourke Ireland Ltd* [2009] IEHC 7 where he referred to the Supreme Court's adoption of the test, set out by Morris P. in *Interfinance Group Limited v. K.P.M.G. Peat Marwick* (Unreported, High Court, Morris P., 29th June, 1998), in *Usk and District Residents Association Ltd v. The Environmental Protection Agency* (Unreported, Supreme Court, Clarke J., 13th January, 2006) where it was advised as follows:-

"(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
- (b) that the plaintiff will not be able to pay the moving party's costs if the moving party be successful;

(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. 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 defendants 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. The list of special circumstances referred to is not, of course, exhaustive."

20. On this appeal, the Court is only concerned with the very first of these requirements, namely, whether or not Mr. Allen has established that he has a *prima facie* defence to the company's claim. The company no longer seeks to resist the relief sought by reference to the existence of any special circumstances which would justify the Court failing to exercise its discretion in favour of the moving party.

21. What the Court should consider constitutes a *prima facie* defence for the purposes of s. 390 of the Act was considered by Finlay Geoghegan J. in her judgment in *Tribune Newspapers (in receivership) v. Associated Newspapers (Ireland) Ltd.* (Ex tempore, High Court, 25th March, 2011) and later in *Webprint Concepts Ltd v. Thomas Crosbie Printers Ltd* [2013] IEHC 359. In the first of these decisions, as referred to in the latter, she summarised the approach to be adopted by the Court when considering this issue in the following manner:-

"What appears from the judgments, in a manner similar to the judgments in relation to summary judgment, is that a defendant seeking to establish a *prima facie* defence which is based on fact must objectively demonstrate the existence of evidence upon which he will rely to establish those facts. Mere assertion will not suffice.

If such evidence was adduced, then the defendant is entitled to have the Court determine whether or not it has established a *prima facie* defence upon an assumption that such evidence will be accepted at trial. Further, the defendant must establish an arguable legal basis for the inferences or conclusions which it submits the Court may arrive at based upon such evidence."

Discussion.

22. From the aforementioned authorities it is abundantly clear that it is not sufficient for a defendant who seeks an order for security for costs under s. 390 to make a bald averment that he has a defence to the claim made against him. The underlying objective of the section is to afford some protection to a defendant who faces a claim from a limited liability company, which, if unsuccessful in its claim, will have insufficient assets to meet an order for costs made in the defendant's favour. However, to be afforded that protection, the defendant must show that there are reasonable prospects that this is likely to occur because in many circumstances the making of an order for security may render the further pursuit of the company's action a financial impossibility with, in some cases, significant potential adverse consequences to creditors who might otherwise have benefited from a judgment, had the company been in a position to pursue its claim to a full hearing.

The evidence of the third named respondent/defendant in support of his application.

23. The averments in Mr. Allen's affidavit of the 31st March, 2014, insofar as the same are directed to identifying his potential defence of these proceedings, assert the truth of the following matters:-

- (a) That he obtained judgment against the company and the first and second named defendants on the 28th February, 2012, for the sum of €200,000 plus costs;
- (b) that on the 21st March, 2012, he converted that judgment into a judgment mortgage against the properties contained in folios 92684F and 92687F;
- (c) that the lands the subject matter of the aforementioned folios, are registered in the names of the first and second named defendants;
- (d) that, there is no instrument, note or memorandum in existence to support the interest now claimed by the company in these lands;
- (e) that the claim on the part of the company is being pursued for the purpose of seeking to frustrate his lawful claim to have these assets well charged with his judgment mortgage.

24. In response to Mr. Allen's affidavit, the liquidator in his affidavit has put forward strong evidence to support the company's claim to an unregistered burden on these properties, which he maintains has priority over that of Mr. Allen as it existed at the time when he registered his judgment mortgage. He exhibits a letter of loan sanction from Allied Irish Bank dated 20th August, 2007, addressed to the company. Its terms provide that the monies in respect of loan No. 3, that being the loan in question, were to be made available to the company to enable it purchase two investment properties i.e. those properties the subject matter of these proceedings. He deposes to the fact that these monies were used by the first and second named defendants to buy the properties and that the monies remain outstanding to the bank. In this regard he exhibits the relevant company bank statement as of the date of his appointment.

25. In support of the company's claim, the liquidator has also exhibited letters which he has received from the solicitors acting on behalf of the first and second named defendants in which they accept that the company is entitled to the relief which it seeks in these proceedings. From this it is to be inferred that these defendants accept that they wrongfully registered the properties in their personal names in circumstances where the purchase monies were provided by the company.

26. It is these facts which form the basis for the company's claim and Mr. Allen does not dispute the truth or accuracy of any of

them. He does not challenge the origins of the monies used to purchase the properties or the fact that the loan was made available to facilitate the purchase of these investment properties on behalf of the company. Perhaps this is not surprising in circumstances where the letter of loan sanction, which evidences the liquidator's assertions, is addressed to the company c/o Mr. Allen. Mr. Allen has simply put forward no evidence whatsoever that could challenge the validity of the company's claim on these facts.

27. While any court would be best advised to refrain from expressing any overly strong views as to the likely outcome of the litigation on a s. 390 application, because there may be other facts not on affidavit which if established at trial might lead to the successful defence of a claim, it has to be said that the company has produced significant evidence to support its claim and which evidence, at this point in time, remains unchallenged.

28. It is the defendant that bears the burden of proof on a s. 390 application. He must demonstrate that he has evidence, which if accepted at trial, will deny the company the relief it seeks. However, Mr. Allen raises no challenge to the facts deposed to by Mr. O'Boyle in his replying affidavit sworn on 7th December, 2012. The fact that he has obtained a lawful judgment and validly registered his judgment mortgage and is likely to obtain a well charging order at a later date simply does not advance his entitlement to an order for security for costs. A well charging order does not adjudicate on the priority to be afforded to any charge. That is an inquiry that takes place after the making of the order.

