INSOLVENCY PROCEEDINGS VS PARTIES' AGREEMENT ON FORUM

THE PRIVY COUNCIL'S JUDGMENT IN SIAN V HALIMEDA

serle court

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This article examines the Privy Council's judgment in Sian Participation Corp v Halimeda International Ltd [2024] UKPC 16, where the court addressed the interplay between insolvency proceedings and forum selection clauses (i.e. arbitration clauses and exclusive jurisdiction clauses). The Privy Court held that, even if the underlying contract contains a forum selection clause, the debtor must demonstrate a genuine and substantial dispute on the debt before the court would stay the insolvency proceedings in favour of arbitration or the foreign court. In doing so, the Privy Council overturned the previous leading authority in England. This article also poses the question of whether the Privy Council's analysis represents a triumph of form over substance.

Arbitration Clauses, Exclusive Jurisdiction Clauses, And Insolvency: A Clash Of Public Policies

When faced with a winding up or bankruptcy petition, it is common for a putative debtor to resist the petition on the basis that the debt is disputed on substantial grounds. But what happens when the underlying contract contains an arbitration clause or an exclusive jurisdiction clause ("EJC")? Would the court stay the insolvency proceedings in favour of the parties' agreed forum (i.e. arbitration or a foreign court)? Or would the court still require the debtor to demonstrate that the dispute is based on sufficiently substantial grounds?

In recent years, the courts in numerous jurisdictions have grappled with this conundrum. Evidently, the courts have not found it easy to arrive at a solution, because there have been a profusion of conflicting decisions both within particular jurisdictions and between different jurisdictions.

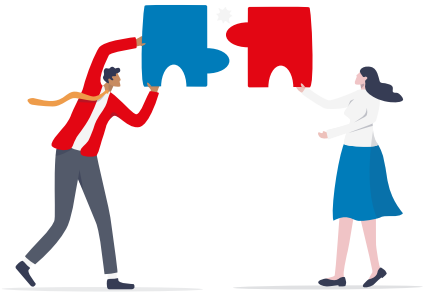
A key reason why the courts have struggled with this quandary is that it embodies a conflict between two important areas of public policy. On the one hand, the courts have long sought to give effect to party autonomy: the freedom for parties to agree how their disputes should be resolved (e.g. by arbitration or the courts of a particular country). On the other hand, there is a different public policy underpinning insolvency law: an aspiration for a system whereby an insolvent debtor can be efficiently placed into an insolvency process, through which its assets can be divided fairly among its creditors.

In Sian Participation Corp v Halimeda International Ltd [2024] UKPC 16, the Privy Council gave an authoritative answer, at least from the perspective of BVI and English law.

Sian V Halimeda: Background

The respondent (Halimeda) had advanced a loan to the appellant (Sian, a BVI company) under a facility agreement. The facility agreement included an arbitration clause which provided that "any claim, dispute or difference of whatever nature arising under, out of or in connection with" it would be referred to arbitration in London.

Sian did not repay the loan. Halimeda applied to the BVI court for the appointment of a liquidator over Sian (the equivalent of a winding up petition in England). However, Sian disputed the debt on the basis that it had a cross-claim against Halimeda (based on an alleged corporate raid aimed against Sian).



The BVI courts, at first instance and on appeal, held that Sian had failed to demonstrate a genuine and substantial dispute regarding the debt. The BVI courts also decided (following previous BVI authority[1]) that the existence of the arbitration clause did not automatically prevent Halimeda from commencing insolvency proceedings. Instead, Sian had to demonstrate that the debt was genuinely disputed on substantial grounds before the court would stay or dismiss the liquidation application in favour of arbitration.

Sian appealed to the Privy Council. Sian did not challenge the BVI courts' holding that the debt was not genuinely disputed on substantial grounds. However, Sian argued that, as a matter of law, the BVI courts should have dismissed or stayed the liquidation application in favour of arbitration, without requiring Sian to first demonstrate a genuine and substantial dispute.

