Neutral Citation: [2016] IEHC 177

THE HIGH COURT

[2014 No. 304 COS]

IN THE MATTER OF GINGERSNAP LIMITED (IN VOLUNTARY LIQUIDATION)

[2014 No. 305 COS]

AND IN THE MATTER OF SCAPPA 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 ENFORCEMENT ACT 2001

BETWEEN

EAMONN LEAHY

APPLICANT

AND

DECLAN DOYLE and BREDA DOYLE

RESPONDENTS

JUDGMENT of Mr. Justice David Keane delivered on the 8th April 2016

Introduction

1. Each of these two sets of proceedings comprises an application for a declaration of restriction against each of the respondent company directors under s. 150 of the Companies Act 1990, as amended ("the 1990 Act"). In each case, while the companies are, of course, different, the liquidator is the same and the respondent company directors are the same. It is not in dispute that Gingersnap Limited ("Gingersnap"), Scappa Limited ("Scappa") and two other companies named Amatrek Limited ("Amatrek") and Combloux Limited ("Combloux") form part of the same group of companies and that Combloux was the parent of both Gingersnap and Scappa. The respondents are husband and wife, although – in the circumstances of the present case – nothing turns on the fact of that relationship.

Gingersnap

2. Gingersnap was incorporated on the 18th December 1998. Both respondents became directors of the company on the 31st March 2001 and each continued to act in that capacity until the company went into liquidation by resolution of its members at a general meeting held on the 27th March 2013.

3. Gingersnap was set up to operate a public house and nightclub named "Redz", which commenced trading in April 2003 from the basement floor of premises at 1-5 D'Olier Street, Dublin 2 in which the company had acquired a leasehold interest. In 2004, the company purchased the freehold interest in Bowe's public house in Fleet Street, Dublin 2 with loan finance secured by a fixed charge over that property and commenced trading from that premises also. In 2009, Gingersnap leased the Bowe's premises in Fleet Street to Scappa, another group company, at an annual rent of €50,000. On the 15th October 2012, Gingersnap sold the Bowe's premises to Amatrek, yet another group company, for €750,000.

4. In December 2009, Gingersnap closed the Redz premises for refurbishment as it was becoming dilapidated. At that time, those premises had a weekly turnover of approximately €50,000. The company acquired an additional lease for the ground floor portion of the same building and, in 2010, it obtained planning permission for the refurbishment of the expanded premises over two floors. The refurbishment work was carried out and the premises reopened in April 2011, trading during normal pub hours under the new name "Lafayette's", with a new emphasis on the food trade and now targeting as its clientele the large number of office workers employed in the immediate vicinity. Unfortunately, the new incarnation of the business was not a success, failing to attract the level of custom anticipated and only generating a weekly turnover of approximately €17,000. The company ceased trading on the 31st December 2012.

5. The applicant avers that Gingersnap's financial statements for the year ended the 31st January 2010 and its internal books and accounts for the three subsequent annual financial periods establish that it made the following losses: €312,494.58 in 2009; €81,028.32 in 2010; €606,137.76 in 2011; and €2,740,308.81 in 2012.

6. In the statement of affairs laid before the creditor's meeting, the directors estimated that Gingersnap had no realisable assets and that it had debts to preferential creditors of €207,913 and debts to non-preferential creditors of €5,787,310, giving rise to a total estimated deficiency of €5,995,223.

Scappa

7. Scappa was incorporated on the 17th January 2005. Both respondents were its directors from that date until it went into liquidation by resolution of its members at a general meeting held on the 30th May 2013.

8. The company commenced trading in July 2009 when, as already described, it entered into a lease agreement with Gingersnap to operate the Bowe's licensed premises at an annual rent of €50,000.

9. In September 2012, Scappa failed to obtain a tax clearance certificate. As the possession of such a certificate was both a condition precedent to the renewal of the liquor licence attached to the premises and a condition of Scappa's lease with Gingersnap,

the company's lease was extinguished. As already noted above, Gingersnap then sold the freehold in the Bowe's premises to Amatrek, another company in the same group, for a consideration of €750,000. It would appear that this was done with a view to Amatrek obtaining a licence for the sale of intoxicating liquor on the premises, thereby continuing the operation of that public house.

