Kluwer Arbitration Blog

Arbitration Clauses, Insolvency Proceedings, and a Lack of Consistency Across the Common Law

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In the recent decision of *AnAn Group (Singapore) Pte Ltd v VTB Bank (Public Joint Stock Company)* [2020] SGCA 33 ("***AnAn***"), the Singapore Court of Appeal found that when a debtor challenges a winding-up application on the basis of a disputed debt or cross-claim that is subject to an arbitration agreement, the court should apply the *prima facie* standard of review in its determination, such that the winding-up proceedings will be stayed or dismissed if (a) there is a valid arbitration agreement between the parties; and (b) the dispute falls within the scope of the arbitration agreement, as long as that the dispute is not being raised by the debtor as an abuse of process.[1)]

For cases where the debt or cross-claim is **not** subject to an arbitration agreement, the standard of review remains whether there is a "*triable issue*". The debtor has to show that there exists a substantial and *bona fide* dispute, whether in relation to a cross-claim or a disputed debt.[2)]

The Court of Appeal's reasoning in its decision was that the reduced standard of review would "*promote coherence in the law concerning stay applications, so that parties to an arbitration agreement are not encouraged to present a winding-up application as a tactic to pressure an alleged debtor to make payment on a debt that is disputed or which may be extinguished by a legitimate cross-claim*".[3)] The Court further found:[4)]

> "[*u*]*nder the present dichotomy of standards, the applicable standard of review would depend solely on the creditor's arbitrary or tactical choice – if the creditor pursues an ordinary debt, the prima facie standard would apply; if the creditor applies, on the basis of the same disputed debt, for the debtor to be wound up, the higher triable issue would apply. This would in turn encourage the abuse of the winding-up jurisdiction of the court, which is not the appropriate forum to adjudicate on disputed claims that are subject to arbitration*".

The Singapore Court of Appeal adopted the same approach as the English Court of Appeal in *Salford Estates (No 2) Ltd v Altomart Ltd (No 2) [2015] Ch 589* ("***Salford***") which found that when faced with a disputed debt that is subject to an arbitration agreement, the English courts

ought to dismiss or stay the winding-up application save in "*wholly exceptional circumstances*", or this would otherwise "*inevitably encourage parties to an arbitration agreement – as a standard tactic – to bypass the arbitration and the [Arbitration Act 1996] by presenting a winding up petition*".[5)]

The authors respectfully submit that the approach espoused by the Singapore and English Courts of Appeal does not take into account the practical realities of the insolvency regime in either jurisdiction for the following reasons:

- There is a significant difference between an application for a stay in favour of arbitration, and an application for stay or dismissal of a winding-up application. In the former, whether there exists a dispute between the parties is not in issue: the issue for the court to determine is the correct forum for the dispute to be determined. The basis of a winding-up application, in contrast, is that the debtor has failed to pay a debt for which there is no substantial or credible dispute. The winding-up court is not a forum for dispute resolution: it is an enforcement court, which will only determine the threshold question of whether there exists a genuine dispute over a debt, so that such dispute may be resolved by another forum before enforcement.
- The test of "*substantial or bona fide dispute*" is the test that would be applied for any debt other than one which arises from a contract subject to arbitration. Following *AnAn* and *Salford*, a creditor now must prove that any dispute raised by a debtor is an abuse of process if the debt arises from a contract subject to an arbitration agreement, which is a higher threshold.
- In the circumstances where that higher threshold cannot be met, a creditor would now have to endure the time and expense of arbitration proceedings before being able to present a winding-up petition against the debtor company (or execute against its assets), without any certainty as to whether the costs of such arbitration proceedings will ultimately be recoverable against the company.
- The key principle espoused by both Courts is the importance of upholding the parties' bargain to arbitrate any disputes between them, and the legislative policy in favour of arbitration. These worthy ideals ignore the fact that the principle underlying the insolvency regime in both jurisdictions is the public interest in creditors being able to apply to wind up companies unable to pay their debts **where no *bona fide* dispute exists**. That principle has now been displaced such that it only applies where the debt does not arise from a contract subject to an arbitration agreement, thus creating a two-tier system where debts subject to litigation and arbitration are treated differently. Coherence in one area of the law has therefore been sacrificed in favour of coherence with the law concerning stay applications where, as respectfully submitted at point (1) above, no coherence is necessary.
- A key factor for the decision in *Salford* was that a court, when presented with a winding-up application, should not be able to conduct a summary judgment type of analysis on liability where the parties have agreed to submit all disputes to arbitration.[6)] However, a summary judgment is a final and conclusive decision on the merits, and this should not be conflated with the circumstances in which the triable standard of review would be applied as a threshold test to determine whether any *bona fide* dispute exists.
- The authors submit that there is in reality little risk of creditors abusing the winding-up regime by an "*arbitrary or tactical choice*" as to whether to pursue a claim for a debt, or make a winding up application. The triable issue standard of review is designed to distinguish cases where there is a *bona fide* and substantial dispute from those where there is not – that is what the test embodies, and any creditor who makes a winding-up application in the face of a credible dispute as to whether the debt is owed should fail – with liability to pay costs – without it being necessary to

introduce the lower *prima facie* standard of review for debts subject to an arbitration agreement.

