

THE HIGH COURT

[2022] IEHC 161

Record No. 2019/388 COS

IN THE MATTER OF RED HERRING SEAFOOD LIMITED
(IN LIQUIDATION)
AND IN THE MATTER OF
SECTIONS 682 AND 819 OF THE COMPANIES ACT 2014

BETWEEN

DAVID KENNEDY

APPLICANT

-AND-

SADIA AZIZ AND MAZHAR ALI BAIG

RESPONDENTS

JUDGMENT of Mr. Justice Quinn delivered on the 21st day of March, 2022

1. The applicant was appointed liquidator of Red Herring Seafood Limited ("the Company") by resolution of the Company on 1 May, 2018.
2. The applicant seeks a declaration of restriction in respect of each of the respondents pursuant to the provisions of s. 819 of the Companies Act, 2014 ("the Act"). Section 819 provides as follows: -

"819. (1) On the application of a person referred to in section 820 (1) and subject to subsection (2), the court shall declare that a person who was a director of an insolvent company shall not, for a period of 5 years, be appointed or act in any way, directly or indirectly, as a director or secretary of a company, or be concerned in or take part in the formation or promotion of a company, unless the company meets the requirements set out in subsection (3).

(2) *The court shall make a declaration under subsection (1) unless it is satisfied that—*

 - (a) *the person concerned has acted honestly and responsibly in relation to the conduct of the affairs of the company in question, whether before or after it became an insolvent company,*
 - (b) *he or she has, when requested to do so by the liquidator of the insolvent company, cooperated as far as could reasonably be expected in relation to the conduct of the winding up of the insolvent company, and*
 - (c) *there is no other reason why it would be just and equitable that he or she should be subject to the restrictions imposed by an order under subsection (1)."*
3. The requirements identified in subsection 3 are that any company of which a restricted person shall be appointed a director or be concerned in its formation or promotion must have an allotted and paid up capital of not less than €500,000 in the case of a public limited company or €100,000 in the case of any other company.
4. Section 682 of the Act imposes on every liquidator of an insolvent company an obligation to make a report to the Director of Corporate Enforcement ("the Director") in a prescribed

form and to provide such information or assistance as the Director may require for the purpose of the Director's appraisal of the report.

5. Section 683 confers on liquidators an obligation to bring applications for restriction pursuant to the provisions of s. 819. It provides as follows: -

"683. (1) In this section—

- (a) "insolvent company" has the same meaning as it has in Chapter 3 (restrictions on directors of insolvent companies) of Part 14; and*
- (b) a reference to a director of the insolvent company is a reference to a person who was a director or shadow director of the company at the date of, or within 12 months before, the commencement of its winding up.*

(2) In a winding up of an insolvent company, where this subsection applies, the liquidator shall apply under section 819 (1) for a declaration under that provision in respect of each of the directors of the company.

(3) As respects subsection (2)—

- (a) that subsection applies unless the Director (being the Director of Corporate Enforcement) has relieved the liquidator of the obligation to make the application under section 819 (1) in relation to the winding up concerned or a particular director or directors (which power to so relieve is conferred on the Director by this paragraph), and*
- (b) where the Director relieves the liquidator of that obligation in respect of one or more but not all of the directors, that subsection shall be read as applying to the director or directors as respects whom the liquidator has not been relieved of that obligation."*

Subsection 4 provides that the application for restriction must be brought within two months from the date in which the Director has notified the liquidator that he has not relieved the liquidator of the obligation to make the application, or such greater period of time as the Director may allow.

6. The Company was incorporated on 20 September 2016 and its principal business was the operation of a seafood restaurant in Clonmel, County Tipperary. It traded from September 2016 to 2 April 2018. On 1 May 2018 the applicant was appointed liquidator.

Affidavits

7. This application is grounded on an affidavit sworn by the applicant on the 11th October, 2019.
8. The second respondent swore a replying affidavit on 28 January 2020 and the third respondent swore a replying affidavit on 8 November 2021.

9. At the hearing the court was informed that the applicant had sworn a second affidavit on 3 November 2021. That affidavit had not been served on the respondents sufficiently in advance of the hearing and the applicant agreed that he would not rely on it. This is of significance because there is no evidence proffered by the applicant to contradict the detail contained in the respondents' affidavits.

Affidavits of non-parties

10. Also before the court were affidavits sworn on 24 February, 2020 by three persons who are known personally to the second named respondent. These affidavits are of limited assistance to the court for the reasons which follow. Nonetheless I shall, for completeness, refer to their contents before moving to the substantive evidence.
11. Catherine O'Donnell states that she has known the second respondent for over three years. She worked in the Red Herring Restaurant from January 2017 to September 2017 when she moved to Mani Restaurant, which is operated by a different company of which the second named respondent is a director. She is still employed at that restaurant. Ms. O'Donnell states that she was not aware of any issues with staff or suppliers at the Company but became aware towards the second half of 2017 that its business was struggling. Ms. O'Donnell says that she has never been aware of any issues with staff or payments to suppliers at Mani Restaurant. She observes that the second respondent is a man committed to providing employment in the local area and making the work environment safe and productive. She says that the second respondent has been understanding of and supportive of her in dealing with certain health issues. She says that she has never felt that her position in employment was in jeopardy and that this was due to the kindness of the second respondent.
12. Michael Leahy says that he has known the second respondent for seven years and rents numerous properties to him including the property used by the Mani Restaurant. He refers to the second respondent's commitment to the town of Clonmel and that he employs approximately 30 persons in the town and that the second respondent provides personal care to his widowed mother and is a caring family man. Mr. Leahy says that he has always found the second respondent to be decent and honourable in his dealings and he concludes by stating that he has "*no hesitation in vouching for the good character of Mr. Baig, both personally and professionally.*"
13. Anna Domagala, is an assistant working in Esquires Coffee Shop in Clonmel which is another business operated by the second respondent. She states that she has never had any issues with pay and is always paid in full and on time. She says that she feels like an appreciated member of the team and that the second respondent is a "*great employer*".
14. On any view of the matter these affidavits can only be described as "*character evidence*". None of the deponents of these three affidavits have direct knowledge of the affairs of the Company or of the matters which have been raised by the applicant in these proceedings. They are therefore of very limited, if any, relevance to this application.