29. While Mr. Allen swears that the present proceedings constitute a deliberate effort on the part of the company to frustrate his ability to recover the sums outstanding to him on foot of his judgment, once again he provides no factual or evidential support for that statement. For my part, having regard to the terms of the letter of loan sanction and the apparent acceptance by the first and second named defendants that the properties were bought with company money, it is hard to see how the liquidator's bona fides can be called into question. It appears to me that he has instituted these proceedings so as to ensure that these assets which were ostensibly bought with company money are repatriated to the company so that their value can be made available to the creditors in the course of the liquidation.

30. Insofar as Mr. Allen seeks to rely upon the fact that "there is no instrument, note or memorandum in existence which would support the claim being made by the plaintiff against the assets described in folios GY92684F and GY92687F", that is an averment which does not support the existence of a *prima facie* defence to the company's claim. First, Mr. Allen does not assert as a matter of law that the interest claimed by the company in the properties is one which must to be supported by a note or memorandum in writing. Second, as a matter of fact, it would be quite extraordinary if such a note or memorandum in writing supporting the unregistered burden contended for by the company existed. The company's claim is one which is based upon the wrongdoing of the first and second named defendants in appropriating to themselves investment properties purchased with company money. It is hardly surprising that in such circumstances the company does not have in its possession some memorandum acknowledging its interest in these properties. How could it be expected that the liquidator would have in his possession some document evidencing the existence of the type of unregistered burden or trust which he contends for in these proceedings? The absence of such a memorandum is, in my view, a wholly irrelevant consideration.

31. It is not necessary to deal with Mr. Kennedy's submission to the effect that any defence that Mr. Allen may later deliver is bound to fail by reason of the consent which the company has obtained from the first and second named defendants to the relief claimed in the proceedings. Notwithstanding that agreement, it might nonetheless be open to Mr. Allen to contend for some type of conspiracy between the company and the first and second named defendants to contrive the existence of an unregistered burden so as to defeat his claim, but no evidential basis to support a defence of that nature has been advanced on affidavit.

32. Indeed, it may well be the case that Mr. Allen, based upon facts unknown to the High Court judge or indeed this Court, may be in a position to advance some defence to these proceedings at the trial of the action. I have to say that I find it challenging to identify what that defence might be. However, if such a defence exists the facts to support it have not been committed to affidavit. That is fatal in circumstances where it is a necessary precondition for the party seeking security to identify the evidence available to support the facts which if proven may defeat the plaintiff's claim.

33. I also reject the assertion made by Mr. Allen at paragraph 12 of his grounding affidavit to the effect that, even if the Court should conclude that the company is entitled to an unregistered burden over the properties as alleged, the same is not capable of ousting his legal charge which was registered in accordance with s. 6 of the Judgment Mortgage Ireland Act 1850. Regrettably, that assertion is incorrect as a matter of law. A judgment mortgage is not a charge created on land for what is commonly referred to as "valuable consideration" within the meaning of s. 68(3) of the Registration of Title Act 1964. (See *Re Strong* [1940] I.R. 382, and *Tempany v. Hynes* [1976] I.R. 101). It has long been accepted that a judgment mortgage is no more than a process of execution and, because it is not a charge created for valuable consideration, the judgment creditor takes his interest in the judgment debtor's lands subject to all unregistered rights attaching to the lands at the time when they became charged with the judgment mortgage. That this is so is made clear by the provisions of s. 117 (3) of the Land and Conveyancing Law Reform Act 2009 which, concerning the rights of those who may register a judgment as a mortgage against a judgment debtor's lands provides:-

"(3) The judgment mortgage is subject to any right or encumbrance affecting the judgment debtor's land, whether registered or not, at the time of its registration."

34. I also consider the submission made on Mr. Allen's behalf to the effect that until such time as the Court finds in favour of the company he could be said to have a *prima facie* defence to that claim because he is the holder of the only charge registered against the property, to be one without merit. That submission is misplaced as it fails to recognise the fact that, as already stated, Mr. Allen's interest in the properties was taken subject to any unregistered burdens affecting them at the time when he registered his judgment mortgage. Thus, on the facts outlined in the liquidator's affidavit, the company's unregistered burden, which is supported by evidence that has not been refuted, must, as a matter of law, enjoy priority to that of Mr. Allen's subsequent charge.

Conclusion

35. This is indeed a distressing case, principally because it involves two innocent parties. On the one hand, there is the company and its creditors who have been denied recourse to the properties the subject matter of these proceedings by virtue of what appears, at this juncture, to have been the wrongful acts of the first and second named defendants. On the other hand, there is Mr. Allen who since 2009 has found himself embroiled in costly litigation for the purpose of seeking to recover monies which are due to him by the company and the first and second named defendants. I am sure that when he obtained his judgment in 2012 he could not have predicted that four years later, having apparently registered his judgment as a mortgage against the unencumbered properties of the first and second named defendants, that he would still be chasing recovery of that sum. Nonetheless, in the context of the loan sanction letter which was addressed to him concerning the intended purchase of the properties on behalf of the company, I would be surprised if he did not suspect that the properties against which he registered his judgment as a charge had been purchased with monies borrowed by the company. ,

36. Having considered the evidence that was before the High Court and the submissions of the parties on this appeal, I find myself in the unenviable position of being unable to uphold the decision of the High Court. I am quite satisfied that the High Court judge fell into error in failing to dismiss the third named defendant's application for security for costs on the basis that he had failed to discharge the burden of advancing evidence so as to demonstrate that he has a *prima facie* defence to this claim.

37. For the aforementioned reasons I would allow the appeal.