Winding up and arbitration clauses: a timely reminder that he who hesitates is lost

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In *Sian Participation Corp. (In Liquidation) –v- Halimeda International Limited BVIHCMAP2021/0017*[1] ("Sian"), the Eastern Caribbean Court of Appeal again had occasion to consider (amongst a number of other things) the interrelationship between an arbitration clause in a loan agreement and the Court's jurisdiction to appoint liquidators to a company under the Insolvency Act 2003. The judgment, in which the Court of Appeal upheld the Order of Wallbank J appointing liquidators, serves as a useful reminder that a party wishing to invoke an arbitration clause as a basis for a stay of winding up proceedings against it, must act promptly in inviting the Court to refer the dispute to arbitration or risk losing the opportunity.

Background

The creditor, Halimeda International Limited (the "Creditor") applied for the winding up of Sian Participation Corp. (the "Company"), on the grounds of insolvency. The debt arose under a loan agreement made between the Creditor and the Company on 7th December 2012 (the "Loan Agreement"). The Loan Agreement contained an arbitration clause (the "Arbitration Clause") which required any dispute arising from the Loan Agreement to be resolved through arbitration. The loan fell due for repayment by 31st December 2018 but the Company did not repay the debt. The Creditor filed its application on 29th September 2020. On 27th November 2020, the Company filed a Notice of Opposition denying that the debt was currently due and payable. That Notice of Opposition was amended on 19th and 23rd March 2021, but, as originally filed, made no reference to the Arbitration Clause or any reference to arbitration. On 30th January 2021, the company filed an application to strike out the winding up application. It was in this application that arbitration was first advanced as an issue. Neither party made a formal request to the Court that it refer the matter to arbitration.

Judgment at first instance

At first instance, the Judge (the Hon. Gerhard Wallbank (Ag.)), found that: (i) the Company had raised the arbitration point too late, (ii) as a matter of BVI law, the mere existence of an arbitration agreement does not preclude a creditor from applying for a winding up order, and (iii) there is no mandatory stay of liquidation proceedings in favour of arbitration. The Judge appointed liquidators to the Company.

The Appeal

The Company appealed. There were five main issues which fell for determination on the appeal, the first of which concerned the effect of the Arbitration Clause.

The Company's position was that the Judge had erred in law in applying the wrong test in assessing the liquidation application in the face of an arbitration agreement and erred in law and in the exercise of his discretion by concluding that the arbitration point was raised too late and was not available as a defence because the Company had not commenced an arbitration.

The Company initially contended, in reliance on *Salford Estates (No 2) Ltd v Altomart Ltd (No 2)*[2] , that the *Sparkasse test*[3] had no utility in liquidation proceedings involving disputes falling within the scope of an arbitration agreement. However, the Company subsequently abandoned that position

[1] November 11 2022, https://www.eccourts.org/sian-participation-corp-in-liquidation-v-halimeda-international-limited
[2] [2015] Ch 589.

and accepted that, while that is the law in England, in the BVI it is now settled that the statutory jurisdiction to make a liquidation order on a creditor's application under section 162(1) of the Act is satisfied if the debt is not disputed on genuine and substantial grounds, without the necessity of proving exceptional circumstances. In such cases, a debtor is not entitled to an automatic stay of the liquidation proceedings under section 18(1) of the Arbitration Act merely by invoking the existence of an arbitration agreement. In the BVI, *Jinpeng Group Limited v Peak Hotels and Resorts Limited*[4] is authority for the proposition that proceedings by way of a creditor's winding-up application, are not covered by arbitration agreements or by section 18(1) of the Arbitration Act[5] but, rather, become an issue between the debtor and its creditors as a class over the debtor's inability to pay its debts as they fall due.

The Company also sought to argue that the existence of an arbitration agreement is highly relevant to the court's determination. It cited in support *Rangecroft Ltd v Lenox International Holdings Ltd*[6], *IS Investment Fund Segregated Portfolio Company v Fair Cheerful Ltd*[7] *and A Creditor v Anonymous Company Ltd*[8]. However, although the Court of Appeal accepted it as self-evident that an arbitration agreement would be relevant to a court's consideration of a liquidation application, because this contention had not been included in the grounds of appeal, the Court was not prepared to entertain it. Similarly, the Court of Appeal declined to consider an argument advanced in submissions but not included in the Notice of Appeal, that if a creditor fails without good reason to serve a statutory demand thereby depriving the company of its absolute right to a stay under section 18 of the Arbitration Act, it would be inappropriate for the court to assess the merits of the defence for the purposes of Sparkasse.