Affidavit of the Applicant

15. The applicant says that on 1 November, 2018 he delivered his first and only report to the Director of Corporate Enforcement pursuant to Section 682. The report is not exhibited. The applicant states that he sought to be relieved "*at that time*" from his obligation to bring proceedings pursuant to Section 819. The Director initially granted relief, but this was later rescinded. The applicant continues by summarising points made in his report as follows: -

"The Report noted, however, that the Respondents were operating a phoenix company named Red Herring Capital Limited ('RHCL'). It was further noted that (a) RHCL was carrying on the remaining trade of the restaurant; (b) RHCL had been added by the Revenue Commissioners ('Revenue') to the Phoenix Monitoring Programme; and (c) Revenue had requested that the Respondents be restricted as company directors pursuant to s. 819 of the 2019 Act."

16. Point (a) above proved to be incorrect, in that RHCL does not carry out a restaurant trade.
17. Neither of the points referred to at (b) and (c) above constitute evidence as to the manner in which the respondents conducted the affairs of the Company. In particular, there is no evidence that Revenue requested that the respondents be restricted pursuant to s. 819. Although there has been exhibited certain correspondence between the applicant and Revenue, which I shall consider below, no request was made by Revenue in the exhibited correspondence that the directors be restricted. In an email dated 1 February, 2019 Revenue enquired of the applicant if he had filed his Section 682 report with the ODCE and whether he sought relief. Remarkably the answer given to this question by the applicant was "*We have not sought relief, we have sought restriction*". This is contradicted by the applicant's affidavit.

"Suspected Phoenix Activity"

18. The applicant refers to what he described as "*Suspected Phoenix Activity*". He says that on foot of the concerns expressed in his report to the Director his investigation of potential phoenix activities by the respondents continued.
19. The applicant states that a company called RHCL was incorporated on 27 June 2016. The respondents are both directors of RHCL and the second respondent is the company secretary of RHCL.
20. The head lease of the premises from which the Company operated, at Unit 8, Poppyfield Retail Park, Clonmel, County Tipperary was granted by Bryant Park QIAIF ICAV to RHCL on 3 October 2016 for a term of 25 years at a rent of €18,010 per annum. RHCL sublet the premises to the Company.
21. The applicant states that RHCL owned not only the head lease but also all of the equipment used by the Company in operating the restaurant together with the domain name and website for the restaurant. However, the Company "*bore the responsibility and costs associated with the fit out of the restaurant*", which had been carried out by an

independent contractor Mansfield Construction Limited ("Mansfield"). The applicant says that Mansfield performed works valued at approximately €71,000 on the restaurant and was not paid in full. The balance claimed by Mansfield at the date of liquidation is €11,778, although the respondents say that balance is disputed. The applicant says that RHCL, as the owner of the lease received the entire benefit of these works notwithstanding that the Company was contractually responsible for and paid most of those costs.

22. The applicant says that after the Company ceased to trade in April 2018 the restaurant never closed. He says that his correspondence with Revenue has indicated that the restaurant is now being operated by a company called SVJ Foods Limited. No connection has been established or is alleged to exist between SVJ Foods Limited and the Company or RHCL. RHCL granted a "Short Term Business Sub-letting" of the premises to SVJ on 1 October, 2018 for a term expiring 30 June 2023 at a rent of €18,010, an amount which corresponds precisely to the rent payable by RHCL under the head lease.
23. Although no evidence has been advanced as to any relationship between RHCL and SVJ, or for that matter the Company itself, the applicant states that the following is clear:-
- "(a) significant debt associated with the restaurant (principally to Revenue and Mansfield) are owed by the Company;
 - (b) the most valuable assets associated with the restaurant (principally the lease and the equipment) were, at all material times, owned by RHCL;
 - (c) RHCL received the benefit of the fit out performed by Mansfield and the goodwill built up by the Company in its nearly two years operating the restaurant;
 - (d) between RHCL and SVJ the restaurant continues to operate (albeit that it is not known whether SVJ does so as a sublessee of RHCL, its successor in title or through some other mechanism); and
 - (e) the creditors of the Company have no access to the business undertaking embodied in the restaurant and the value associated therewith".
24. The applicant states that in his professional opinion the arrangements between RHCL and the Company were "grossly disadvantageous to the Company (and its creditors) and conferred an essentially gratuitous benefit on RHCL; and it is impossible to infer that the arrangement was not premeditated for precisely that purpose."

Statement of Affairs

25. The directors' estimated statement of affairs as at 17 April, 2018 presented to the statutory meeting of creditors at which the applicant's appointment was confirmed was exhibited to the replying affidavit of the first respondent. Its description of assets contains a provision for "*fixtures and fittings*" having a book value of €71,643 and an estimated realisable value of nil. No other assets are identified. No assets were realised by the applicant for the benefit of the liquidation.

