Which Trumps: Creditor Protection or Choice of Forum?

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Divergence between England & Wales and the British Virgin Islands in the Treatment of Jurisdiction and Arbitration Clauses in Insolvency Proceedings

Introduction

Any insolvency lawyer in the British Virgin Islands (**"BVI"**) or in England & Wales (**"E&W"**) will tell you that the most common ground for seeking to set aside a statutory demand, or opposing the appointment of a liquidator, is an allegation that the debt is disputed. They will also tell you that the test is whether the Court is satisfied that the debt is disputed on *substantial and bona fide* grounds. The concept of a *substantial and bona fide* dispute is so entrenched in the authorities that it seems uncontroversial. Yet the Court of Appeal in each jurisdiction has come to a strikingly different conclusion about what it really means when there is a jurisdiction or arbitration clause.

'Substantial Dispute'

In E&W the test to set aside a statutory demand or challenge a winding-up petition is a common law one. The debtor must show that the debt is:

> *"bona fide disputed on substantial grounds"*
>
> (***Arena Corporation Ltd v Schroeder*** **[2004] EWCA Civ 37**)

In the BVI the 'substantial dispute' test is on a statutory footing. In s. 157 Insolvency Act 2003 (BVI) (**IA 2003**) the requirements are:

> *"(1) The Court shall set aside a statutory demand if it is satisfied that*

(a) there is a substantial dispute as to whether-

(i) the debt; or

(ii) a part of the debt sufficient to reduce the undisputed debt to less than the prescribed minimum, is owing or due;"

In the BVI and E&W the common law is aligned on what constitutes a substantial dispute. In the E&W decision of ***Collier v P & MJ Wright (Holdings)*** **[2008] 1 WLR 643** it is explained as follows:

"…the burden was on [the debtor] *to show that there was a genuine triable issue that would be incapable now for* [the creditor] *to insist on payment. He does not have to prove his case at this stage. On the other hand, as I have said, it is not enough for a debtor merely to assert that he thinks he has a defence. He has to produce some tangible evidence in support, though it need not be all his evidence that he would adduce if there was a trial, nor even need he raise all the possible defences open to him."*

The early decisions of the BVI court echo the position in the E&W cases. The leading case is ***Sparkasse Bregenz Bank AG and in the Matter of Associated Capital Corporation*** **BVIHCMAP 2002/0010**, in which the then Chief Justice said:

"the dispute must be genuine in both a subjective and objective sense… the reason for not paying the debt must be honestly believed to exist and must be based on substantial or reasonable grounds. Substantial means having substance and not frivolous, which disputes the Court should ignore. There must be so much doubt and question about the liability to pay the debt that the Court sees that there is a question to be decided. The onus is on the company to bring forward a prima facie case which satisfies the Court that there is something which ought to be tried."

Developments in BVI Case Law

Between 2009 and 2011, the BVI court confronted the question of the extent to which it should evaluate a dispute when there was an arbitration or jurisdiction agreement. In ***Pioneer Freight Futures Co Ltd v Worldlink Shipping Ltd Samoa*** **BVIHCV 2009/0135 and BVIHCV 2009/0152,** Bannister J's finding was that, where the court reaches the point where it recognizes the existence of any dispute, it should not even attempt to decide whether or not that dispute is in itself a substantial one.

This position was at odds with the language of s. 157. The statute requires the dispute to be 'substantial'. Indeed, two years later in ***De Wet v Vascon Trading Limited*** **BVIHC (COM) 2011/0129**, Bannister J reconsidered the position in ***Pioneer***. He held that, while ***Pioneer*** was rightly decided on its facts, he had erred by misinterpreting ***Sparkasse***. On considering the E&W Court of Appeal decision of ***BST Properties v Reorg Apport Penzugyi RT [*****2001] EWCA Civ 1997**

he agreed that:

> *"….[an] exclusive jurisdiction clause was irrelevant to the question whether the debt was bona fide disputed on substantial grounds. Only if a substantial dispute is identified will the exclusive jurisdiction clause fall to be taken into account."*

Divergence in BVI and E&W case law: *Salford Estates* and *Jinpeng Group*

Following these BVI cases there has been a recent and marked divergence between the BVI and E&W Courts of Appeal. The question each has been asked is: what difference, if any, does a jurisdiction or arbitration clause make?

