The Privy Council makes landmark decision on the arbitrability of winding up petitions

Insights - 26/10/2023

In the recent decision of *FamilyMart China Holding Co v Ting Chuan (Cayman Islands) Holding Corporation* [2023] UKPC 33 (***FamilyMart***),[1] the Judicial Committee of the Privy Council (the **Board**) found that, although an arbitral tribunal does not have the power to determine whether it is just and equitable to wind up a company nor to make a winding up order, it may determine matters underlying a winding up petition. The Board heard this case and two other cases[2] in the week of 15 to 18 November 2022 in the historic first ever sitting of the Board to occur in the Cayman Islands. The Board's decision in *FamilyMart* is a landmark decision on the issue of arbitrability and provides useful guidance for shareholders, directors and other stakeholders of Cayman companies on the interaction between arbitration clauses and the just and equitable jurisdiction.

Background

China CVS (Cayman Islands) Holding Corp (the **Company**) is a Cayman Islands holding company which operates a convenience store business in the People's Republic of China under the "FamilyMart" brand. The Company is a joint venture between the majority shareholder, Ting Chuan (Cayman Islands) Holding Corporation (**Ting Chuan**) and the minority shareholder, FamilyMart China Holding Co. Ltd (**FMCH**). The relationship between the two shareholders is governed by a shareholders agreement which contains an arbitration clause.

The Petitioner presented a petition to wind up the Company on the just and equitable ground (the **Petition**) and sought alternative relief in the form of buyout orders pursuant to section 95(3) of the Companies Act. The Petition is, in part, based on allegations that the majority directors, nominated by Ting Chuan, had caused the Company to engage in extensive related party dealings which were not disclosed to the minority directors appointed by FMCH or to FMCH itself in its capacity as minority shareholder. FMCH alleged this, among other things, had given rise to a loss of trust and confidence which justified a finding that it would be just and equitable to wind up the

Company.

At first instance, Kawaley J ordered that the Petition be stayed pursuant to section 4 of the Foreign Arbitral Awards Enforcement Act (1997 Revision) (the **FAAEA**) until the complaints therein had been arbitrated. On appeal, the Cayman Islands Court of Appeal (**CICA**) found that no part of the Petition was arbitrable and overturned Kawaley J's decision. Ting Chuan was granted leave to appeal to the Board.

Before the Board, Ting Chuan contended that the questions in issue in the proceedings were divisible into five separate "matters" as follows:

(1) Whether FMCH has lost trust and confidence in Ting Chuan and in the conduct and management of the Company's affairs.

(2) Whether the fundamental relationship between FMCH and Ting Chuan has irretrievably broken down.

(3) Whether it is just and equitable that the Company should be wound up.

(4) Whether FMCH should be granted the alternative relief, which it prefers, under section 95(3)(d) of the Companies Act, namely an order requiring Ting Chuan to sell its shares in the Company to FMCH, and, if so, what is the value of those shares.

(5) Whether, if such alternative relief is not appropriate, an order winding up the Company should be made and whether the persons identified by FMCH should be appointed as joint official liquidators.

While both parties agreed that matter (5) was not arbitrable as only the Court could make a winding up order, Ting Chuan contended that matters (1) to (4) were arbitrable or, in the alternative, only matters (1) and (2) were arbitrable. FMCH's position was that none of the matters were arbitrable.

Section 4 of the FAAEA

In forming its decision, the Board focused on the proper construction of section 4 of the FAAEA, including by reference to similar provisions throughout the common law world. Section 4 provides:

"If any party to an arbitration agreement, or any person claiming through or under him, commences any legal proceedings in any court against any other party to the agreement, or any person claiming through or under him, in respect of any matter agreed to be referred, any party to the proceedings may at any time after appearance, and before delivering any pleadings or taking any other steps in the proceedings, apply to the court to stay the proceedings; and the court, unless satisfied that the arbitration agreement is null and void, inoperative or incapable of being

performed or that there is not in fact any dispute between the parties with regard to the matter agreed to be referred, shall make an order staying the proceedings." (emphasis added)

The two key legal issues before the Board which arise from section 4 of the FAAEA were:

1. What is a matter agreed to be referred?
2. When is an arbitration agreement inoperative?

What is a "matter"?