10. The applicant avers that Scappa's financial statements and its internal books and accounts disclose that the company made a loss in every year of its trading life. It lost €37,030.00 in 2009; €78,508.00 in 2010; €26,430.33 in 2011; and €110,883.45 in 2012.

11. In the statement of affairs that the first respondent furnished to the creditor's meeting, he estimated that Scappa had no realisable assets; an issued share capital of just €100; debts to preferential creditors of €49,153; and debts to unsecured creditors of €292,458, representing a total estimated deficiency of €341,711, before taking into account the costs of the liquidation.

Grounds for resisting restriction

12. It is not contested that neither Gingersnap nor Scappa was able to pay its debts at the commencement of its winding up. Nor is it denied that each of the respondents was a director of each of those companies 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 Company Law Enforcement Act 2001 ("the 2001 Act") to bring the present application against each respondent in respect of each of the two companies.

13. It follows that the Court is obliged to make a declaration of restriction under s. 150 of the 1990 Act against each of the respondents in each set of proceedings unless satisfied that the position of one or both of them comes within one of the circumstances set out in s. 150 (2) of that Act. In light of certain averments made by the first respondent in affidavits that he has sworn on behalf of both respondents, in effect requesting the court to exercise "its discretion" not to restrict either of them, it is perhaps important to emphasise that the making of a restriction order for a five-year period is mandatory where the circumstances identified in ss. 149 and 150 of the 1990 Act are established and where none of the defences under s. 150 (2) of that Act is found to apply - there is no discretion vested in the Court to refrain from making the appropriate declaration in such an event.

14. The respondents do raise an affirmative defence under s. 150 (2) of the 1990 Act in each case. Specifically, they contend that the court should be satisfied that they have each acted honestly and responsibly in relation to the conduct of the affairs of each company and that there is no other reason why it would be just and equitable to restrict either of them.

15. The applicant acknowledges that no issue of dishonesty on the part of either respondent arises on the evidence presented and I accept that that is so. The issue, therefore, boils down to the one that most often arises in applications of this kind viz. whether each of the respondents acted responsibly as a director in relation to the conduct of the affairs of each company.

16. In suggesting that neither respondent did so in relation to the affairs of Gingersnap, the applicant principally relies on three matters. The first is that Gingersnap operated its licensed premises in D'Olier Street without a liquor licence from the time those premises reopened in April 2011 until the business ceased trading on the 31st December 2012. That occurred in circumstances where Gingersnap had been unable to obtain a tax clearance certificate from the Revenue Commissioners in or about September 2010 and could not renew its liquor licence as a result.

17. The second matter relied upon by the applicant is that the respondents permitted Gingersnap to accrue a liability of €212,611 to the Revenue Commissioners between April 2011 and the commencement of the company's winding up in March 2013. That liability comprises €106,354.25 in unpaid PAYE and PRSI going back to April 2011 and €106,131.00 in unpaid VAT for the period from the end of April 2012 onwards (in circumstances where the VAT liabilities that arose in the ordinary course of trade from the re-opening of the premises in April 2011 until the VAT period March/April 2012 were effectively balanced by the VAT refunds to which Gingersnap was entitled arising from its expenditure on the refurbishment works that had been carried out on the D'Olier Street premises, leaving no net payment due for any of those periods). In other words, the payments that Gingersnap made in respect of its net VAT and PAYE/PRSI liabilities from its resumption of trade in April 2011 were negligible. The respondents do not deny that, at the creditor's meeting that took place on the 27th March 2013, the first respondent acknowledged that the monies due to the Revenue Commissioners in respect of VAT and PAYE/PRSI had been used to cover the company's "running expenses."

18. The third matter is that Gingersnap failed to make the necessary annual returns for any period after the year ended 31st January 2010.

19. In suggesting that neither of the respondents acted responsibly in relation to the conduct of the affairs of Scappa, the liquidator points to the following matters. First, the respondents, as the controllers of the Combloux group of companies, have walked away from the debts of their failed company Scappa by placing it in liquidation, while continuing to operate the same business (that of Bowe's public house) from the same premises through another company they control, Amatrek, thereby availing once again of all of the advantages of limited liability. The liquidator submits that this amounts to a classic instance of the so-called 'phoenix syndrome', one of the principal problems that the statutory duty to restrict directors was created to address.

