No More Automatic Stays for Winding-Up Petitions Involving an Arbitration or Exclusive Jurisdiction Clause

20 June 2024

At a Glance

The Privy Council — the court of final appeal for UK overseas territories — yesterday ruled on how to approach winding-up petitions where the relevant debt is subject to an arbitration or exclusive jurisdiction clause. The decision in *Sian Participation v Halimeda* considers public policy issues on the intersection of arbitration and insolvency. It adjusts not only BVI law but also English law. The judgment means that:

- where the debt on which a winding-up petition (or liquidation application) is based is subject to an arbitration agreement[1] or an exclusive jurisdiction clause[2], and
- the relevant debt is disputed, then
- the correct test for English and BVI courts to apply, in considering the exercise of their discretion whether to make an order for the liquidation of a company, is whether the debt is disputed on genuine and substantial grounds.

This adjusts the current practice[3] under which the court found it had discretion (under the Arbitration Act) to stay creditors' winding-up petitions where an insubstantial dispute about the creditor's debt was raised between parties to an arbitration agreement.

In practice, this shift means that where a creditor seeks to wind up a debtor based on a debt that is subject to an arbitration clause or an exclusive jurisdiction clause in favour of another jurisdiction, parties' original expectations of resolving disputes via arbitration or in another court may not be borne out:

arbitration award before enforcing a debt which is completely undisputed. "To require the creditor to go through an arbitration where there is no genuine or substantial dispute as the prelude to seeking a liquidation just adds delay, trouble and expense for no good purpose. Party autonomy [is] not offended because seeking a liquidation is not something which the creditor has promised not to do"; and

- similar issues arise for exclusive jurisdiction clauses, depending on the proper interpretation of the relevant clause — "if there is no breach of the clause then there is no basis for a stay" (of the winding-up petition).

In such circumstances, it will now be easier for the creditor to succeed in (and harder for the debtor to oppose) a winding-up petition, because the court's discretion to refuse will *only* arise if the debt is disputed on genuine and substantial grounds — and not merely by virtue of the fact that the debt is subject to an arbitration or exclusive jurisdiction clause.

The court was clear that "above all there is nothing anti-arbitration in this conclusion". If anything, parties (in particular, lenders) are more likely to agree to include an arbitration clause if it does not impede a liquidation where there is no genuine or substantial dispute about the debt.

Background

The relevant facility agreement included an arbitration clause to the effect that any dispute arising in connection with the agreement would be referred to arbitration at the London Court of International Arbitration. The loan was not repaid. The BVI-incorporated debtor disputed that the debt was due and payable, on the basis of a cross-claim and/or set-off, amid allegations of a "corporate raid" backed by Russia and allegedly assisted by the creditor (although such allegations were denied).

The creditor successfully applied for the debtor's liquidation in the BVI, with the court finding that (a) the debtor had failed to show the debt was disputed on genuine and substantial grounds or that there were other reasons why the liquidation application ought to be dismissed (or stayed) and (b) there was no *prima facie* case of a cross-claim. The BVI Court of Appeal upheld (b) on appeal; the debtor did not appeal the finding in (a).

Upholding the BVI Court of Appeal's decision, the Privy Council held that, as a matter of English and BVI law:

- the correct test for the court to apply to the exercise of its discretion whether to make an order for the liquidation of a company, where the debt on which the application is based is subject to an arbitration agreement or an exclusive jurisdiction clause and is said to be disputed, is whether the debt is disputed on genuine and substantial grounds; and
- current practice — in exercising a supposed discretion to stay or dismiss a creditors' winding-up petition on the ground that the debt is covered by an arbitration clause, without being shown to be genuinely disputed on substantial grounds — should no longer be followed.

This conclusion applies to a generally worded arbitration agreement or exclusive jurisdiction clause. Different considerations would arise if the agreement or clause was framed in terms which applied to such a liquidation application.

This decision is expected to influence the approach in insolvency courts of other jurisdictions. In particular, the courts of Malaysia and Singapore currently follow the former English approach, whilst there have been divergent decisions in Hong Kong. We expect such courts will soon need to consider whether to adjust their approach in light of this decision.

---

1. In which the parties agree to refer disputes under the agreement to arbitration. ↩

2. In which the parties have granted a court in another jurisdiction the exclusive jurisdiction to rule on claims under the agreement. ↩

3. Pursuant to the judgment of the Court of Appeal in *Salford Estates (No. 2) Ltd v Altomart Ltd* [2014] EWCA Civ 1575, and subsequent cases. ↩

Author

Kate Stephenson

Related Services

Practices

- Restructuring

Suggested Reading

- 14 June 2024 Award Lawdragon Recognizes 17 Kirkland Attorneys in its 2024 List of 500 Leading Global Bankruptcy & Restructuring Lawyers
- 13 June 2024 Award Kirkland Named Bankruptcy Law Firm of the Year at Chambers USA Awards 2024
- 12 June 2024 Kirkland Alert English Court Imposes >£18 Million Personal Liability on Former Directors of BHS for Breach of Directors' Duties and Wrongful Trading