A number of recent authorities from common law jurisdictions have construed "matter" in a broad and expansive manner.[3] The decision in *FamilyMart* was handed down on the same day as and determined in parallel with the UK Supreme Court decision in *Republic of Mozambique (acting through its Attorney General) v Privinvest Shipbuilding SAL* [2023] UKSC 32 (***Mozambique***) which also considered the meaning of the term "matter". Although both *FamilyMart* and *Mozambique* represent a retreat from some of the most expansive language of the recent cases, they nevertheless give a broad definition to the term "matter" as follows:

"a substantial issue that is legally relevant to a claim or a defence, or foreseeable defence, in the legal proceedings, and is susceptible to be determined by an arbitrator as a discrete dispute. If the "matter" is not an essential element of the claim or of a relevant defence, it is not a matter in respect of which the legal proceedings are brought……a "matter" requiring a stay does not extend to an issue that is peripheral or tangential to the subject matter of the legal proceedings……a "matter" is something more than a mere issue or question that might fall for decision in the court proceedings or in the arbitral proceedings."[4] (emphasis added)

The Board further held that:

1. The definition of a "matter" does not cover "all issues which may be the subject of the arbitration agreement" and the matters must be of "reasonable substance". [5]
2. No judicial formula encapsulating the meaning of "matter" should be treated as if it were a statutory test and the Court should approach the question in a practical and common-sense way. [6]
3. The complexity and practical futility of a stay is not an irrelevant consideration, but such fragmentation could be resolved by effective case management and was not necessarily a basis on which to conclude that a "matter" was not arbitrable. [7]

Arbitrability

The Board then considered the meaning of the phrase "the arbitration agreement is….inoperative" in section 4 of the FAAEA, which relates to the question of arbitrability. The Board referred to two

types of non-arbitrability: (i) subject matter non-arbitrability: where certain disputes are excluded by statute or public policy from determination by arbitration; and (ii) remedial non-arbitrability: where the award of certain remedies is beyond the jurisdiction which the parties can confer.[8]

As to remedial non-arbitrability, which was relevant to the appeal, the Board pointed out that there was strong authority for the proposition that the power to wind up a company lies within the exclusive jurisdiction of the Court.[9] However, the Board noted that:

1. there was general consensus from the cases that an arbitral tribunal has the power to grant inter partes remedies such as buy out orders, notwithstanding the fact that the power to make such orders are provided by statute; [10]and
2. there was "substantial agreement amongst common law jurisdictions" that in an application to wind up a company on just and equitable grounds there may be matters in dispute between the parties, such as breaches of a shareholders' agreement, which can be referred to an arbitral tribunal for determination, notwithstanding that only a court can make a winding up order. [11]The Board concluded that:

"Matters, such as whether one party has breached its obligations under a shareholders' agreement or whether equitable rights arising out of the relationship between the parties have been flouted, are arbitrable in the context of an application to wind up a company on the just and equitable ground and the arbitration agreement is not inoperative because the arbitral tribunal cannot make a winding up order."[12] (emphasis added)

Were matters (3) and (4) arbitrable?

On the question of whether the arbitral tribunal could make a finding as to whether it was just and equitable that the Company be wound up and the appropriate form of remedy, the Board agreed with the interpretation of the Companies Act provided by Moses JA in the judgment of the CICA, and said:

1. The Court's consideration under section 92 of the Companies Act as to whether it is just and equitable that a company should be wound up is a threshold question which must be answered before a petitioner can gain access to any of the remedies available under section 95; [13]
2. When considering whether to make a winding up order, the Court must make a wide ranging enquiry into and evaluation of the facts and the relevant circumstances which exist at the date of the hearing; [14]
3. An arbitrator's decision that a winding up order should be made based on circumstances which existed at an earlier date could not determine the issue which the Court has to consider, and the obiter suggestion by Patten LJ in *Fulham Football Club (1987) Ltd v Richards*[15] that an arbitrator could make a ruling on whether it would be appropriate for a complainant to initiate

winding up proceedings or be limited to some other remedy was incorrect; [16]

4. a ruling by a tribunal that it was of the view that it is just and equitable that a company be wound up would be ineffective and it could not bind the parties in a hearing before the Court and, given the interests of third parties in a possible winding up of the company which must be taken into account under section 95 of the Companies Act, [17]it could also not bind the court.