26. The statement then refers to the Company's liability to preferential creditors, namely Revenue in an amount of €31,251 and the following other liabilities: -

(1) Director's Loans	€43,029
(2) Bank Loans	€43,115
(3) Employee Claims	€2,460
(4) Unsecured Creditors	€26,281

27. The total amount due to creditors was a sum of €146,136.

28. In the context of the issues identified by the applicant the most important feature of the statement of affairs is the inclusion by the directors of a book value for fixtures and fittings of €71,643, having an estimated realisable value of nil. The essence of the applicant's case is that the respondents acted otherwise than honestly and responsibly in circumstances where the Company expended €71,643 on fixtures and fittings for which the applicant has been unable to obtain any value.

29. It is said by the respondents that the applicant made no efforts to secure any value for these assets. That submission carries no weight in light of their own statement of affairs estimating the realisable value of those assets at nil.

Financial Position at Winding Up

30. The applicant refers to the general subjects of the "*financial position at winding up*" and the "*reasons for insolvency*". He says that the "*proximate trigger for the company's insolvency was debt owed to Revenue*". He says that the Company had begun to fall behind on its agreed payment schedules "*(especially to Revenue) and that due to pressure from the Revenue Sheriff the Company was unable to obtain new funds in time to keep creditors...(sic)*" His conclusion as regards the financial position at winding up is as follows:-

"No dishonesty or responsibility are alleged against the respondents in relation to the insolvency itself."

Reasons for Insolvency

31. The applicant identifies the factors which combined to render the Company insolvent as including the following: -

- (a) underfunding and poor reserves;
- (b) a slow ascent to profitability and cash flow problems as the Company struggled to reach a level of business consistent with profitability;
- (c) low margins;
- (d) high levels of waste; and

- (e) an inability to accurately predict levels of demand.
32. The applicant says that the combination of the foregoing led the Company to be unable to service its creditors as and when they fell due, thereby forcing it to cease trade. His conclusion as regards the reasons for insolvency is as follows: -

"No dishonesty or irresponsibility are alleged against the respondents in relation to the manner in which these financial problems came to pass".

Dishonesty and Irresponsibility

33. The applicant's conclusion is that the arrangements between the Company and RHCL "represent classic phoenix activity" and he then says the following: -

"(b) the effect of the manner in which the restaurant was structured, with RHCL owning all of the principal assets and the Company being saddled with the responsibilities was grossly irresponsible, bearing in mind the respondent's fiduciary duties;

(c) the above arrangement, which wilfully separated the assets and the liabilities of the restaurant into separate companies, represented a fraud on the Company's creditors;

(d) it is impossible to draw any inference other than that the respondents deliberately structured the affairs of the Company and RHCL in such a way as to wilfully disadvantage the Company's creditors; and

(e) by reason of the above the respondents acted dishonestly and irresponsibly."

34. Finally, the liquidator says that he believes it would be just and equitable to restrict the respondents from acting as company directors:

"by reason of the severe disadvantage suffered by the Company's creditors as a result of the respondent's decision to manage its affairs in a manner which wilfully cheated its creditors."

35. The applicant also summarises his interaction with the Office of the Director of Corporate Enforcement and exhibits certain correspondence with that office, to which I shall return.

Affidavit of Second Respondent, sworn 28th January, 2020

36. The second respondent stated that his affidavit was delivered on his own behalf and on behalf of the first respondent and with her authority and consent. There is a later affidavit sworn by the first respondent.

37. The second respondent refers to his activity as a director of other companies which he says are successful, including Esquires Limited, which operates a coffee shop franchise in Clonmel, and Dodok Limited, which operates the "Mani Restaurant" also in Clonmel. He said that each of these companies is trading normally.

38. The second respondent says that the purpose of setting up the two companies, namely the Company and RHCL, was to devise a franchise arrangement. He says that he has experience of the franchise structure through his operation of the Esquires coffee shop in Clonmel. He says that the franchiser, Esquires Coffee, holds the head lease of the premises and his company Esquires Esquires Limited is the franchisee and sublets the premises from the franchiser. As he is already operating a successful franchise coffee business, he wished to develop a similar business model for seafood restaurants. He believed that it was a common business model to have one company set up to hold the lease on the property and a second company to sublease the company and carry on the trading business itself.
39. He says that it was as a result of his experience in the Esquires coffee franchise model and on the advice of his accountant that RHCL and the company were set up with a view to operating on such a model.
40. The second respondent refutes the allegation that there was anything "*premeditated*" about the structure as far as concerns its prejudicial effect on creditors. He says that this structure was established at a time when the Company was solvent. The Company traded for a period of eighteen months before the decision was taken to wind it up, after it became clear that it could not pay its debts. He says that when the Company was facing difficulties in 2017 the respondents worked "*tirelessly*" to attempt to overcome the financial difficulties which the company was facing and made many attempts to secure new funding and the success of the business.
41. The second respondent describes the Company's engagement with Revenue, and says that arrears only began to accumulate at the end of 2017, a few months before the company was wound up. The liquidator acknowledges that the manner in which the company incurred its liabilities was not dishonest or irresponsible.
42. The respondent says that, at the time of the winding up of the company, the balance claimed by Mansfield was disputed by the Company.
43. The respondent says that, when RHCL sublet the premises to the Company, the Company engaged Mansfield to fit out the premises so that it could operate the restaurant. He said that the cost of the Mansfield works was invoiced at a total of €63,278 and he exhibits a statement of that account. The fit out works comprised the installation of flooring, tiling, plastering, painting, lighting units, utilities, bathroom, storage, doors, etc. He says that the company paid Mansfield the sum of €51,500, leaving a balance of €13,278 unpaid. He says that when the works were carried out, the respondents were dissatisfied with the quality of the works. The defects were notified to Mansfield and an agreement was reached for the payment of the balance by way of instalments. The company paid the first instalment of €1,500. The respondent says that, despite this arrangement, Mansfield failed to commence the agreed remedial work and instigated legal proceedings to recover the balance. The effect of the payment of €1,500 was to leave a balance of €11,778, owing at the time of liquidation.

