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UPDATE

Arbitration clauses and winding up petitions: The future of arbitration stay applications in the BVI

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The recent decision of the BVI Court of Appeal in the case of C-Mobile Services Limited v Huawei Technologies Co. Limited BVIHCMAP 2014/0006, considered the availability of stays of winding-up proceedings based upon contracts containing arbitration clauses. This update discusses that case and its implications.

Two recent decisions of the BVI Court of Appeal in the case of *C-Mobile Services Limited v Huawei Technologies Co. Limited* BVIHCMAP 2014/0006 and BVIHCMAP 2014/0017, concerning the interplay between section 6(2) of the 1976 Arbitration Ordinance and the Insolvency Act 2003, serves to highlight why the old Arbitration Ordinance has benefitted from revision, whilst leaving open the door for the courts to resolve the apparent conflict between the circumstances in which the mandatory stay provisions in section 18 of the new BVI Arbitration Act 2013 are engaged.

C-Mobile concerned an unsuccessful application to set aside a statutory demand under section 156(1) of the Insolvency Act 2003, followed (one month later) by an unsuccessful application under section 6(2) of the Arbitration Ordinance to stay proceedings to appoint liquidators over the company on the grounds of an arbitration stay. On appeal the two applications were heard back-to-back, however, the Court of Appeal was careful to ensure that its judgments were handed down in the order in which the applications were determined at first instance. This is of some significance, as the dismissal of the appeal to set aside the statutory demand played a part in the Court's determination of the appeal on the arbitration stay.

Turning first to the application to set aside the statutory demand, one of the grounds for the application, at first instance, was that the alleged debt giving rise to the statutory demand arose under a contract which contained an arbitration clause. The applicant sought to rely upon Bannister J's decision in *Applied Enterprises Ltd v Interisle Holdings Ltd et al* BVIHVC (COM) 2012/0135 in which the Court had stayed a claim brought to enforce various provisions of an agreement on the basis of an arbitration clause contained in that agreement. Crucially, although as the court in Applied Enterprises had recognized, there was a substantial dispute between the parties in that case, Bannister J had stated that it was not necessary for there to be a substantial dispute in light of the narrow interpretation of the extent of the Court's merits review jurisdiction suggestion by Lord Mustill in *Channel Tunnel Group Ltd v Balfour Beatty Construction Ltd* [1993] AC 334. Bannister J held that even if the dispute was not a substantial one, a stay should be granted.

However, in C-Mobile the BVI Commercial Court made short shrift of the company's argument relying on the arbitration clause. It said that Applied Enterprises did not apply to applications to set aside statutory demands. If it did, the Court said, the BVI case of *Sparkasse Bregenz Bank AG v Associated Capital Corporation BVI Civ App* 10/2002 (which held that the court will strike out a petition if the respondent to that petition 'can demonstrate that the alleged debt on which the petition is founded is genuinely disputed on substantial grounds') would be wrong. This is because, in order to strike out a petition, a respondent would only need to show the existence of *any* dispute, rather than a genuine dispute on 'substantial grounds'.

On appeal, the Court of Appeal upheld the BVI Commercial Court's decision. Pereira CJ said:

'To my mind however, the learned judge was perfectly entitled to treat the point as summarily as he did as no further development of the point would result in a more favorable result. The court was here dealing with the setting aside of a statutory demand which is a precursor to the commencement of proceedings for the appointment of a liquidator on insolvency grounds.

This has nothing to do with proceedings brought to recover a disputed debt which has arisen under an agreement containing an arbitration clause covering such dispute under the agreement as was the case in Applied Enterprises. In my view, he was right to hold that Applied Enterprises was decided in a completely different context and was not applicable in the context of an application to set aside a statutory demand on the basis of a substantial dispute as required to be shown under section 157(1) of the IA.'

Accordingly, the Court of Appeal held that absent any dispute on substantial grounds, it was not prepared to set aside the statutory demand, irrespective of the fact that relevant contract (which gave rise to the disputed debt) contained within it an arbitration clause.

Having reached this conclusion on the application to set aside the statutory demand, the Court of Appeal then went on to consider 'whether the winding up proceedings which have been commenced on the basis of the underlying ... [d]ebt are caught by the arbitration clause in the Supply Contract so as to bring the liquidation proceedings within the ambit of section 6(2) of the Arbitration Ordinance.'

Section 6(2) of the Arbitration Ordinance (the mandatory stay provisions) was drafted in materially different terms to the current mandatory stay provisions to be found in section 18 of the BVI Arbitration Act 2013.

Section 6(2) provides that:

'if any party to an arbitration agreement ... commences any legal proceedings in any court against any other party to the agreement ... in respect of any matter agreed to be referred, any party to the proceedings may at any time after appearance, and before delivering pleadings or taking any other steps in the proceedings, apply to the court to stay the proceedings; and the court, unless satisfied that that arbitration agreement is null and void, inoperative or incapable of being performed or that there is not in fact a dispute between the parties with regard to the matter agreed to be referred shall make an order staying the proceedings.'

Section 18 of the BVI Arbitration Act 2013 (which came into force on 1 October 2014) provides:

'(1) A court before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party so requests not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.'