Accordingly, the Board agreed with FMCH's position that matters (3) and (4) were not arbitrable and that a tribunal does not have the power to decide whether it is just and equitable that the company should be wound up or the alternative remedy to be granted.

Were matters (1) and (2) arbitrable?

As to whether the factual matters underlying the petition were arbitrable (the loss of trust and confidence and relationship breakdown) the Board found:

1. Although a fragmented process (involving both an arbitration and court proceedings) may frustrate the expectations of reasonable businesspeople, this was a policy question which may be relevant to consider when considering the interpretation of the arbitration agreement. [18]However, it was not a relevant factor in the arbitrability of matters (1) and (2) and the Board was not satisfied that the risk of delay excluded those matters from arbitration, particularly in light of the parties' contractual obligations. [19]

2. There was nothing stopping the parties from presenting the Court with a statement of agreed facts following arbitration and such a statement could include, in principle, an agreement on matters (1) and (2). [20]Since the Court would be bound by any such statement, there is no reason why it would not be bound that way in respect of a question determined by an arbitral tribunal. [21]

3. The fact that all that the arbitral tribunal would be able to render at the close of an arbitration on matters (1) and (2) was a declaration did not change the fact that they were arbitrable. [22]

The Board thus concluded that findings as to loss of trust and confidence and irretrievable breakdown of a corporate relationship are "matters" under section 4 of the FAAEA for which a stay of the winding up proceedings was mandated.[23]

Conclusion

Ultimately, the appeal was allowed as, although the Board agreed with FMCH that the question of winding up and remedy were not arbitrable, it agreed with Ting Chuan that the existence of a loss of trust and confidence and irretrievable breakdown were arbitrable, giving rise to a mandatory arbitration stay under section 4 of the FAAEA.

FamilyMart is a groundbreaking decision on the interplay between arbitration and the winding up jurisdiction of common law courts. Although the Board confirmed that an arbitral tribunal has no jurisdiction to make a winding up order nor any jurisdiction to decide whether it is just and equitable to wind up a company, it found that certain matters which underlie a winding up petition (i.e. allegations of wrongdoing) are arbitrable. Therefore, in cases where there is an arbitration agreement, those underlying allegations may need to be resolved and determined through arbitration before the Grand Court will consider whether it is just and equitable to wind up the company.

It will be interesting to see how the Court will case manage winding up petitions stayed due to an arbitration clause, however, the bifurcated approach adopted by the Board may lead to procedural difficulties. For instance, there may be cases where, between the date of the arbitral award and the date of the hearing before the Court, there are allegations of further oppressive conduct which could constitute grounds for winding up. Given the need for a Court to form an opinion as to whether it is just and equitable to wind up a company as at the date of the hearing,[24] this could result in the Court being compelled to order that the parties return to arbitration to determine whether such conduct occurred and, if so, whether it supports a finding that trust and confidence has broken down. In cases where oppressive conduct is ongoing, such an approach could lead to an unmanageable, potentially never-ending merry-go-round of arbitration and Court hearings. While this argument was raised before the Board, it was ultimately not addressed in the judgment.

In the meantime, given the prevalence of just and equitable winding up petitions in the Cayman Islands (and the absence of a statutory remedy for unfair prejudice or oppression), shareholders of Cayman companies should carefully review their shareholders' agreements before presenting a winding up petition. If those agreements contain arbitration clauses, although the clause will not, of itself, prevent them from presenting a winding up petition, they might be obliged to have the underlying disputes of fact resolved via arbitration before seeking relief from the Grand Court.

