

**In-House Editor**  
Kristiina Kojamo

**Consultant Editors**

Deborah H. Wheeler,  
BL, TEP

Ruth Cannon, BL

James Dwyer, SC

Cedric Christie,  
Solicitor, TEP

Albert Keating, BCL,  
LLB, LL.M.,  
DLitt, BL

**Subscription  
information**

Four issues annually  
€325 +VAT(13.5%)

**Citation**

This journal may be  
cited as  
(2010) 15(4) C.P.L.J.

Round Hall  
43 Fitzwilliam Place  
Dublin 2, Ireland

T: +353 1 662 5301  
F: +353 1 662 5302  
E: info@roundhall.ie  
www.roundhall.ie

# CONVEYANCING AND PROPERTY LAW

## J O U R N A L C O N T E N T S

- |   |           |   |           |
|---|-----------|---|-----------|
| <b>Repudiation and Disclaimer of<br/>Leases in Examinership and<br/>Liquidation</b>                       | <b>78</b> | <b>Book Review: Peter Bland, 91<br/><i>Easements</i>, 2nd edn</b> |           |
| <i>Louise Wright</i>  |           | <i>Neil Maddox</i>  |           |
| <b>Landlord v Tenant: Security of<br/>Tenure as we now know it—the<br/>Residential Tenancies Act 2004</b> | <b>83</b> | <b>Cases and Comment</b>  | <b>92</b> |
| <i>Úna Cassidy and Jennifer Ring</i>  |           | <i>Helen McCarthy</i>   |           |
| <b>Adverse Possession: Will<br/>Letters Stop Time Running?</b>  | <b>88</b> |   |           |
| <i>Laura Farrell</i>  |           |   |           |

© Thomson Reuters (Professional) Ireland Limited, 2010

The views expressed in this publication, save where otherwise expressed, are the views of the individual contributors and are not necessarily the views of the Publisher or the Editors.

Contributions published in this journal are not intended to, and do not represent, legal advice on the subject matter contained herein. This publication should not be used as a substitute for professional advice.

ISSN: 1393-3213

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means, including photocopying and recording, without the written permission of the publishers. Such written permission must also be obtained before any part of this publication is stored in a retrieval system.

If one of your issues of the *Conveyancing and Property Law Journal* is lost in the post, please notify us immediately. We will be able to replace missing issues up to six months after publication only.

# Repudiation and Disclaimer of Leases in Examinership and Liquidation

## Introduction

The recent unprecedented economic downturn has resulted in many companies suffering substantial loss of business revenue due to a lack of demand for their products and services. Although companies have been faced with a reduction in their revenues, there has been no corresponding reduction in their overheads including the payment of rent which for many companies is a significant cost. A substantial amount of companies operate their businesses from properties which are held under lease. Most of these leases were negotiated prior to the downturn when rents were inflated. They contain upwards only rent review clauses with a limited option to break, usually subject to the payment of a penalty. It has become apparent that onerous covenants in leases coupled with high rents are playing a substantial role in the financial hardship of companies leading in many cases to insolvency. The recession has resulted in a dramatic surge in the number of companies seeking to appoint an examiner where they are considered to have a reasonable prospect of survival. The large volume of examinerships and liquidations has required both examiners and liquidators to address and resolve one of the key causes of insolvency, namely onerous leases with over-inflated rents. This article proposes to outline the legislation governing the repudiation and disclaimer of leases in an examinership and in a liquidation and the interpretation and clarification of such legislation as a result of various cases.

## Examinership

Examinership is generally construed as a positive option for a company suffering financial hardship which has a reasonable prospect of survival if restructured. It allows the company the opportunity to find an investor, which is considered crucial for the likely success of an examinership. Provided that the scheme of arrangement is approved it prevents the company from going into liquidation and allows it to continue its business operation and to preserve employment. Clarke J. stated in the case of *Re Traffic*

*Group Limited*<sup>1</sup> that, "it is clear that the principle focus of the legislation is to enable, in an appropriate case, an enterprise to continue in existence for the benefit of the economy as a whole and, of equal, or indeed, greater importance, to enable as many as possible of the jobs which may be at stake in such enterprise to be maintained for the benefit of the community in which the relevant employment was located."