44. The respondents exhibited a report which they had engaged in the context of the litigation with Mansfield by Michael Reilly and Associates, Engineers.
45. It is not appropriate for this court to embark on an adjudication of the merits of the dispute between the Company and Mansfield. Nonetheless it is evident from the report from Messrs Reilly that a genuine dispute existed in relation to the quality of the works. This included such serious matters as leaving exposed electrical wiring, dislocation of a fly eliminator causing a local fire, to mention only two of the fourteen issues identified by Messrs Reilly.
46. In relation to the allegation of "*phoenix trading*", the second respondent makes an important correction to the information advanced by the liquidator. He says that, when the company was liquidated, the premises was rented by RHCL to a company called Marblecrest Limited from April 2018 to October 2018 and Marblecrest carried on its business from there. No evidence is adduced of a connection between the Company and Marblecrest. A number of the staff employed by the Company before liquidation were re-employed in the respondent's other businesses.
47. When Marblecrest experienced difficulties in its business and wished to pull out of its operations in October 2018, SVJ Foods Limited took over the sublease on the premises. The respondent exhibits the sublease to SVJ Foods Limited and says that SVJ Foods has continued to rent the premises and trade from that location ever since.
48. Insofar as the liquidator in his original affidavit alleged that a "*phoenix activity*" was being undertaken by RHCL, it is clear from this evidence, not contradicted by the liquidator, that RHCL never took over the trading business of the Company. The applicant appears to have had no knowledge of Marblecrest, but only of SVJ Foods which only entered the premises in October 2018.
49. In *Re Gingersnap Limited (In Voluntary Liquidation)*, *Leahy v. Doyle* [2016] IEHC 177, Keane J. considered the concept of phoenix trading and quoted with approval the report of the Working Group on Company Law Compliance and Enforcement cited by Courtney in the Law of Companies (3rd Ed.) at p. 1790 as meaning the following:-
- "...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."*
50. On the facts of this case, it is clear that RHCL did not take over the business of the company. It is, however, clear that RHCL continued after the liquidation of the company to enjoy the rental income associated with the premises which it enjoyed prior to the liquidation of the company. To that extent, there is no doubt that RHCL remained "insulated" from the immediate effects of the liquidation. If anything, its position had been improved by the enhancement of the premises by way of the expenditure on fixture

and fittings. However, it is clear that the applicant's allegation of what he referred to as "phoenix trading" was based on a fundamental misdescription of the facts.

51. In relation to the expenditure on the premises, the second respondent states that the Company incurred the costs of the fit out because it was expected that the company would trade from the relevant unit for many years into the future. He says that those assets are not owned by RHCL but by the Company. He says that the estimate in the statement of affairs of a "nil" realisable value for fixtures and fittings was based on professional advice obtained by the directors in preparation for the meeting of creditors due to the difficulty in the practicality of removing and reselling bespoke fittings.
52. The second respondent describes the costs associated with the fit out as "*essentially sunk costs*".
53. The second respondent says that RHCL:-

"...are not benefitting from these assets as they are not operating a business from the premises. SVJ Food Limited are operating from the premises and the liquidator has conceded that there is no connection between them and RHCL."

This description is selective in that it ignores the fact that RHCL are continuing to enjoy the benefit of rental income which by definition reflects the letting of the premises with the benefit of the fit out expenditure by the Company.

Affidavit of the First Names Respondent, sworn 8th November, 2021

54. The first respondent agrees with the contents of the second respondent's affidavit and makes a number of additional points.
55. She says that she was a non-executive director of the company. To her credit, she does not claim that she was unaware of the issues which have given rise to these proceedings and it is clear from her affidavit that she participated in the relevant decisions made by directors of the Company.
56. The first respondent says that prior to initiating the project the respondents sought accounting and commercial advice in relation to the structure. She refers also to the Esquires coffee structure which has been described by the second respondent. She says that on the basis of the franchiser/franchisee model and professional advice, the respondents established and registered the two separate companies, one to hold the lease on the property and the second to sublease the property and carry on the restaurant trade. She points out that the liquidator has not advanced any evidence to contradict the respondent's position regarding the validity and commercial soundness of the intended franchise structure.
57. The second respondent says that it would not have been possible to open the restaurant for trade without incurring the costs of fit out which were incurred. She refers to the fact that, at the time of the liquidation, the directors had loaned €43,029 to the Company which was entirely lost on the liquidation. She says also that the Company had a term

loan of €50,000 with Bank of Ireland, of which €43,115 was outstanding at the date of liquidation. The respondents are personally liable for that loan on foot of guarantees given to the bank.

58. The first respondent stated that the respondents expected the business to succeed and that they would over time recover the investment on the property.