[1] Ogier (Cayman) LLP together with Tom Lowe KC of Wilberforce Chambers and Hilary Stonefrost of South Square Chambers, acted on behalf of the Respondents. This article was co-authored with Hilary Stonefrost and was also published in the South Square Digest.

[2] The other two cases were a property dispute and a claim relating to the Bill of Rights of the Cayman Islands: *HEB Enterprises Ltd v Richards* [2023] UKPC 7; *Ramoon v Governor of the Cayman Islands* [2023] UKPC 9.

[3] This included the Singapore Court of Appeal Decision of *Tomolugen Holdings Ltd v Silica Investors Ltd* [2015] SGCA 57 (***Tomolugen***), and the English decisions of Popplewall J in *Sodzawiczny v Ruhan* [2018] EWHC 1908 (Comm) (***Sodzawiczny***) and the English Court of Appeal in *Republic of Mozambique (acting through its Attorney General) v Credit Suisse International* [2021] EWCA Civ

329.

[4] *FamilyMart* at [61] citing *Tomolugen* at [113]; *WDR Delaware Corporation v Hydrox Holdings Pty Ltd* [2016] FCA 1164 at [110]; *Mozambique* at [75].

[5] *FamilyMart* at [63] citing *Tomolugen* at [113] and disagreeing with *Sodzawiczny* at [63].

[6] *FamilyMart* at [64].

[7] *FamilyMart* at [66].

[8] *FamilyMart* at [69].

[9] *FamilyMart* at [75].

[10] *FamilyMart* at [76] citing *Fulham* at [77]-[78], [96] and [99]; *Tomolugen* at [88]-[89] and [103] and *WDR Delaware* at [147].

[11] *FamilyMart* at [77] citing *Fulham* at [76]; *Quiksilver Greater China Ltd v Quiksilver Glorious Sun JV Ltd* [2014] 4 HKLRD 759 at [14]; *Tomolugen* at [96]-[103]; *WDR Delaware* at [161]-[164].

[12] *FamilyMart* at [78].

[13] *FamilyMart* at [80].

[14] *FamilyMart* at [81] citing *Lau v Chu* [2020] UKPC 24 at [43].

[15] [2011] EWCA Civ 855.

[16] *FamilyMart* at [81] citing *Fulham* at [83]; *Tomolugen* at [100].

[17] See *Fulham* at [46]; *In re Neath Rugby Ltd* [2009] EWCA Civ 291, [2010] BCC 597 at [84]; *In re Asia Television Ltd* [2015] 1 HKLRD 607 at [55]-[58].

[18] *FamilyMart* at [89].

[19] *FamilyMart* at [90].

[20] *FamilyMart* at [92].

[21] In relation to an arbitration between FMCH and Ting Chuan, such a finding would be binding under Article 35(6) the ICC Rules of Arbitration: *FamilyMart* at [93].

[22] *FamilyMart* at [96].

[23] *FamilyMart* at [97].

[24] *Lau v Chu* [2020] 1 WLR 4656 at [43] per Lord Briggs JSC.

About Ogier

Ogier is a professional services firm with the knowledge and expertise to handle the most demanding and complex transactions and provide expert, efficient and cost-effective services to all our clients. We regularly win awards for the quality of our client service, our work and our people.

Disclaimer

Key Contacts

Corey Byrne

Senior Associate

Cayman Islands

E: corey.byrne@ogier.com

T: +1 345 815 1842

Oliver Payne 彭奥礼

Partner 合伙人

Hong Kong

E: oliver.payne@ogier.com

T: +852 3656 6044

Gemma Bellfield (nee Lardner)

Partner

Cayman Islands

E: gemma.bellfield@ogier.com

T: +1 345 815 1880

Edwin Gomez

Counsel 顾问律师

Hong Kong

E: edwin.gomez@ogier.com

T: +852 3656 6046

Related Services

Dispute Resolution