Examinership is governed by the Companies (Amendment) Act 1990 (the "1990 Act") as amended by the Companies (Amendment) (No.2) Act 1999 (the "1999 Act"). There are two pre-requisites to the appointment of an examiner: (i) that the company is insolvent; and (ii) that there "is a reasonable prospect of survival of the company and the whole or any part of its undertaking as a going concern". In accordance with s.3 of the 1990 Act the company's application for examinership may be made by the company, directors of the company, the creditors including contingent or prospective creditors (including an employee) of the company, or members of the company holding at the date of presentation of the petition at least 10 per cent of the issued share capital. In most cases the application is made by the company. Under the 1999 Act the petition must be accompanied by an independent accountant's report, which must among other matters contain his opinion as to whether the company has a reasonable prospect of survival as a going concern and whether the formulation, acceptance and confirmation of the scheme of arrangement offers a reasonable prospect of survival for the company. The examiner is appointed for 70 days which period may be extended by a further 30 days upon application to the court. During this time the examiner prepares a survival plan known as "the scheme of arrangement" to facilitate the company's continued operation.

During an examinership the company is protected by the court and creditors are prohibited from taking action against the company. Secured creditors will not be permitted to enforce charges over part or all of the company's property unless the examiner consents. A receiver may not be appointed. If a receiver is already in place, the court may restrict his work. No proceedings for the winding-up of the company may be commenced or resolution for winding-up passed in relation to the company and any resolution so passed will have no effect. No attachment, sequestration, distress or execution can take place against the property or effects of the company except with the consent of the examiner. An examiner may ignore negative pledge clauses and

Louise Wright,  
Solicitor, Dillon Eustace

debentures so as to borrow the necessary funds for the period of the protection provided that this has been approved by the court. If the scheme of arrangement is approved by the court it then makes whatever orders are required to give it effect and to bring the examinership and the High Court protection to an end. The company will then emerge from examinership and proceed to trade normally. In recent case law on examinership the issue of the ability of a company/examiner to repudiate/disclaim leases has become a central issue in a number of recent cases brought before the High Court and the Supreme Court as the repudiation/disclaimer of leases is necessary for many companies to have a reasonable prospect of survival and features as a central part of many schemes of arrangement.

#### **Right of Company to Repudiate a Lease**

Repudiation of leases in an examinership is governed by s.20 of the 1990 Act which provides as follows:

- 20(1) – 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.
- 20(2) – 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.
- 20(3) – in order to facilitate the formulation, consideration or confirmation of a compromise or 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 judgement debt.
- 20(4) – Where the examiner is not a party to an application to the court for the purposes of *subsection (1)*, the company shall serve notice of such application on the examiner and the examiner may appear and be heard on the hearing of any such application.
- 20(5) – Where the court approves the affirmation or repudiation of a contract under this 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.

#### ***O'Briens Irish Sandwich Bars Limited ("OBISBL") v Companies Acts<sup>2</sup>***

One of the first High Court cases taken under s.20 of the 1990 Act was the *OBISBL* case. *OBISBL* was a successful sandwich franchise business whereby franchisees operated under its name. One of the main elements of the business model was that *OBISBL* obtained leases of suitable properties and then sub-let them to franchisees. Most of the sub-leases granted were subject to the same conditions as those granted in the head-leases to include the passing rent in the head-leases. The majority of the head-leases were granted during the economic boom when rents were over-inflated with upwards only rent review provisions. Due to the recession and the consequent impact on consumer spending the revenues of the sandwich franchise were seriously impacted leaving the franchisees unable to meet the rents payable and in some cases having to vacate the properties due to insolvency. As *OBISBL* was the tenant under the head-leases it remained bound by all the covenants and conditions in the head-leases to include the discharge of the rents payable. This was a key factor contributing to the financial hardship and insolvency suffered by the *OBISBL* resulting in the petition for an examiner. During the course of the examinership negotiations took place with various investors. *OBISBL* entered into an agreement with *Abrahebabra Investments Limited ("AIL")* which proposed to invest a substantial amount of money into *OBISBL* subject to *OBISBL* no longer being a party to any leases which proposal could be effected either by surrender or repudiation such that the business would become a franchise operation with no leasing obligations. *OBISBL* brought 60 motions for repudiation. During the course of the hearings agreement was reached in a number of cases resulting in the unresolved cases remaining at 40 motions. In light of the proposed investment by *AIL* being conditional on *OBISBL* holding no leasehold interest *OBISBL* made an application to have the remaining 40 leases repudiated. It was held that the application to repudiate the leases did not come within the terms of s.20(1) of the 1990 Act, as the main purpose of the section was to apply to a situation that did not involve the payment of monies. It was also held that the section could not be construed as allowing the

