Neutral Citation: [2016] IEHC 588

THE HIGH COURT

[2013 No. 222 Cos]

IN THE MATTER OF DOHERTY BROTHERS TIMBER COMPANY LIMITED (IN VOLUNTARY LIQUIDATION)

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

AND IN THE MATTER OF SECTION 56 OF THE COMPANY LAW

ENFORCEMENT ACT, 2001

BETWEEN

EAMONN LEAHY

APPLICANT

and

DERMOT DOHERTY, JOHN DOHERTY

and FERGAL DOHERTY

RESPONDENTS

JUDGMENT of Mr. Justice David Keane delivered on the 21st of October 2016

Introduction

1. This judgment concerns an application for a declaration of restriction against each of the respondents, pursuant to s. 150 of the Companies Act 1990 ('the 1990 Act').

Background

2. Doherty Brothers Timber Company Limited ('the company') was incorporated on the 22nd November 1993. It carried on the business of timber merchants and builders providers. At a general meeting held on the 4th May 2011, the members of the company resolved to wind it up voluntarily, being satisfied that it could not continue in business by reason of its liabilities. The members passed a further resolution at that meeting appointing the applicant as liquidator.

3. Each of the three respondents was a director of the company at the date of the commencement of its winding up. The first and second named respondents were directors of the company throughout its existence; the third named defendant became one on the 28th August 2006.

4. On the 14th May 2013, the applicant certified that, both then and on the date of the commencement of its winding up, the company was unable to pay its debts within the meaning of s. 214 of the Companies Act 1963.

5. Between the 2nd November 2011 and the 31st October 2012, the applicant submitted four reports to the Office of the Director of Corporate Enforcement ('ODCE'). By letter dated the 31st January 2013, the ODCE informed the applicant that he was not relieved of his obligation as liquidator of the company to bring a restriction application against each of the respondents.

6. The present application is brought by motion issued on the 15th May 2013, originally made returnable for the 24th June of that year. After an extensive exchange of affidavits, the application was heard on the 26th and 27th November 2015 and judgment was reserved.

7. Although one of the reliefs sought in the applicant's notice of motion was an order, if necessary, pursuant to s. 56(2) of the Company Law Enforcement Act 2001('the 2001 Act'), extending time for bringing an application under s. 150 of the 1990 Act, the applicant confirmed through Counsel at the commencement of the hearing that, while the substantive application was proceeding, the relevant extension of time was no longer being pursued.

The legal issue

8. The respondents do not dispute that the company was unable to pay its debts at the commencement of its winding up. Nor do they deny that they were each a director of the company at the material time or that the Director of Corporate Enforcement has not relieved the applicant of the obligation to bring the present application.

9. It follows that the Court is obliged to make a declaration of restriction under s. 150 of the 1990 Act (now s. 819 of the 2014 Act) in respect of each of the respondents unless satisfied that the conduct of either or both comes within the circumstances set out in sub-s. (2) of that section.

10. The specific issue that arises under s. 150(2) of the 1990 Act is whether each of the respondents acted honestly and, more particularly, responsibly in relation to the conduct of the company's affairs.

The evidence

11. The company traded for a period of approximately eighteen years between 1993, shortly after its incorporation, and March 2011, shortly before the decision was taken to place it in liquidation.

12. The essential details of the company's trading history are not in dispute. The company traded profitably until 2008. In that year it had a turnover of €8 million and a staff of approximately 25 full time employees. As a timber merchant and builders' supplier, trading from a premises at Ashbourne, County Meath, it dealt extensively with builders operating in the greater Leinster area. After the dramatic collapse of the construction sector at about that time, the company made a loss of approximately €100,000 in 2009. In response, it quickly reduced its overheads by half and then progressively reduced them still further until they stood at approximately 15% of their original figure. The company incurred a number of bad debts, standing at more than €1.5 million at the commencement of its winding up. The combination of circumstances just described gave rise to cash flow problems for the company, which in turn damaged its reputation with its own suppliers.

13. The respondents did not hide from these difficulties. Instead, they took suitably drastic action; the company sold four of its five forklift trucks; stopped all expense, bonus and pension payments to directors; brought all cleaning and delivery services in house to save on the external supply of those services; replaced its fleet of company cars with cheaper models; and reduced the size of the premises it was leasing.

14. The respondents believed that, through these measures and the anticipated bottoming out of the downturn in the construction industry, the company would be able to continue to trade, albeit at a more modest level. However, severe weather in December 2010 further hampered activity in the construction sector, which, in turn, further adversely affected the company's trade. The respondents sought professional advice in early 2011. Upon consideration of that advice and after consultation with the company's bankers, the respondents resolved to liquidate the company.

15. The scale of the difficulties that the company encountered are vividly illustrated by the decline in its turnover from €11.9 million in 2006/2007 to €1.8 million in 2010/2011, a fall of over 85%. The company's financial statements disclose that it made profits of €251,237 in 2007; €9,664 in 2008; and a loss of €119,771 in 2009. The applicant estimates that the company made further losses of approximately €153,792 in the year to the 28th February 2010 and €238,730 in the year to the same date in 2011.