20. Second, the respondents permitted Scappa to trade while insolvent throughout the period from 2010 until it entered liquidation in May 2013.

21. Third, the respondents permitted Scappa to accrue a liability of some €154,865.00 to the Revenue Commissioners over a period of some years. That liability comprises €98,817.00 in unpaid VAT and €56,048.00 in unpaid PAYE and PRSI. As regards VAT, Scappa filed no bi-monthly returns for both the 2011 and 2012 periods until the 31st January 2013, save for the period March/April 2011 in respect of which a return was submitted on the 16th June 2011. In 2011, the company paid €27,744 solely directed towards VAT liabilities that had arisen between 2008 and 2010. In 2012, the company made no payments whatsoever towards the discharge of its VAT liabilities. As regards PAYE and PRSI, the company filed returns for the year 2010 on the 15th June 2012 and for 2011 on the 31st January 2013, in each case long past the due date of the 15th February of the year following each period. In 2011, the company paid €12,265 in PAYE and PRSI which went mainly, if not entirely, towards liabilities incurred in 2010. In 2012, the company paid €2,286 toward PAYE and PRSI, which also went towards liabilities incurred during 2010.

22. Accordingly, the liquidator notes that Scappa was permitted to trade during 2011 and 2012 primarily at the expense of the Revenue Commissioners, as well as at that of other creditors. Indeed, once again the respondents do not deny that, when questioned by a representative of the Revenue Commissioners at the creditors' meeting that took place on the 30th May 2013 concerning what became of the fiduciary taxes due owed to the Revenue, the first respondent acknowledged that they "were used to keep other companies in the group afloat."

23. None of these matters is seriously disputed by either of the respondents in respect of either company.

24. Instead, the respondents invite the court to have regard to certain other asserted facts in considering whether to make a declaration of restriction. Those asserted facts include the following:

> (a) Neither respondent took a salary as director of Gingersnap after that company's D'Olier Street trading premises closed for refurbishment at the end of 2009 or the beginning of 2010.
>
> (b) Gingersnap provided employment for approximately 25 people and directly paid those persons their entitlements when it ceased to trade.
>
> (c) The respondents personally guaranteed some €3,078,307 of Gingersnap's indebtedness. The first respondent baldly avers that the continued employment of the staff currently working in Bowe's public house and of the staff working in another public house named 'Doyle's' is contingent upon his escaping a declaration of restriction because – for reasons that are not explained – the continued employment of those persons is said to depend upon the successful renegotiation of the respondents' indebtedness under the relevant guarantee(s). The first respondent further avers without explanation that this renegotiation can only succeed if he remains actively involved in the management of those premises, and that his continued involvement in the management of those premises will only be possible if he is not restricted as a director.
>
> (d) No other issue of irresponsibility or misconduct has been raised in respect of either respondent whether as director of Gingersnap during any other part of its prior trading history from 2003 onwards or as director of Scappa during the trading history of that company.
>
> (e) No prior issue of non-compliance in respect of Gingersnap's PAYE/PRSI obligations arose between 2003, when it commenced trading, and 2011.
>
> (f) Scappa's insolvency arose not through any irresponsibility on the part of the respondents but because it was called upon to provide monies to Gingersnap when the latter fell into financial difficulty and the advances it provided were never repaid.
>
> (g) In taking over the business of Bowe's public house, Amatrek was not a 'phoenix company' because it had been incorporated many years previously in 1994.
>
> (h) The second named respondent was merely a non-executive director of each company, albeit – as Counsel on her behalf conceded - a person directly involved in the catering side of the business and, as she did not dispute, an experienced publican in her own right.

Issues of fact

25. Before considering the matters to which it is appropriate to have regard in determining whether each respondent has acted responsibly as a director of each company for the purpose of s. 150 of the 1990 Act, it seems to me that there are two contested issues of fact that I must address. The first is whether, as the first respondent informed the creditors' meeting of Scappa and as he has subsequently sworn on affidavit in opposition to the present application, Scappa's insolvency was precipitated by the need to make financial advances to Gingersnap that subsequently proved irrecoverable and, if so, how that affects the question of what responsibility, if any, the respondents bear for Scappa's insolvency and its net deficiency of assets. The second is whether the acquisition of the business of Bowe's public house from Scappa by Amatrek represents an instance of the 'phoenix syndrome' and, if so, what the significance of that might be for the purpose of the present application. I propose to address each of those issues in turn.