repudiation of a volume of 40 leases and the application was refused.

*Linen Supply of Ireland Limited ("LSOIL") v Companies Acts*<sup>3</sup>

LSOIL was a leading supplier of linen to various entities in Ireland which included the health sector, restaurants and hotels. LSOIL operated its business from various leasehold properties held by it which were subject to the payment of over-inflated rents. Due to the downturn in the economy there was a severe decrease in the demand for its services. This resulted in a decrease in the company's turnover which was further exacerbated as there was no corresponding decrease in its outgoings including the excessive rents and outlays payable. LSOIL petitioned for an examiner to be appointed during which time it required the financial support of its parent company, CWS-Boco International GmbH. There were two applications made to the court: (i) an application by LSOIL seeking an order for the repudiation of the leases held by LSOIL pursuant to s.20(1) of the 1990 Act and an order pursuant to s.20(3) of the 1990 Act determining the amount of loss suffered by the landlords; and (ii) an application by the examiner seeking an order pursuant to s.9(1) of the 1990 Act transferring the functions and powers of the directors of the company to the examiner, an order pursuant to s.9(4) of the 1990 Act such that the examiner could have the powers conferred upon a liquidator by s.290 of the Companies Act 1963 (the "1963 Act") and an order granting the examiner leave to disclaim the leases. The High Court held that it had no jurisdiction to make an order repudiating the leases sought by LSOIL. The application to disclaim the leases was refused also.

The matter was referred to the Supreme Court and it was held on appeal that there was a statutory basis under s.20 of the 1990 Act to repudiate a lease and the matter was remitted back to the High Court to exercise its discretion under s.24 of the 1990 Act. The section 24 application was made in the case of *Linen Supply of Ireland Limited v Companies Acts*.<sup>4</sup> First, the landlords objected on the basis that the debts due to them were not subject to impairment under the 1990 Act and that the court had no jurisdiction to approve a scheme of arrangement which made provision for the monies due and owing to them by way of future rent. Secondly, they claimed that the proposals were unfair and inequitable and that they were unfairly prejudiced. It was held in this case that the leases could be repudiated in accordance with the 1990 Act and that the court could

appoint an examiner who may present a scheme of arrangement which impairs the rights of a creditor including a prospective creditor. Accordingly, it was held that the agreed debts due to the landlord creditors were subject to impairment under the 1990 Act and that the court had the jurisdiction to confirm a scheme which made provision for such an impairment. It was held that the landlords were not treated any differently to the other creditors and that there was no evidence to indicate that the proposals were unfair or inequitable. The scheme of arrangement was approved allowing LSOIL to emerge from examinership and to continue trading.

**Right of Examiner to Disclaim a Lease**

Disclaimer of leases in an examinership is governed by s.9 of the 1990 Act, s.9(4) states as follows:

Without prejudice to the generality of subsections (1) and (3), an order under this section may provide that the examiner shall have all or any of the powers that he would have if he were a liquidator appointed by the court in respect of the company and, where such order so provides, the court shall have all the powers that it would have if it had made a winding up order and appointed a liquidator in respect of the company concerned.

This permits the examiner to make an application to the court to have all or any of the powers that they would have if they were a liquidator appointed by the court in respect of the company.