Engagement between the applicant and the Director of Corporate Enforcement

59. It is clear from the applicant's affidavit that the focus of his application is entirely on what is characterised as the "phoenix activity" and the "structuring of the affairs of the Company and RHCL in such a way as to wilfully disadvantage the Company's creditors". The applicant exhibits exchanges of correspondence between his office, the Office of the Director of Corporate Enforcement and Revenue. A number of matters arise in the correspondence exhibited on which the applicant does not rely. However, it is instructive to consider the exhibited correspondence and the unusual circumstances in which the Director granted relief from the obligation to bring this application, and later rescinded it.
60. On 1 November, 2018 the applicant delivered his report to the Director pursuant to s.682.
61. In this report he sought relief from the obligation to bring a restriction application.
62. It appears from the correspondence that on 29 November, 2018 Mr. Davitt of the Director's office emailed the applicant requesting certain additional information. That email is not exhibited but the applicant's reply dated 13 January, 2019 is exhibited. In this reply he stated the following:

"Overall whilst I accept that the majority of the requirements of the Companies Act and indeed the Taxes Consolidation Act were complied with, I am of the opinion that the Directors did not act honestly and responsibly in relation to the conduct of the Company's affairs. The fact that the Directors in my opinion knowingly operated a second Phoenix company in tandem, namely Red Herring Capital Limited, which now benefits from the significant investment made by Red Herring Capital Limited (sic) at the expense of the Company's creditors was in my opinion premeditated".

63. On 13 March, 2019 Mr. Davitt replied to the applicant stating as follows:

"I refer to your letter dated 13th January 2019 in which you state that in your opinion the directors knowingly operated a second phoenix company – Red Herring Capital Limited.

It is not at all clear from your report and analysis submitted that this is unequivocally the case. As no other issues of significance arise in this case I would ask you, as a matter of urgency to provide a comprehensive analysis which sets out clearly the evidence for your contention as regards the directors' operation of a phoenix company and the grounds (including Phoenix activity) on which you would intend making an application to the courts for the directors' restriction.

I would ask that you submit this information within 28 days.

At this time, I am not inclined, regardless of the evidence that you may provide, to offer restriction undertakings to the directors and I would be of the opinion that allegations of phoenix activity in this case would be better argued and determined in court."

64. On 11 April, 2019 the applicant replied to Mr. Davitt as follows:

"In relation to the business now operating through a phoenix company. (sic) The evidence available which I have based my opinion on is as follows:

- 1. The directors freely admitted at the creditors' meeting that the premises lease was in the name of Red Herring Capital Limited and all equipment was owned by Red Herring Capital Limited and Red Herring Capital Limited was operating as the subletting landlord.*
- 2. Red Herring Seafood however arranged for the fit out of the premises. The fit out was completed by creditor Mansfield Construction who were not paid in full. It would appear that the sub landlord Red Herring Capital Limited have now benefited from this fit out cost for an amount of circa €71,000.*
- 3. The restaurant appears to have never closed after Red Herring Seafood went into liquidation. All online profiles remain active and all business operations continued as normal albeit through a different company.*

Unfortunately, I do not have jurisdiction to assess or examine the trading details of the current tenant. If the above is not sufficient in order to issue restriction undertakings, I have no objection to clearance being issued in the matter. Or if you require any further investigation on my part please advise and I will address as a matter of urgency".

65. The letter of 11 April, 2019 is remarkable for the suggestion by the applicant that if the information contained in his letter is not sufficient for the Director of Corporate Enforcement to "issue restriction undertakings" (meaning an invitation to the respondents to give such undertakings) he has no objection to "clearance" being issued. By "clearance" I understand the applicant to mean relief pursuant to s.683(3) of the Act.

66. The next letter in this sequence is a letter from Mr. Davitt dated 16 April, 2019 stating:-

"I refer to your Report received by this office on 1/11/2018 pursuant to Section 682 of the Companies Act 2014 in respect of the above company. In respect of this report I wish to inform you that you are hereby relieved of your obligation pursuant to s.683 (3) of the Companies Act, 2014 to make an application pursuant to s.819 of the Companies Act, 2014 for the restriction of the directors of the above company."

67. The letter continues by stating that a further report pursuant to s.682 is not being requested "at this time":-

"However, the Director does reserve the right to request a further report at a later interval if he deems this to be appropriate. "

68. This letter makes no reference to the applicant's letter of 11 April, 2019.

69. A common form of letter issued by the Director in response to first or other early reports by liquidators pursuant to s.682 is one in which relief is granted "at this time". This is not such a letter, although it contains the reservation of the right to request a further report.

70. There is no evidence that the Director ever sought a further report.

71. On 28 August, 2019 Mr. Davitt wrote to the applicant referring again to the report delivered on 1 November, 2018 and referring to his letter of 16 April, 2019 granting the applicant relief from the obligation to bring a restriction application (he makes no reference to the applicant's letter of 11 April 2019). He continued:

"On the basis of information obtained from the Revenue Commissioners in the intervening period I wish to inform you that I have rescinded my earlier decision. Therefore, you are not relieved of your obligation pursuant to s.683 (3) of the Companies Act, 2014 to make an application pursuant to s. 819 of the Companies Act, 2014 for the restriction of the directors of the above company".

72. In his grounding affidavit the applicant states that it is on foot of this letter of 28 August, 2019 that this application has been made. With reference to Mr. Davitt's reference to information obtained from the Revenue Commissioners "in the intervening period" the applicant states that the Director subsequently forwarded to him "the Revenue correspondence on foot of which the Director reversed his previous decision". He exhibits that correspondence. The exhibited correspondence comprises the following.

Correspondence with Revenue

73. On 1 February, 2019 Ms Elizabeth Griffin of the Insolvency Unit of the Office of the Collector General emailed the applicant a series of questions. In her opening paragraph she says:-

"The Revenue Commissioners are a large creditor in this liquidation per the statement of affairs and I am concerned that the assets valued in the statement of affairs at €71,643, being "Fixtures and Fittings" estimated to realise nil are being used by another entity still trading as "Red Herring" from the same commercial premises at Poppyfield Retail Park."