16. At the commencement of the winding up, the company had realisable assets of €27,792, preferential creditors amounting to €210,424 and unsecured creditors amounting to €1,706,645, giving rise to an estimated total deficiency of €1,889,531 before the costs of the liquidation are taken into account.

17. The company has a liability to the Revenue Commissioners of some €189,843, comprising €84,728 in unpaid VAT and €105,115 in respect of unpaid PAYE/PRSI. The company ceased to file VAT returns after the period November/December 2010 and ceased to pay its VAT liabilities with effect from the end of the period January/February 2010. The company filed all PAYE/PRSI returns up to March 2011 and, having paid €6,000 per month in respect of its PAYE/PRSI liabilities to the end of June 2010, ceased to make any such payments after that date.

18. The company filed its annual return in the Companies Registration Office until 2009. Its last return was submitted in November 2009 and included the company's accounts for the year ending on the 28th February 2009. The company failed to submit its return for 2010 or its accounts for the year ending the 28th February 2010 by the required deadline in December 2010.

The factual issue

19. While the applicant very properly drew attention to the company's failure to make the appropriate Companies Registration Office and tax returns during the final phase of its existence, and its failure to make the appropriate tax payments during that period, he did not press the argument that this was sufficient to preclude the respondents from establishing that they acted honestly or responsibly in the conduct of the company's affairs, having regard to the particular circumstances in which those failures occurred.

20. In adopting that course, no doubt he had in mind the frequently quoted passage from the judgment of Finlay Geoghegan J. in *Digital Channel Partners* [2004] 2 ILRM 35 at 40 to the effect that the mere fact that a company is in breach of its obligations in that regard for a relatively limited period will not, of itself, indicate dishonesty or irresponsibility on the part of its directors, without something more.

21. The specific factual issue that the applicant did raise, refined in the course of argument, is whether each of the respondents can satisfy the court that he acted responsibly as a director in relation to the conduct of the company's affairs in permitting the company to continue to operate between the Spring or Summer of 2010, at which point the applicant contends the company was clearly insolvent, and March 2011, when the company ceased trading.

The applicant's position

22. The applicant invites the Court to have regard to the three types of situation that a court is typically required to consider in s. 150 applications, as those situations were described by Clarke J. in *Re Swanpool Ltd; McLaughlin v Lannen* [2006] 2 ILRM 217 at 223. The applicant submits that the issue he has raised falls to be considered within the rubric of the second type of situation contemplated, in that it relates to 'the commercial management of the company most particularly at the period when the company was insolvent or heading in that direction.' In making that submission, the applicant acknowledges, as Clarke J. pointed out, that mere commercial misjudgement would not be enough in that context, it would be necessary to establish 'gross mismanagement.' This, in turn, echoes the conclusion of McGuinness J. in the Supreme Court appeal in *Re Squash (Ireland) Ltd* [2001] 3 IR 35 that 'commercial errors may have occurred, misjudgements may well have been made; but to categorise conduct as irresponsible I feel that one must go further than this.'

23. Undeterred, the applicant invokes the following well-known dictum of MacMenamin J. in *Re MDN Rochford Construction Limited; Fennell v Rochford & Anor* [2009] IEHC 397 (at para. 50):

> "While each case must be judged on its facts, there comes a point where optimism becomes hubris, and where belief that a company can trade out of its difficulties is simply wilful self-delusion. Commercial acumen is necessary. Hope must be matched by verification and objectivity. The absence of all of these necessary characteristics constitutes irresponsibility.'

24. For the purpose of completeness, I should say that it was at one stage of the application mooted that there may also be an issue coming within the third type of situation described by Clarke J. in *Re Swanpool*, namely, one where there was a question of 'compliance by the directors with the obligations identified [by the Supreme Court] in [*Re Frederick Inns Ltd* [1994] 1 ILRM 387] to ensure that, once the company was facing insolvency, its assets were dealt with in a manner designed to ensure the proper distribution of those assets in accordance with insolvency law.'

25. There appears to have been a suggestion that the respondents caused the company to acquire goods on credit from its suppliers during the final phase of its trading life in order to allow it to effect sales for the ulterior purpose of enabling the preferential repayment of the company's invoice finance facility with Bank of Ireland, in circumstances where that facility was the subject of a personal guarantee from the first and second named respondents. That allegation or assertion was trenchantly denied by the respondents who contend that they were unable to obtain any significant fresh or additional credit from most of their suppliers during the relevant period in view of both the prevailing economic situation and the company's own financial circumstances during the period in question. Despite considerable forensic efforts on the part of the applicant, including the preparation or recreation of an extensive aged debtor analysis and a consideration of the company's stock levels over the period at issue as disclosed in its accounts, the evidence before the Court falls far short of permitting any conclusion to be drawn that the respondents engaged in, or caused the company to engage in, any such conduct.