Privy Council's Decision

The Privy Council (with Lord Briggs and Lord Hamblen giving the opinion) rejected Sian's appeal. It agreed with the BVI courts that a debtor had to demonstrate that the debt was genuinely disputed on substantial grounds before the court would give effect to an arbitration clause or EJC by staying or dismissing the liquidation application.[2] In doing so, it decided that the English Court of Appeal's decision in Salford Estates (No 2) Ltd v Altomart Ltd (No 2) [2014] EWCA Civ 1575 should no longer be followed, whether in the BVI or in England.[3]

Overturning Salford Estates

In Salford Estates, it was held that, where a creditor petitions to wind up a company on the basis of a debt but the underlying contract contains an arbitration clause, the court would, as a matter of discretion, generally dismiss or stay the petition in favour of arbitration. This was consistent with the policy underlying the Arbitration Act 1996, which was to enable parties to make binding agreements on the forum in which their disputes would be resolved. If a debtor were required to demonstrate a genuine and substantial dispute, that would oblige the court to undertake a "summary judgment type analysis", which would run contrary to that policy.[4]

The Privy Council held that Salford Estates was wrong. It observed that a winding up petition does not seek to resolve whether the debtor owes the petition debt to the creditor; does not result in a judgment for that debt; and is not analogous to a summary judgment application. Therefore, the presentation of such petition does not violate the

1 Jinpeng Group Ltd v Peak Hotels and Resorts Ltd BVIHCMAP2014/0025 (8 December 2015)
2 [5], [85], [99]
3 The Privy Council at [125] made a 'Willers v Joyce' direction, with the effect that its decision represented English law (as well as BVI law)
4 Salford Estates (No 2) Ltd v Altomart Ltd (No 2) [2014] EWCA Civ 1575, [39]-[41]

parties' agreement to have their disputes resolved by an arbitral tribunal or a foreign court. Applying to wind up the debtor company is simply not something that the petitioner has agreed to refrain from doing.[5]

The Privy Council dismissed a concern expressed in Salford Estates[6] that, if debtors were (despite any arbitration agreement) required to demonstrate substantial grounds for disputing the debt, that would encourage creditors to bypass the arbitration agreement by presenting a winding up petition, thereby putting pressure on the debtor to pay up. The Privy Council's answer was that the risk of abusive petitions could be met by ordering indemnity costs, which is a familiar tool used by the courts to deter creditors from using insolvency proceedings to collect disputed debt.[7]

Form Over Substance?

It could be argued that the Privy Council's decision represents a triumph of form over substance. Even if technically the nature of a winding petition is distinct from that of a summary judgment application, in substance they are closely related. In winding up proceedings, the court examines whether the debtor has raised a dispute on substantial grounds. In a summary judgment application, the court considers whether the defendant has any real prospect of defending the claim. In both contexts, the arguments advanced by counsel, and the substantive analysis conducted by the court, are likely to be similar.

Arguably, it is also artificial for the Privy Council to base its decision on the premise that a winding up petition does not seek to 'resolve' anything about the debt. Where a petitioner seeks a winding up order, he is for practical purposes asking the court to rule that the debtor has no substantial grounds to dispute the debt (at least to the threshold sum for a winding up petition).

It is instructive to compare the Privy Council's approach with those of the Hong Kong[8] and Singapore[9] apex courts. Those jurisdictions have essentially followed Salford Estates; in their view, where parties have included a forum selection clause in their contract, their intention is that the (domestic) court should not be engaged in deciding whether one party has raised a viable dispute on the debt; instead, that is a matter for the parties' chosen forum. It can be argued that the Hong Kong and Singapore courts' approach accords more with the practical experience of practitioners than the Privy Council's decision in Sian.

Lessons For Drafting

Intriguingly, the Privy Council commented that its analysis was applicable to a generally worded arbitration agreement or EJC, and that

"different considerations would arise" if the arbitration clause or EJC "was framed in terms" which covered insolvency proceedings.[10]

Thus, the Privy Council recognised (unfortunately, without elaboration) that it was possible to draft an arbitration clause or EJC which would incline the court to stay or dismiss a winding up petition without examining whether there was a genuine and substantial dispute on the debt.

The lesson is that if parties intend for all their disputes to be decided in the chosen forum and do not intend that the other party would be able to present a winding up petition against them for any alleged indebtedness, they should make express stipulation in their contract.

5 Sian, [82], [88]-[96]
6 Salford Estates, [40]
7 Sian, [82], [97].
8 Re Lam Kwok Hung Guy (2023) 26 HKCFAR 119. See also Re Simplicity & Vogue Retailing (HK) Co Ltd [2024] 2 HKLRD 1064 (CA) and Re Shandong Chenming Paper Holdings Ltd [2024] 2 HKLRD 1040 (CA)
9 AnAn Group (Singapore) Pte Ltd v VTB Bank (Public Joint Stock Co) [2020] 1 SLR 1158
10 [99], [127]