74. The applicant replied to this email on 20 March, 2019. On this first part he replied as follows:-

"I would agree completely with your analysis. I believe the assets are being used by Red Herring Capital Limited (however they may have changed tenant since) and I have referred this matter to the ODCE for direction".

75. Ms. Griffin asked a number of further questions about the applicant's actions to recover payment for the fixtures and fittings, realisations in the liquidation, the directors' loan account, invoices, rates and employees to each of which the applicant replied. The final two questions and answers are relevant.

Q: Have you discovered any fraudulent preference?

A: Nothing that can be classified as fraudulent preference in the normal definition of the word (select payments of creditors, repayment of personal guarantees, etc). However, the "unusual" relationship between Red Herring Seafood and Red Herring Capital has been notified to the ODCE. This in my opinion may not be classified as fraudulent preference however it is clearly an act to put the assets deliberately beyond the reach of the creditors.

Q: Have you filed your s.682 report with the ODCE and have you sought relief?

A: Yes, this has been filed. We have not sought relief, we have sought restriction, notified them of all matters above and asked them for direction on how to proceed in any potential case against the directors or the related companies.

76. No explanation was proffered by the applicant as to why he informed Revenue that he had not sought relief, when his affidavit, exhibiting this correspondence, states that he sought relief.
77. The applicant's reply of 20 March, 2019 was sent to Ms. Griffin and to Mr. Mansfield of Mansfield Construction.

Mansfield Construction

78. In exhibiting his correspondence with Revenue, the applicant, without any comment, includes an email dated 23 February, 2019 from Mr. Mansfield of Mansfield Construction to Ms. Griffin.
79. In Mr. Mansfield's email he says that he was owed a balance of €11,780 by the Company and took legal action against it. He said that the week before the due date for the court hearing "they filed for a liquidation".
80. Mr. Mansfield refers to the creditors meeting at which certain allegations and questions were raised regarding a "phoenix-type operation" and the expression of opinion by Elaine Byrne of Revenue at the creditors meeting to the effect that there was "a clear trend here".
81. Mr. Mansfield complained that nothing has been done and that his contacts with the applicant have not been responded to. He says that the "Red Herring is still open and trading very well. Mr. Baig can be seen entering the premises regularly and is in my

opinion still owner". He makes further allegations regarding the activities of the second respondent in his operations of Esquires Coffee Shop and the Mani Restaurant and then makes the following allegations:

1. I was not the only business to get burned by him so he does not have a good reputation around here.
 2. I also know that he used to have a restaurant in Cork but closed down previously.
 3. I received a phone call from one of my subcontractors who was told that Mr. Baig is going to close Mani restaurant in the next few weeks.
 4. In the eighteen months prior to the Red Herring liquidation no VAT PRSI or income tax was paid to Revenue, approximately €35,000 in total nor were any company reports filed.
82. Mr. Mansfield concludes by stating that he has contacted his local T.D. and the Office of the Director of Corporate Enforcement about the matter.
83. Each of these communications predates the decision of the Director communicated on 16 April, 2019 to grant relief pursuant to s.683.
84. The applicant also exhibits, again without any comment or context, an email by Mr. Mansfield written on 21 June, 2019 to Revenue, the applicant, the Director, and to mattie.mcgrath@oireachtas.ie. In this email Mr. Mansfield restates a number of the allegations referred to above including the allegation that "not one cent was paid to Revenue".
85. These exhibits are emails of complaint by Mr. Mansfield, an aggrieved creditor, or disputed creditor, making a series of allegations against the first named respondent. Firstly, these emails of Mr. Mansfield are not probative of his allegations.
86. Secondly, nowhere is it suggested that the applicant himself undertook any investigation of the allegations made by Mr. Mansfield.
87. Thirdly, the applicant does not make any observation as to the merits or otherwise of the allegations, other than to state his view that there has been a "phoenix activity" and a "fraud on the company's creditors". In the course of the hearing counsel for the applicant indicated that he was not pursuing the allegation of fraud, although the entire basis for the suggestion that the respondents had acted otherwise than honestly and responsibly appears to be based on the suggestion that the structure of the two companies was premeditated to the disadvantage of the company's creditors.
88. Fourthly, although none of Mr. Mansfield's allegations are before the court as evidence, in her replying affidavit the first named respondent addresses all of the contents of Mr. Mansfield's emails. As the applicant does not seek to stand over the contents of those emails or, surprisingly, to have conducted an investigation in relation to their contents it

is unnecessary to analyse them item by item. However, the most serious allegations have been addressed on affidavit by the first respondent as follows:-

1. The allegation that the company paid no VAT, PRSI or other tax to Revenue in its eighteen months of trading is refuted by reference to the summary of liabilities from Revenue exhibited by the applicant which show that payments to Revenue were made from time to time. The applicant acknowledged that the company was substantially compliant with its obligations under the Taxes Consolidation Act.
 2. The first respondent states that the necessary reports and returns were made to the Companies Registration Office and that these are publicly available as a matter of record.
 3. The second respondent swears in relation to the restaurant in Cork that he was a chef in that restaurant. It did close down but he had no part or ownership in the management of the company and was only an employee.
89. The respondents deny in their affidavits that there was any intention to liquidate the company which operates the Mani Restaurant.
90. The respondents also point out that none of the allegations made by Mr. Mansfield or the questions raised by Revenue were ever put by the applicant to them, whether by way of a liquidator's questionnaire or otherwise.
91. Mr. Mansfield's email of 21 June, 2019 is largely a repetition of allegations and complaints made by him on 23 February, 2019 which were before Revenue at that time. The email of 21 June, 2019 is the only communication exhibited which post-dates the Director's initial decision to grant relief, although the court is not told as to when precisely the earlier communications were placed before the Director.
92. At one level, this court should not be distracted by these email exchanges. They represent a dialogue between the applicant and Revenue, and a series of unverified complaints by an aggrieved creditor. Yet the applicant exhibits them as the correspondence given by Revenue to the Director on the basis of which apparently the Director rescinded his decision to grant relief.
93. As a general rule, there is nothing improper about the Director rescinding a decision to grant relief pursuant to s.683 (3). In his initial letter granting relief he reserved his position in this regard. However, the following features are not explained:
1. There is no evidence of the liquidator having conducted his own investigation of the allegations made by Mr. Mansfield.
 2. Clearly the emails of Mr. Mansfield are not of themselves probative of their contents.