BVI law

On the question of timing, section 18 of the BVI Arbitration Act introduces into BVI law the provisions of Article 8 of the UNCITRAL Model Law. Article 8(1) of the Model Law requires a court to refer a dispute to arbitration if one party so requests "*not later than when submitting his first statement on the substance of the dispute*"[9] . This provision requires the Court to refer to arbitration disputes that are the subject of an arbitration agreement provided that a request for such referral is made in the respondent's first statement to the Court on the substance of the dispute.

Also relevant in the context of an application to wind up is rule 164 of the *BVI Insolvency Rules*[10] (the "Insolvency Rules") which requires a company wishing to oppose an application to wind it up to file and serve a notice setting out the grounds on which it opposes that application not later than 7 days before the date fixed for the hearing of the application supported by evidence in support.

Court of Appeal's decision

The Court of Appeal interpreted these two provisions, read together, as meaning that a company which is faced with an application to wind it up in a matter that is the subject of a valid and operative arbitration agreement, must file and serve a request for referral to arbitration not later than when submitting its first statement on the substance of the dispute. After the first statement is filed, the Court of Appeal held, this stipulation becomes a discretion, to be exercised under the over-arching umbrella of fairness and just disposition, important components of which include consideration of all relevant factors such as the timing of the request.

In the present case, however, the Company's first substantial statement to the court regarding the dispute was the Notice of Opposition filed on 27 November 2020. However, not only was the Notice of Opposition filed after the time limit prescribed by rule 164, but it did not raise the issue of arbitration. Arbitration was first advanced by the Company as an issue on 1st February 2021, when the Company filed a Notice of Application to Strike out the winding up application. In fact, the Company did not raise the arbitration issue as grounds on which it opposed the winding up application until late March 2021, when it filed an Amended Notice of Opposition, well outside the time stipulated in rule 165 of the Insolvency Rules.

In the circumstances, the Court of Appeal was entirely satisfied that judge's determination that the issue of arbitration was raised late and was thereby invalid, was unassailable and supported by the legal provisions underpinning the automatic referral mandate in section 18(1) the Arbitration Act.

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[3] *Sparkasse Bregenz Bank AG v In the Matter of Associated Capital Corporation BVIHCVAP2002/0010* (delivered 18th June 2003, unreported). The *Sparkasse test* requires that the dispute raised by the company must be substantial and genuine in both a subjective and objective sense, which means that 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.

[4] Ibid. fn4.

[5] Act No. 13 of 2013, Laws of the Virgin Islands.

[6] BVIHC (COM) 2020/0037 6th July 2020, unreported.

[7] BVIHC (COM) 2020/0034 16th July 2020, unreported.

[8] 28th January 2021, unreported

[9] "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 that 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." (Emphasis added)

[10] S.I. No. 45 of 2005, Laws of the Virgin Islands.

Accordingly, and since the Company had not identified any relevant factors to which the judge attributed either too much or too little weight, or any irrelevant factors he took into account which might have rendered his decision blatantly wrong and outside the ambit of reasonable disagreement, the Court of Appeal concluded that the Judge did not err in law or in the exercise of his discretion and dismissed the Company's appeal in so far as it relied on the existence of the Arbitration Clause as grounds to displace the Judge's conclusion.

No need to commence an arbitration

The Court of Appeal also considered an argument, which the Company had made, suggesting that the Judge had held that the Company had to initiate an arbitration in order to invoke the arbitration clause in the present proceedings. The Court of Appeal held that this was a misinterpretation of the Judge's words. Rather, the Judge had simply highlighted the obvious point that, on the one hand, the Company is pressing the arbitration avenue as one which the Court should enforce by referral pursuant to Article 8(1) of the Model law, whilst on the other, it had deliberately and intentionally elected to forgo arbitration in respect of its cross-claim against the Creditor, when it was open to it to pursue that course. This inconsistency undermined the Company's belated entreaty for referral to arbitration in respect of the liquidation proceedings such that the Company's contention that the Judge erred in law in this regard was also without merit.

Lessons to be learnt

The obvious lessons to be learnt from Sian for a BVI company, served with an application to wind it up, which wishes to rely on arbitration clause as grounds to dismiss the application, is that it must formally request that the Court refer the dispute to arbitration and that it must act promptly in so doing. It should do so at the first possible opportunity and no later than "*when submitting [its] first statement on the substance of the dispute*" that is, usually, its Notice of Opposition. Although it is not the case that a company must have initiated an arbitration before it can rely on an arbitration clause, and the Court of Appeal confirms that to be the case in *Sian*, in order to avoid any suggestion that its wish to arbitrate is less than genuine, the company is also likely to be best advised actually to commence an arbitration within which its dispute can be resolved.

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