Section 18 is very similar in scope to section 9 of the English Arbitration Act 1996. However, unlike the English Act, the BVI Legislation more closely resembles the Model Law.

In considering whether a mandatory stay under section 6(2) of the Arbitration Ordinance was engaged, the Court of Appeal commented that the starting point was to consider whether an application to wind up a company is a dispute arising out of or in connection with the formation, construction and performance of the contact such that it can be considered to be legal proceedings commenced in respect of any matter agreed to be referred to arbitration.

On this issue, the Court of Appeal held that an application to wind up a company, although it may be premised on the underlying debt, is not an action or proceeding on the debt or under contract. It is a class remedy which falls outside the scope of the arbitration clause and in so concluding the court relied on the English Court of Appeal in the case of *Salford Estates (No.2) Limited v Altomart Limited* [2014] EWCA Civ 1575.

In Salford Estates, the English Court of Appeal considered the High Court's decision to stay a winding up petition, due to the fact that the debt which was the subject of the petition arose out of a lease that contained an arbitration clause. In that case the High Court had regarded itself as bound to stay the winding up petition, by the mandatory stay provisions in sections 9(1) and 9(4) of the English Arbitration Act, which provides as follows:

'(1) A party to an arbitration agreement against whom legal proceedings are brought (whether by way of claim or counterclaim) in respect of a matter which under the agreement is to be referred to arbitration

may (upon notice to the other parties to the proceedings) apply to the court in which the proceedings have bene brought to stay the proceedings so far as they concern that matter.'

'(4) On an application under this section the court shall grant a stay unless satisfied that the arbitration agreement is null and void, inoperative, or incapable of being performed.'

The Court of Appeal disagreed with this conclusion, holding that an issue on a winding up petition relating to a disputed debt does not become a claim falling within section 9 of the English Arbitration Act. Accordingly, the court is not bound by the Arbitration Act to stay that petition. This conclusion is similar to the one reached by the BVI Courts in relation to the stay sought in C-Mobile.

However, the English Court of Appeal then went on and held that section 122(1)(f) of the English Insolvency Act 1986 confers on the court a discretionary power to wind up a company and that this power should, save in wholly exceptional circumstances, be exercised consistently with the legislative policy embodied in the 1996 Arbitration Act. It went on to say that:

- it would be anomalous, in the circumstances, for the companies' court to conduct a summary judgment type analysis of liability for an unadmitted debt, on which a winding up petition is grounded, when the creditor has agreed to refer any dispute relating to the debt to arbitration;
- exercise of the discretion otherwise than consistently with the policy underlying the Arbitration Act would inevitably encourage parties to seek to bypass arbitration agreements by presenting winding up petitions, which would be entirely contrary to the parties' agreement as to the proper forum for the resolution of such issues and to the legislative policy of the 1996 Act; and
- in those circumstances, as a matter of the exercise of the court's discretion under the Insolvency Act, it was right for the court either to dismiss or to stay the petition so as to compel the parties to resolve their dispute over the debt by arbitration, rather than require the court to investigate whether or not the debt is bona fide disputed on substantial grounds.

In C-Mobile, the BVI Court of Appeal considered the relevant passages from the Court of Appeal's judgment in Salford Estates; however, distinguished the application of the case to C-Mobile's appeal on the following grounds:

First, the arbitration clause in Salford Estates was deemed to be wider in scope than the arbitration clause in C-Mobile. Secondly, the court held that it had already adjudicated on the question of whether the debt in C-Mobile's case was disputed on substantial grounds. Having agreed with the finding at first instance, the Court of Appeal held that there was no dispute to form the basis of a stay application. Thirdly, the arbitration proceedings initially commenced by C-Mobile were no longer on foot, having been withdrawn earlier that year.

In reaching its conclusion, the Court of Appeal noted that it did so having due regard to the policy reasons underlying the mandatory stay provisions in the Ordinance and the need to discourage parties from seeking to bypass their chosen method of dispute resolution. However, once a statutory demand had been served on a company, then the burden was on the company to demonstrate that the debt was disputed on bona fide and substantial grounds, or by asking the court to exercise its discretion and set aside the statutory demand, by showing that to maintain it would cause substantial injustice, for example the referral to arbitration.

Conclusion

Although the decision in C-Mobile endorses the continued maintenance of a distinction between winding up proceedings and the mandatory stay provisions in the arbitration Ordinance, the judgment made it clear that 'the court must always be astute to ensure that it is giving effect to the terms of the parties' bargain as it relates to their agreed forum for settling their disputes'. In this regard the Court of Appeal noted the discretion afforded to the court under section 162 of the Insolvency Act in deciding whether or not liquidators should be appointed.

This decision was rendered under the provisions of the Arbitration Ordinance, which is no longer in force; however, it serves to demonstrate that this continues to be a developing area of law and, given the similarities between section 18 of the BVI Act and section 9 of the English Act, it will be interesting to see whether, in the future, the BVI courts elect to follow the English courts' approach to these issues and, if so, in what circumstances the BVI courts might be prepared to stay winding up petitions based on contracts containing arbitration clauses.

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