3. There is no evidence of the applicant putting to the respondents any of these allegations either in the context of his first and only report to the Director, or thereafter when he was in receipt of correspondence from Revenue and Mr. Mansfield.
94. There is no statutory obligation on the liquidator to engage in further correspondence with the respondents on these issues, but in circumstances where the decision of the Director to rescind relief was stated in the letter of 28 August, 2019 to be on the basis of "information received from the Revenue Commissioners in the intervening period" and where the only communication in the relevant "intervening period" was one email from Mr. Mansfield repeating complaints and allegations which had been made by him on 23 February, 2019, the effect was to deprive the respondents of an opportunity to address these matters, if in fact they were of concern to the applicant or the Director. Nor did the Director request a second Report.
95. On receipt of the letter of 28 August, 2019 the applicant came under a statutory obligation to bring these proceedings. However, when he says in his grounding affidavit that the ODCE subsequently forwarded to him "*the Revenue correspondence on foot of which the Director reversed his previous decision*" he does not say whether he made any further enquiries of his own or engaged with the Director, with Revenue or the respondents. He simply states that "*it is on foot of this letter that the herein application has been made*".

Submissions

96. The applicant acknowledged that the facts in this case were not a "classic phoenix" in the sense described by Keane J. in *Ginger Snap Limited*. He instead submitted that this was "akin" to a phoenix structure. Whilst RHCL is not itself carrying on the trade previously carried on by the Company, it now stands in the position of holding the 25-year lease of the property, with the benefit of a subletting by which it receives rent corresponding exactly to the amount payable to the head landlord.
97. The applicant submits that the potential prejudice to the creditors of the Company by its expenditure of €71,000 on fixtures and fittings which did not enure for the benefit of the creditors of the company was a prejudice which was either known or ought to have been known to the respondents when they established the corporate structure of the Company and RHCL.
98. In the hearing, counsel for the liquidator stated that, contrary to the contents of the grounding affidavit, he was not pursuing the allegation that there had been deliberate or wilful defrauding of creditors. The applicant relies entirely on the proposition that the respondents ought to have known of the possibility that the Company could fail and that by the corporate structure utilised the creditors would be left with no recourse to assets. He submitted that this amounts to a gratuitous benefit conferred on RHCL to the extent of the €71,000 expended on the fixtures and fittings at the expense of the Company's creditors.

99. Key undisputed facts in this matter are as follows: -
- (1) The liquidator was unable to realise any value for assets of the company, including fixtures and fittings on which the company had expended €71,000.
 - (2) RHCL is the holder of a 25-year lease of the premises, now with the benefit of a lease to SVJ at a rent corresponding exactly to the amount of rent payable under the head lease.
 - (3) RHCL, a company of which the respondents were both directors, was placed in a position where on the liquidation of the Company it was in a position to re-let the premises immediately to Marblecrest and later to SVJ Foods. It appears that this continuity of occupation and trade, yielding the rent of €18,010, continued uninterrupted following the liquidation of the company.
100. There is no evidence before the court as to whether the head lease is itself an asset of value.
101. The respondents say that insofar as the company expended €71,000 on fixtures and fittings, this expenditure did in fact enure for the benefit of the company whilst it was trading. They say that they, the respondents, were the "biggest losers". This is borne out when account is taken of the fact that the directors' loan in the Company stood at €43,029 and the respondents have personal exposure for the company's bank loan at the sum of €43,115, resulting in direct losses to the respondents of a total sum of €86,144. They say that the applicant is applying the benefit of hindsight in his analysis and that they fully expected the business to succeed and to recover the benefit of the investment. They say that the outlay was a standard business setup cost which would have been recovered over time.
102. The second respondent has exhibited the statement of account with Mansfield Construction Limited. It is noteworthy that of the total account of €63,278, €45,000 had been invoiced and paid before the end of December 2016. A further €5,000 had been invoiced and paid in February 2017, and the final invoice of €13,278 was issued on 15 March 2017. The effect of this is that the Company had expended the overwhelming majority of the amounts paid on fit out in the period ending December 2016 and therefore enjoyed the benefit of the refit in its trade for the following 16 months.
103. No information is before the court as to the level of the Company's revenues or outgoings over the entire period of its trading. However, it is clear from the Mansfield statement that the company had spent this money and had the benefit of the relevant works for more than a full year's trading before liquidation, being 16 of the total of 19 months trading. It was not until early 2018 that the respondents determined that the Company should be wound up, and there is no suggestion by the applicant that the Company was insolvent earlier or that the decision to wind up the Company ought to have been made earlier.