*Bestseller Retail Ireland Limited ("BRIL") v Companies Act*<sup>5</sup>

BRIL has been trading in Ireland since 1991 and is a wholly owned subsidiary of Bestseller A/S ("AS") which is incorporated in Denmark. In Ireland it operates under four brands, namely Name It, Vero Moda, Jack and Jones, and Only. It became insolvent and an examiner's appointment was confirmed. The main contributing factors to BRIL becoming insolvent were over-inflated rents payable, the upward only rent review provisions and the absence of a break clause. AS agreed to invest in BRIL provided that all the unprofitable leases were terminated. An application was made by BRIL pursuant to s.20(1) and (3) of the 1990 Act to have a number of leases repudiated in respect of under-performing stores. On the application to appoint the examiner, an independent accountant's report was furnished which recommended that 14 stores be shut down along with such other stores that may be identified as causing a deficit on the financial

position of BRIL. Subsequently the examiner included a further 3 stores as being a financial strain on BRIL. An agreement was reached with some landlords but other landlords rejected the application on the basis of a lack of transparency. They objected because BRIL failed to make full disclosure of all material facts relating to the decision to close retail outlets and in particular to provide details of the criteria applied to determine which stores ought to be closed. It was also alleged that BRIL failed to provide confirmation that the same criteria was applied consistently across all stores and that any details of financial analysis carried out in order to make the decision had not been furnished. Notably in the application for the repudiation of unprofitable leases no repudiation was sought for the leases where there was a guarantee by AS. The judge referred to Clarke J. in the case *Re Traffic Group Limited*<sup>6</sup> who stated: "It is not designed to help shareholders whose investment has proved to be unsuccessful. It is to seek to save the enterprise and jobs." It was held that the leases excluded from the repudiation application were those that had guarantees by AS in order to protect the interest of AS which was the shareholder in BRIL. The application for the repudiation was refused.

The examiner for BRIL proceeded to make an application to the High Court for an order granting to him the powers of a liquidator pursuant to s.9 of the 1990 Act and granting him the power of an official liquidator to disclaim contracts to include leases. AS had removed the requirement to exclude the leases where there was a guarantee by AS from the application to disclaim as part of its proposal to invest in BRIL and the High Court allowed the examiner the power as an official liquidator to disclaim the leases.

### **Liquidation**

Liquidation is a process by which the assets of a company are realised and the proceeds distributed to the creditors and members in the order of priority as determined by the Companies Acts. There are two types of liquidations on insolvency:

*Creditors Voluntary Liquidation ("CVL")*—s.266 of the 1963 Act sets out the requirements to be observed in a CVL. A CVL is the process used where the company is insolvent. This is usually initiated by the insolvent company acting through its board. In a CVL the liquidator is primarily concerned with the interest of the creditors.

*Compulsory Liquidation* (also known as official liquidation)—a form of liquidation initiated by the order of the High Court. The procedure is commenced by way of petition normally by a creditor. The liquidator,

who is known as an official liquidator is appointed by the court and is an officer of the High Court for the duration of the liquidation. The petitioner in a compulsory liquidation is most commonly the company or creditor who petitioned on the grounds that a company is unable to pay its debts.

### **Right of Liquidator to Disclaim a Lease**

In the case of a tenant company going into liquidation, the liquidator has a right to disclaim an onerous lease, otherwise the rent shall become an expense of the liquidation to be met out of the company's assets to the extent that these are available. Leave of the court is required for a disclaimer. The right of the liquidator to disclaim a lease is governed by s.290 of the 1963 Act and s.290(1) states as follows:

Subject to subsections (2) and (5), where any part of the property of a company which is being wound up consists of land of any tenure burdened with onerous covenants, of shares or stock in companies, of unprofitable contracts, or of any other property which is unsaleable or not readily saleable by reason of its binding the possessor thereof to the performance of any onerous act or to the payment of any sum of money, the liquidator of the company, notwithstanding that he has endeavoured to sell or has taken possession of the property or exercised any act of ownership in relation thereto, may, with the leave of the court and subject to the provisions of this section, by writing signed by him, at any time within twelve months after the commencement of the winding up or such extended period as may be allowed by the court, disclaim the property.