- In any event, whilst the decision in *AnAn* was at pains to emphasise that the court, when presented with a winding-up application founded on a debt subject to arbitration, should not descend into any investigation of the merits of the dispute, even the *prima facie* standard of review, with the abuse of process safeguard, is likely, in practice, to involve some consideration of whether the debtor's dispute is *bona fide*. This begs the question as to how differently the tests will actually be applied in practice, and also whether the two-tier system put forward by the court will achieve its stated purpose.

Lack of Consistency Across the Common Law

The lack of consistency across the common law on this point illustrates that the approach adopted by the Courts in *AnAn* and *Salford* is by no means obvious.

The **Eastern Caribbean Court of Appeal** in *Jinpeng Group Ltd v Peak Hotels and Resorts Ltd (BVIHCMAP2014/0025 and BVIHCMAP2015/0003)* ("***Jinpeng***") departed from the *Salford* approach because the triable issue standard of review was "*too firmly a part of BVI law*",[7] and also because it felt that the *Salford* approach came too close to being an automatic stay position.

The **Malaysian High Court** took a different route in *Awangsa Bina Sdn Bhd v Mayland Avenue Sdn Bhd (WA-28NCC-1146-12/2018)* ("***Awangsa***"), adopting the *prima facie* standard of review after reviewing the authorities in England, Singapore and Hong Kong. The approach in Malaysia in fact operates like an automatic stay, because where there is an arbitration agreement, the court only has to "*ascertain whether there is a prima facie dispute of the debt claimed by the [applicant]*",[8] which the debtor may do simply by denying its indebtedness.

In *The City Hotel (Londonderry) Limited v Stephenson [2003] NICA 47*, the **Northern Irish Court of Appeal** rejected a submission that the debtor-company should satisfy a less onerous test than proving a *bona fide* dispute on substantial grounds to the debt which was subject to an arbitration clause.

In **Hong Kong,** *Re Southwest Pacific Bauxite (HK) Ltd [2018] 2 HKLRD 449* ("***Lasmos***") broadly adopted the position in *Salford*. This position was then cast with some uncertainty by the **Hong Kong Court of Appeal** in *But Ka Chon v Interactive Brokers LLC [2019] HKCA 873* where it expressed *obiter* reservations about the decision in *Lasmos*, considering it to be a substantial curtailment of a creditor's right under the existing insolvency legislation to present a winding-up application.

The recent **Hong Kong High Court** decision of *Dayang (HK) Marine Shipping Co, Ltd v Asia Master Logistics Ltd [2020] HKCU 494* applied the triable issue standard of review. Part of the Court's reasoning was that the presentation of a winding-up petition does not entail the submission of a dispute for the determination and/or resolution by the Court – disputes over the debt are only finally resolved upon determination by the liquidator, who acts in a quasi-judicial capacity. In the authors' view, this analysis misses the point – genuinely disputed debts should not reach a liquidator, and should be resolved by whatever forum the parties agreed to in their contract. As highlighted at point (6) above, this is what is entailed by the application of the threshold triable issue standard of review by the Court presented with a creditor's winding-up application.

The diverging caselaw within **Singapore** itself prior to *AnAn* illustrates some of the challenges with *AnAn's* approach. At [23] of *BDG v BDH [2016] SGHC 211*, the learned first instance judge found that if issues were not raised by a debtor *bona fide*, that would be a reason to find there is no *prima facie* dispute – this appears to conflate the triable issue and *prima facie* standards of review, which is a risk of the two-tier system introduced by *AnAn*. The key objection to *AnAn's* approach was well summarised by the learned first instance judge in *VTB Bank (Public Joint Stock Co) v Anan Group (Singapore) Pte Ltd [2018] SGHC 250* at [67] as follows:

> "*On the whole, the Salford approach appears to "place a very heavy obstacle in the way of a party who presents a petition claiming sums due under an agreement that contains an arbitration clause" (see Eco Measure at [10]). This may be seen to deal a blow to the insolvency regime since creditors legitimately seeking to wind up insolvent companies may be delayed in or entirely derailed from the recovery of their debts by debtor-companies, which would be able to stave off winding up proceedings simply by raising disputes which they say should be resolved by arbitration, even if these allegations may be entirely unmeritorious.*"

Last Word

It is possible that the position expressed in *AnAn* will not be the last word of the Singapore Court of Appeal on this issue. It remains to be seen how matters will evolve from what the Singapore Court of Appeal describes in the case as "*the perceived state of flux in the Commonwealth on this issue*"[9] and, in particular, whether this issue will be reconsidered by the English courts, whose judgments continue to provide guidance and inspiration across the common law. In the authors' humble submission, the approach adopted by both the Singapore and English courts merits revisiting.

References

?1 The views expressed in this blog are those of the authors and do not represent the views of their firm.

?2 *AnAn* at [25].

?3 *AnAn* at [60].

?4 *AnAn* at [63].

?5 *AnAn* at [30], citing *Salford* at [40].

?6 *Salford* at [40].

?7 *Jinpeng* at [47].

?8 *Awangsa* at [25].

?9 *AnAn* at [88].

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