26. In the written statement that he presented to the creditors' meeting of Scappa on the 30th May 2013, the first respondent asserted, in material part, as follows:

> "[Gingersnap] got into financial difficulties in 2011 and it called on monies from group companies to cover losses arising in that company and [to] pay for fit out costs.
>
> In late 2012 it was clear that those advances were not going to be recovered and that debts building in this company were not going to be settled."

27. In the affidavit that he swore in opposition to the present application on the 16th December 2014, the first respondent repeated that assertion on oath in the following terms:

> "8. I say that in 2011, Gingersnap Limited was in financial difficulty and called on monies from group companies to cover losses arising in it and to cover some of the financial costs of the refurbishments.
>
> 9. In late 2012 it became clear that the company's advances to Gingersnap Limited were not going to be recovered and thus debts owed to the Revenue Commissioners could not be sufficiently discharged."

28. The applicant, very pertinently in my view, makes two observations in response to these claims. First, he points out that they are nowhere supported in Scappa's accounts. On the contrary, the information available is that Scappa was consistently indebted to Gingersnap during the relevant period. It owed Gingersnap €159,527.74 at the beginning of 2011; €162,714 in 2012; and €136, 869 in 2013. Scappa's accounts record no asset in the form of any debt due to it from Gingersnap in respect of monies previously advanced by the former to the latter. Obversely, Gingersnap's accounts for the relevant period show no evidence of a liability in the form of any such debt due to Scappa.

29. Second, the applicant enquires rhetorically whether, even if it were accepted in the face of the available evidence that Scappa advanced monies to Gingersnap of sufficient magnitude to render the former insolvent when the latter failed to repay them, it could have been responsible conduct for the directors of Scappa to permit that to occur, in circumstances where Scappa never managed to trade at a profit and where during the period in question it consistently failed to remit to the Revenue Commissioners the PAYE/PRSI it was deducting from its employees wages and the VAT it was collecting from its customers.

30. I have come to the conclusion that both of these points are well taken by the applicant. There is no sufficient evidence to satisfy me that the reason for the commercial demise of Scappa was that it made very substantial – or, indeed, any - advances to

Gingersnap that proved irrecoverable. And even if it had done so, it is difficult to see how that might avail the respondents when it would seem instead to provide compelling evidence of the directors' responsibility to that extent for Scappa's insolvency and net deficiency of assets.

31. The other factual issue in controversy between the parties is the extent to which the acquisition of the business of Bowe's public house by Amatrek, a company controlled by the respondents, represents an instance of the 'phoenix syndrome.' In Courtney, T*he Law of Companies*, 3rd ed. (Dublin, 2012) (at p. 1790), citing the *Report of the Working Group on Company Law Compliance and Enforcement* (1998), the 'phoenix syndrome' is defined as "the situation where the controllers of a company, which becomes insolvent by reason of their acts or omissions, walk away from their failed company (and especially their debts) and immediately re-establish themselves in a new company doing the same business, again availing of all of the advantages of limited liability."

32. The respondents' argument appears to be that this is not such a situation because Amatrek was incorporated in 1994, almost twenty years before that company acquired the business at issue. In that regard, I will limit myself to the comment that whether the controllers of a failed business that has become insolvent by reason of their acts and omissions walk away from their debts and re-establish themselves in the same business through a pre-existing company they control or a new one they establish does not seem to me to be the pivotal consideration in relation to whether those events fall within the definition of the objectionable commercial phenomenon described as the 'phoenix syndrome.' However, it is not necessary to resolve that question in circumstances where the test posited under s. 150 (2) of the 1990 Act is directed towards the conduct of the directors of an insolvent company in relation to the affairs of that company regardless of whether – and, if so, in what guise – the business it had previously conducted subsequently emerges phoenix-like from the ashes under the effective control of the same persons through a different corporate vehicle, old or new.