The application is brought by the liquidator on the basis that the property of the company consists of land burdened "with onerous covenants". Where the liquidator does disclaim, the landlord may still be entitled to claim rent in full for the period in which the property is retained by the liquidator for the benefit of the creditors in general. That may be fixed as the period from the appointment of the liquidator to the date which the landlord obtains notice of intention to disclaim. Although a disclaimer by the liquidator discharges the company and the liquidator from further liability under the lease this does not affect the rights or liabilities of third parties which was confirmed in the case of *Maurice Tempamy v Royal Liver Trustees Limited (The Trustees of the Royal*

*Liver Friendly Society*).<sup>7</sup> This case was the subject of an application to disclaim a lease by a liquidator in accordance with s.290 of the 1963 Act. The lease was a 35-year lease which was granted by the landlord to Massey Ferguson (Eire) Limited ("MFEL"). Massey Ferguson Holdings Limited ("MFHL") was a third party to the lease acting as a guarantor. The TMG Group ("TMG") purchased the issued share capital of MFEL and also agreed to assume full responsibility for the guarantee provided by MFHL. TMG passed an ordinary resolution to be wound up on January 4, 1983, which was during a period when property markets were depressed. The liquidator was advised that the value of the lease was greatly decreased given the property market and in order to attract a potential assignee, a "reverse premium" would have to be paid to the assignee. The lease also contained an onerous covenant for repair and the landlord had served a notice on TMG of breaches of its repairing covenant and served it with a notice of dilapidations. The landlord also furnished the liquidator with a notice of further repairs and a further schedule of dilapidations.

The liquidator claimed that the lease was onerous as it represented a financial liability of approximately IR£1,250,000.00, being the rent payable which was in excess of the current market rents; the possible two-year period required to assign the lease to an assignee of the same covenant as the tenant given the deflated market; the reverse premium payable to a proposed assignee; and the cost of carrying out the repairs in respect of the schedule of dilapidations served. The solicitor acting on behalf of the liquidator wrote to the solicitor for the landlord requesting that the landlord agree to the surrender of TMG's interest in the lease advising that in the event that it refused that the liquidator would make the necessary application to disclaim the lease under s.290 of the 1963 Act. The landlord would not agree to the requested surrender and advised that it would reject any application made for an order allowing the liquidator liberty to disclaim. The liquidator made an

application for an order to disclaim the lease. The court also had to consider the position of the guarantor and to decide as to whether or not a disclaimer would terminate the responsibility of the guarantor provided in the lease. It was held by Keane J. that the liquidator could disclaim the lease and granted an order allowing the liquidator to disclaim the lease. It was further held that the release of the guarantor was not necessary for the purposes of releasing TMG and the property held by TMG from liability and that the liability of the guarantor was not affected by the disclaimer by the liquidator.

### Conclusion

It is evident from the case law, in particular that relating to examinerships, that leases may now be repudiated and disclaimed in both examinerships and liquidations which has been clarified by cases presented before the High Court and the Supreme Court. This is crucial to a business where the repudiation/disclaimer of onerous and burdensome leases may be necessary for the survival of the company from insolvency. Although this is welcome news to a tenant company, it is not such to a landlord. Where a landlord has a tenant who is suffering severe financial losses with a possibility of becoming insolvent due to the rent payable pursuant to the lease it may be in the interest of the landlord to reduce the rent temporarily so as to retain the tenant and review the matter when the economic market recovers. This enables the tenant to operate its business preserving employment and provides the landlord with much needed rent and occupancy of its property. In extreme cases it may be worthwhile for a landlord to consider temporarily suspending the rent payable until the tenant's business is operating profitably. This provides the landlord with the comfort of having its property occupied, secured, maintained (in accordance with the repairing obligation pursuant to the lease) and the outgoings discharged (save the rent payable). Failing the implementation of such measures landlords are now faced with the possibility of leases being repudiated or disclaimed.

<sup>1</sup> [2008] 3 I.R. 253.

<sup>2</sup> [2009] IEHC 465.

<sup>3</sup> [2009] IEHC 544.

<sup>4</sup> [2010] IEHC 28.

<sup>5</sup> [2010] IEHC 155.

<sup>6</sup> [2008] 3 I.R. 253.

<sup>7</sup> [1984] I.L.R.M. 273.