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Ireland briefing from ByrneWallace published in the May 2010 issue of The In-House Lawyer:

Recent developments in examinership law

THE IN-HOUSE LAWYER

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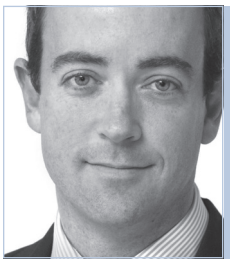

BY JOHN FITZGERALD
associate,
ByrneWallace
(formerly BCM
Hanby Wallace)

THERE HAVE BEEN SEVERAL SIGNIFICANT developments concerning examinerships in the Irish jurisdiction recently. In *Re Vantive Holdings & ors* [2009], the criteria laid down in Vantive Holdings' applications for the appointment of an examiner have raised the evidential bar significantly. Applicants now have to ensure that they are armed with a very credible Independent Accountant's Report, based on reliable projections and assumptions, before the High Court will consider exercising its discretion to appoint an examiner. In *Missford Ltd t/a Residence Members Club* [2010], Kelly J made it clear that the use of money deducted by way of VAT and PAYE or Pay Related Social Insurance (PRSI) as working capital was a major factor in influencing the court not to exercise its discretion in favour of appointing an examiner.

More recently, judgments of the Supreme Court and the High Court in *Linen Supply of Ireland Ltd v Companies Acts* [2010] have clarified how certain provisions of the Companies (Amendment) Act 1990 (the 1990 Act) are to be interpreted in so far as leases are concerned.

REPUDIATION OF LEASES

The law in relation to the repudiation or disclaimer of contracts (including leases), in the context of examinership, is governed by s20 and s9 (s9 brings in s290 of the Companies Act 1963) of the 1990 Act.

Section 20 provides:

> **'i)** where proposals for a compromise or scheme of arrangement are to be formulated in relation to a company, the company may, subject to the approval of the court, affirm or repudiate any contract under which some element of performance (other than payment) remains to be rendered both by the company and the other contracting party or parties;
>
> **ii)** any person who suffers loss or damage as a result of such repudiation shall stand as an unsecured creditor for the amount of such loss or damage;
>
> **iii)** to facilitate the formulation, consideration or confirmation of a scheme of arrangement, the court may hold a hearing and make an order determining the amount of any such loss or damage, and the amount so determined shall be due by the company to the creditor as a judgment debt; [and]
>
> ...
>
> **v)** where the court approves the affirmation or repudiation of a contract under the section, it may, in giving such approval, make such orders as it thinks fit for the purposes of giving full effect to its approval, including orders as to notice to, or declaring the rights of, any party affected by such affirmation or repudiation.'

Section 9 affords a less direct means to disclaim a lease, allowing an examiner to apply to court for an order that the examiner shall have all or any of the powers that they would have if they were a liquidator appointed by the court. This opens up the possibility of a section 290 disclaimer application. However, in *Fate Park Ltd & ors v Companies Acts* [2009], the court held that an examiner will only be given the powers of an official liquidator if an order has made pursuant to s9(1), vesting in the examiner some or all of the functions or powers vested in, or exercisable by, the directors. Therefore, it is not a stand-alone order.

In *Linen Supply*, the Supreme Court had to rule on an appeal by the company against the decision of the High Court that it was not possible to repudiate a lease under s20. The High Court was of the view that s25(b) of the 1990 Act was inconsistent with the proposition that a company could repudiate a lease under s20 of the 1990 Act. Section 25(b) essentially states that an examiner's proposals shall not allow for a reduction in rent that falls to be paid after the compromise or scheme of arrangement would take effect.

The majority of the Supreme Court (Hardiman J dissenting) held that the company could repudiate a lease pursuant to s20 of the 1990 Act. In doing so, the court accepted that:

'Judgments of the Supreme Court and the High Court have clarified how certain provisions of the Companies (Amendment) Act 1990 are to be interpreted.'

'Section 9 affords a less direct means to disclaim a lease, by allowing an examiner to apply to court for an order that the examiner shall have all or any of the powers that they would have if they were a liquidator.'

i) leases fall within the definition of 'contract' as contained within s20;

ii) s25(b) of the 1990 Act applies to situations where a scheme of arrangement has already been formulated and did not prohibit the repudiation of a lease pursuant to s20, prior to the formulation of such a scheme; and

iii) positive and negative covenants contained in commercial leases relating to user, repair or quiet enjoyment, are sufficient to constitute the non-monetary element of performance that is required to be outstanding on behalf of both parties to invoke the jurisdiction of s20. (This is where Hardiman J dissented, saying that he accepted that a lease is a 'contract' for the purposes of the section, but that covenants of quiet enjoyment or insurance are not obligations requiring to be performed by both landlord and tenant.)

IMPAIRMENT OF SUMS PAYABLE TO LANDLORDS IN RESPECT OF LOSS OF RENT AND/OR DELAPIDATIONS POST-REPUDIATION

Following on from the Supreme Court decision in *Linen Supply*, the High Court permitted the company to repudiate several leases entered into by the company and the examiner-formulated proposals that were opposed by numerous landlord creditors. Their main objection was that the damages due to them should not be subject to impairment under the 1990 Act and that the court had no jurisdiction to confirm the scheme that makes provision for impairment of the sums due by way of future rent.

The parties had agreed the sums due in respect of loss or rent and/or dilapidations that arose in the event of the court making an order pursuant to s20, permitting a repudiation. There were five leases involved and the damages figures ranged from €500,000 to €1.1m approximately. (These figures do not include loss of rent during the course of the examinership, as the court directed it should be paid in full.)

The landlords complained that under the scheme, they would only receive 30% of the figure agreed as the damages that follow the repudiation of the leases. They argued that a scheme is only intended to apply to debts due at the date of presentation of the petition (none, in the case of these landlords). They contended that post-petition liabilities (including a judgment debt against the company following its repudiation of a lease) can only be written down if there is express statutory authority to this affect (there is none).

McGovern J held that the landlords were prospective creditors at the date of commencement of the examinership. While they also argued that their claim was not a claim for unpaid rent, but for damages arising on the repudiation of their leases, in McGovern J's view this did not alter their status as prospective creditors. He held that the intent of the legislation was clear to the effect that a court could appoint an examiner who may present a scheme that impairs the rights of a creditor, including a prospective creditor.

CONCLUSION

Leases may now be disclaimed on application and the resulting damages can be impaired under a scheme of arrangement.

These decisions make life easier for the examiner and the company once court protection is granted. Whether the decision is fair to landlords is another matter entirely, particularly where they have repayment obligations to their own funders based on a certain income stream.

By John Fitzgerald, associate, ByrneWallace (formerly BCM Hanby Wallace). E-mail: jfitzgerald@byrnewallace.com.

Fate Park Ltd & ors v Companies Acts [2009] IEHC 375

Linen Supply of Ireland Ltd v Companies Acts (2010, unreported)

Missford Ltd t/a Residence Members Club v Companies Acts [2010] IEHC 11

Re Vantive Holdings & ors [2009] IESC 69