Analysis

33. I turn now to consider whether each of the respondents acted responsibly in relation to the conduct of the affairs of each company. I propose to do so in light of those considerations which seem to me most apposite from the list of relevant factors identified by Shanley J. in *Re La Moselle Clothing Ltd and Rosegreen Ltd* [1998] 2 ILRM 345 (at 352).

34. In the case of both companies, significant issues of lack of commercial probity and want of proper standards plainly arise. Each company failed to pay the taxes due from it to the Revenue Commissioners over a protracted period of time. Gingersnap incurred a liability of €212,611 to the Revenue Commissioners between April 2011 and the commencement of the company's winding up in March 2013. Scappa accrued a liability of some €154,865.00 to the Revenue Commissioners over a period of some years.

35. In my view, this was not in either case the sort of limited failure to make tax returns and failure to pay tax liabilities over a limited period that was envisaged by Finlay Geoghegan J. in *Re Digital Channel Partners Limited* [2004] 2 ILRM 35 (at 40) as not, in itself, sufficient to demonstrate irresponsibility. Rather, it was very much closer to what was described in that case as "a decision to effectively seek to use taxation liabilities for the purpose of financing a company, that of itself will normally be indicative of the fact that the directors have been acting at least irresponsibly." It will be recalled that the respondents have acknowledged in respect of the monies deducted by each company from its employees' wages for PAYE/PRSI and charged by each company to its customers for VAT that Gingersnap used those monies to cover its "running expenses" and Scappa used them "to keep other companies in the group afloat."

36. While I fully accept that the failure of each of the two companies in that regard was not as egregious as that considered by McCracken J. in *Re Verit Hotel and Leisure (Ireland) Ltd: Duignan v Carway et al* (23rd January 2002, unreported, HC), I am satisfied nevertheless that it amounted in each case to a conscious and deliberate decision to use the monies due to the Revenue Commissioners to keep each company going over an extended period of time, amounting to a level of irresponsibility sufficient in itself to justify the making of a restriction order.

37. In addition, the fact that Gingersnap was permitted to trade without the necessary liquor licence for a period of approximately 21 months also demonstrates, in my view, a lack of commercial probity and want of proper standards on the part of each of the respondents as directors of that company.

38. I am also satisfied that each of the respondents bears a significant responsibility for the net deficiency in the assets of each company at the date of the commencement of its winding up in that I find as a fact that each respondent permitted each company to trade for some years while insolvent and, as already stated, to use monies properly due to the Revenue Commissioners for that purpose.

39. While I fully accept, as McGuinness J. pointed out in *Re Squash (Ireland) Ltd* [2001] 3 IR 35, that when considering whether a director has acted responsibly the director's entire tenure should be taken into account, it seems to me that neither the respondents' personal financial exposure on foot of guarantees they provided in respect of Gingersnap's borrowing; nor the decision of each to forego a salary as director of Gingersnap from 2010 onwards; nor the employment that the businesses concerned provided prior to becoming insolvent; nor the compliance of each company with its taxation and regulatory obligations at some point in the past is capable of displacing the finding of irresponsibility that I have been obliged to make in respect of each respondent as director of each company by reference to the specific issues that have been identified and addressed above.

40. I should add that, even if I were to accept the first respondent's unsupported assertion that the continued employment of the entire staff of two separate public houses is unequivocally dependent upon his not being made the subject of a declaration of restriction under s. 150 of the 1990 Act, there would still be nothing I could do in the face of the findings that I have made that he has acted irresponsibly in relation to the conduct of the affairs of two separate companies. That is because, as has already been noted, there is no discretion vested in the Court to refrain from making the appropriate declaration in that event.

41. Finally, I have given careful consideration to the particular position of the second respondent as a non-executive director of each company. It seems to me that, even on the most narrow view of the common law duties owed to a company by a non-executive director, the lack of oversight in this case in respect of the lengthy period during which each company was permitted to trade while insolvent and the lack of commercial probity and want of proper standards involved in permitting the persistent and continuing diversion of fiduciary taxes to fund the companies' trading and, in the case of Scappa, to fund the trading of other companies in the same group, amounts to a breach of those duties and is, in consequence, irresponsible conduct.

Conclusion

42. For the reasons I have set out, I will make the declaration sought in each case against each respondent.