Conclusion

104. Because of the manner in which s. 819 is constructed, the onus of proof rests on the respondent directors to establish that they acted honestly and responsibly in relation to the affairs of the company, that they have cooperated with the liquidator and that there is no other reason why they should be subject to a restriction order.
105. If it were not for this reversal by statute of the traditional burden of proof which would otherwise fall on a liquidator I would have no hesitation in finding that the complaints made by the applicant in this case are not made out having regard to the general manner in which they are described, to the very limited evidence proffered by the applicant, some of which transpired to be inaccurate, and to the state of the correspondence which appears to have informed his reporting to the Director and the decision made by the Director. However, in view of the fact that the section requires the respondents to establish that they have acted honestly and responsibly this Court is faced with an examination of their account of events, and in particular their response to the central allegation of irresponsibility based on the manner in which the respondents structured the corporate entities and the fit out expenditure.
106. Although the applicant in his grounding affidavit uses phrases such as "grossly irresponsible", "fraud", "wilful separation of assets and liabilities", it is clear from the submissions by counsel for the applicant that he was not persisting with the allegation of fraud. Instead, the court is invited to infer from the corporate structure adopted by the respondents that the fit out expenditure was all a scheme for the benefit of RHCL and to the detriment of the Company's creditors, such as to display an absence of responsibility such as would require the court to make a declaration of restriction.
107. In his seminal judgment in *La Moselle Clothing Limited (In liquidation)* [1998] 2 ILRM 345, Shanley J. considered the factors to which the court should have regard in determining the "responsibility" of a director for the purposes of s. 150 of the Act of 1990 (being the predecessor of s. 819). He identified the factors as follows: -
- "(a) The extent to which the director has or has not complied with any obligation imposed on him by the Companies Acts 1963 - 1990.*
- (b) The extent to which his conduct could be regarded as so incompetent as to amount to irresponsibility.*
- (c) The extent of the director's responsibility for the insolvency of the company.*
- (d) The extent of the director's responsibility for the net deficiency in the assets of the company disclosed at the date of the winding up or thereafter.*
- (e) The extent to which the director, in his conduct of the affairs of the company, has displayed a lack of commercial probity or want of proper standards".*
108. No allegation has been made of non-compliance with the Companies Act or any other legislation. As regards responsibility for the insolvency and for the extent of the deficit,

the applicant says in his grounding affidavit that no dishonesty or irresponsibility is alleged against the respondents "in relation to the insolvency itself". He states in relation to the liabilities of the company that "no dishonesty or irresponsibility are alleged against the respondents in relation to the manner in which these financial problems came to pass".

109. I am therefore left with a consideration as to whether the structure adapted by the respondents combined with the manner of the expenditure on fixtures and fittings amounted to acts which were "so incompetent as to amount to irresponsibility" or "displayed a lack of commercial probity or want of proper standards".
110. The sworn evidence of the respondents is that the corporate structure was based on a typical franchise model and that the fit out expenditure was properly incurred by the trading Company itself. As against this, the applicant asserts that the structure was designed to confer "gratuitous benefit" on RHCL, being another company controlled by the respondents.
111. There is a certain weakness to the "franchise" explanation. The important difference between the structure adopted in this case and the franchise structure adopted in the case of Esquires Coffee is that in the latter instance the franchiser is not a company owned or controlled by the same parties, but is an external party which grants franchises internationally. Nor have the respondents provided any detail of the nature of the advice which they were given, other than the bare assertion that they "sought accounting and commercial advice". Nonetheless, their evidence is that the structure was established in good faith. More importantly, their evidence, which is not contradicted, is that the trading company incurred expenditure on fit out which it then availed of for the duration of its trading existence. Although one creditor, namely Mansfield which is owed €11,778, has protested more than others, the true position is that other creditors have suffered greater losses, namely the respondents themselves and Bank of Ireland, albeit that the bank holds personal guarantees for the respondents.
112. I have been referred also the cautionary words of McGuinness J. in *Re Squash Ireland Limited* [2001] IR 35 and of Peart J. in *Re Usit World plc.* [2005] IEHC 285 concerning the dangers of applying hindsight.
113. As McGuinness J. put it: -

"In the case of all companies which have become insolvent it is likely that some criticisms of the directors may be made. 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".

114. The applicant acknowledged that the respondents did not act dishonestly or irresponsibly in relation to the incurrence of debts or the manner in which the insolvency arose. He has not advanced evidence of intent on the part of the respondents to defraud creditors or to wilfully deprive creditors of recourse to assets, beyond his statement in his grounding

affidavit to the effect that "it is impossible to infer that the arrangement was not premeditated".

115. Because the burden rests on directors in s.819 applications, directors of insolvent companies should not, as a general rule, escape sanction merely because of deficiencies in the liquidator's presentation of their application, or paucity of evidence proffered by the liquidator. Nor should they escape sanction merely because of inconsistencies in the contents of communications between the liquidator and the Director of Corporate Enforcement, Revenue and others. Nonetheless, the shifting of the burden of proof by s.819 does not mean that respondents should be deprived of fair procedures, or that the court should accept incomplete and hearsay evidence such as the applicant has advanced.
116. The Director was entitled to rescind his decision to grant relief under s683(3) and there is no statutory obligation on the Director or on the applicant to give reasons for such a decision. However, the applicant states that this application was brought "on foot of" a letter from the Director which in turn refers to correspondence from Revenue. When that exhibited correspondence, taken together with other contradictory correspondence between the applicant and the Director is examined, it bears no scrutiny and reveals a failure by the applicant to investigate the matters alleged.
117. Taking all these factors into account I have concluded that the respondents acted honestly and responsibly in relation to the affairs of the company and there is no other reason why they should be subject to a restriction order.
118. Nowhere has it been suggested that there has been any failure on the part of the respondents to cooperate with the liquidator. On the contrary, the application is entirely silent on what communications took place between the applicant and the respondents throughout the process.
119. I therefore refuse the declaration sought in the notice of motion.