The respondents' position on the issue raised
26. The respondents deny that they were irresponsible in causing the company to continue to trade between the Spring or Summer of 2010 and March 2011 or that they failed to have appropriate regard to the position of the company's creditors during that period. They point to the uncontroverted evidence that the company addressed the losses it incurred in both 2009 and 2010 by making drastic cost reductions; that, until November 2010, the company was engaged in meaningful discussions with its bankers and with its invoice finance provider to secure the credit facilities necessary to keep the company afloat; and that the company had retained the services of a professional consultant throughout that year to assist it towards that end.

27. The respondents rely on the dictum of the Supreme Court (*per* McGuinness J.) in *Re Squash (Ireland) Ltd* that, in considering whether a director has acted responsibly, the Court should have regard to the entire tenure of the director and not merely the months in the run up to the liquidation. In this case, the evidence is that, under the stewardship of the respondents, the company had a perfect revenue record for over sixteen years.

Conclusion on the issue raised
28. Having considered carefully the evidence presented in this case and the arguments advanced by the parties, I have come to the conclusion that, having due regard to the entire tenure the respondents as directors of the company and to the uncontroverted evidence of their engagement with professional advisers and financial institutions throughout the period at issue, albeit subject to some disagreement about the precise nature and extent of that engagement, the respondents have satisfied me that, although they undoubtedly made commercial errors and misjudgements in the twilight period of the company's existence, they have acted responsibly in relation to the conduct of the company's affairs.

Other matters
29. It would be wrong to conclude without expressly recording the Court's rejection of certain criticisms that the respondents made of the applicant's conduct of the liquidation in general and of his presentation of the present application in particular.

30. The respondents devoted a considerable, one might easily say disproportionate, amount of their evidence on affidavit to criticism of the applicant for his perceived failure to provide them with what they consider to be the information and material necessary to defend the present application. In particular, they point to the failure of the liquidator to retrieve the company's computer servers from the information technology company to which the third named respondent had returned them at around the time the company entered liquidation. They criticise the liquidator for failing to exercise his powers under s. 244A of the Companies Act 1963, as amended, to retrieve the information stored on those servers (presumably, as a 'document' or 'book of account') from that company. They further criticise the liquidator for failing to locate certain back-up disks containing the relevant information, which they say were left at the company's premises.

31. However, I find the third named respondent's explanation for his apparent solicitude in moving with such alacrity to assist that other company in removing its servers from the company's premises at the commencement of the liquidation to be incomplete and unconvincing. I question why no steps were taken to retrieve the company's information from those servers and to secure it before doing so. I think it is reasonable to wonder why nothing is said concerning any practical assistance offered to the liquidator to locate the back-up disks, which the directors say were left in the company's premises. The respondents' deprecation of the applicant's asserted failure to exercise his powers to retrieve the information on the servers from that other company takes no account of the applicant's evidence that, upon making inquiry, he was informed that the servers concerned had already been scrapped or stripped for parts.

32. As the foregoing observations suggest, I take the view that the relevant controversy raises much more obvious questions about the respondents' conduct after the commencement of the liquidation than it does about that of the applicant. That conduct might have warranted consideration of whether a declaration of restriction is appropriate on the 'just and equitable' ground in respect of the respondents failure to co-operate with the applicant as liquidator, had the applicant chosen to press the matter; see, for example, the judgment of Shanley J. in *La Moselle Clothing Ltd and Rosegem Ltd v Soualhi* [1998] 2 ILRM 345 at 353.

33. Nor do I accept the respondents' submission that the decision of Barrett J. in *Re Gleneagle Woodcrafts Ltd; Hughes v Caffrey & Anor* [2014] IEHC 366 casts an additional onus on the applicant, as liquidator, to provide them with information in the manner for which they contend. It is clear that, in the context of a s. 150 application, the liquidator's role is more obviously that of information provider to the Court than that of adversarial litigant in the true sense. I understand the relevant observations of Barrett J. in that case to go no further than that, insofar as the liquidator believes he has information – in the form of evidence – to offer on the issue of a respondent's honest or responsible conduct in relation to the conduct of the affairs of the company concerned, he should properly explain the relevance and significance of that evidence, as he perceives it, to the determination of that issue.

34. I reject also the submission made on behalf of the respondents that the Court should have regard to the fact, if fact it be, that significant parts of the evidence contained in the affidavits sworn, and relied upon, by the applicant comprise inadmissible hearsay of the kind expressly disapproved of by the Supreme Court in *Re Bovale Developments Ltd* [2011] 3 I.R. 279. The parties to the present application exchanged what was, by my reckoning, a total of 15 affidavits between the 14th May 2013 and the 8th January 2015. Any objection to the admissibility of any evidence contained in any of those affidavits should have been raised, with the necessary particularity, in good time prior to the hearing of the application, as was done in *Bovale Developments*, and not as a nebulous submission on the merits of the application in the course of the hearing itself.

35. On the basis of the conclusions that I have reached on the issues as I perceive them, it is unnecessary to express any view on the question of the significance, if any, of the delay in bringing the present application and I do not propose to do so.

Conclusion
36. For the reasons I have given, each of the respondents has satisfied me that he acted honestly and responsibly in relation to the conduct of the company's affairs and, accordingly, I must decline to make the declaration of restriction sought.