The E&W Court of Appeal's Answer

In ***Salford Estates (No. 2) Limited v Altomart Limited* [2014] EWCA 1575 Civ** the E&W Court of Appeal held that:

> *"It would be anomalous… to conduct a summary judgment type analysis of liability for an unadmitted debt… when the creditor has agreed to refer any dispute relating to the debt to arbitration."*

The court went on to say that to do otherwise would:

> "*…encourage parties to an arbitration agreement – as a standard tactic – to by-pass the arbitration agreement…by presenting a winding-up petition. The way would be left open to one party, through the Draconian threat of liquidation, to apply pressure on the alleged debtor to pay up immediately or face the burden, often at short notice on an application to restrain a petition or advertisement of a winding-up petition, of satisfying the Companies Court that the debt is bona fide disputed on substantial grounds.*
>
> *It is entirely appropriate that the court should, save in wholly exceptional circumstances, which I presently find difficulty to envisage, exercise its discretion consistently with the legislative policy embodied in the 1996 [Arbitration]* Act."

Importantly, the above was so even where – as with ***Salford Estates*** itself - the court is of the view that the dispute raised is not a substantial or *bona fide* one.

The BVI Court of Appeal's Answer

In two recent decisions of the Court of Appeal in the BVI, the contrary approach has been taken and is now settled law.

***C-Mobile Services Limited v Huawei Technologies Co. Limited* BVIHCMAP 2014/0017** concerned an application to set aside a statutory demand. In considering a submission that an arbitration

clause was relevant to the exercise of the Court's discretion, the Chief Justice observed:

> "*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…*"

Jinpeng Group Limited v Peak Hotels and Resorts Limited **BVIHCMAP 2014/0025 and BVIHCMAP 2015/0003** was an appeal from a refusal to appoint liquidators in a case where there was an alleged dispute said to be covered by an arbitration agreement.

In granting the appeal and appointing liquidators, the Court of Appeal expressly rejected the conclusion reached in ***Salford Estates*** and reinforced the critical task of considering whether or not there is a substantial and *bona fide* dispute, regardless of an arbitration or jurisdiction clause:

> "*[The Court of Appeal in E&W] is saying in very clear terms that a winding up application based on a debt that is covered by an arbitration agreement will be stayed unless there are exceptional circumstances. However, I do not think that a creditor should have to prove exceptional circumstances. This Court's judgment in the* ***C-Mobile*** *case sets out and distinguishes the BVI court's statutory jurisdiction to wind up a company based on its inability to pay its debts as they fall due unless the debt is disputed on genuine and substantial grounds.* ***This principle is too firmly a part of BVI law to now require a creditor exercising the statutory right belonging to all the creditors of the company to apply to wind up the company, to prove exceptional circumstances to establish his status to apply***." [Emphasis added.]

Conclusion

Far from the position of a creditor in E&W having to prove exceptional circumstances, the Court in the BVI will always assess whether or not there is a substantial and *bona fide* dispute.

Any uncertainty in the BVI created by the change in position between the first instance decisions in ***Pioneer*** and then ***De Wet*** has been settled, and the Court of Appeal decisions in ***C-Mobile*** and ***Jinpeng*** are being applied in the Commercial Court in favour of the creditor.

Given the propensity of desperate debtors to manufacture alleged disputes, the restraint on the exercise of the E&W Court's discretion imposed by ***Salford Estates*** – requiring there to be exceptional circumstances – is perhaps surprising. A BVI debtor who happens to have an arbitration or jurisdiction agreement will have to do more than merely deny the debt to avoid liquidation.

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Key Contacts

Brian Lacy

Partner

British Virgin Islands

Jersey

E: brian.lacy@ogier.com

T: +44 1534 514493

Nicholas Brookes

Partner

British Virgin Islands

E: nicholas.brookes@ogier.com

T: +1 284 852 7366

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