BVI Arbitration Group in collaboration with BVI IAC

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Arbitration & Insolvency Wars Post *Lenox v Rangecroft*:

A New Hope or a Phantom of Menace?

On 5 March 2021 the BVI IAC Arbitration Group held a webinar to discuss issues that arise in insolvency proceedings when the agreement that gives rise to the debt contains an arbitration clause. The panel brought together practitioners and academics with different points of views and from different backgrounds: **Arabella di Iorio**, a BVI legal practitioner and a partner at Agon Litigation, **John Rooney, Jr., Esq.**, an arbitrator, a practitioner and an academic teaching arbitration law at the Miami School of Law, **David Alexander QC**, a barrister at the South Square, and **Andrew Willins**, a BVI legal practitioner and a partner at Appleby. The discussion was moderated by **Jane Fedotova** from Conyers. The webinar attracted attendance of practitioners from 32 countries which clearly demonstrates that the topic is live and relevant to the worldwide international arbitration community.

New Case Law

The discussion focused on the BVI Commercial Court decisions of Mr Justice Jack in *Lenox v Rangecroft*[1], *IS Investment Fund Segregated Portfolio Company v Fair Cheerful*[2] and the anonymised decision in *A Creditor v Anonymous Company Ltd*[3].

In all three cases the judge considered whether, in circumstances where the debt is disputed, the question whether that dispute is *bona fide* and on substantial grounds (the *Sparkasse v Bregenz*[4] test) should be referred to an arbitrator in accordance with the parties' agreement to arbitrate any dispute arising out of a contract.

BVI law on this point appeared to be settled and was most clearly explained in the decision of the Eastern Caribbean Court of Appeal in *Jinpeng Group Limited v Peak Hotels and Resorts Limited*[5]. The Court of Appeal held that although the winding up court had no jurisdiction to

[1] BVIHC(COM) 2020/0037
[2] BVIHC(COM) 2020/0034
[3] BVIHC(COM) [redacted]
[4] BVIHCVAP 2010/0010 *Sparkasse Bregenz Bank AG v In the Matter of Associated Capital Operation*
[5] BVIHCMAP2014/0025 & BVIHCMAP2015/0003

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resolve a dispute about a debt on a summary basis, it had a duty to carry out a preliminary investigation of the facts to determine whether the dispute was raised on genuine and substantial grounds. The Court of Appeal explained that once the creditor submitted a winding up petition in respect of a debt that had arisen under a contract containing an arbitration clause the dispute was no longer between creditor and debtor, rather it was a dispute between the company and its creditors. The Court followed the English Court of Appeal authority of *Salford Estates (No 2) Ltd v Altomart Ltd (No 2)*[6] in concluding that such a dispute was not covered by the arbitration clause and that section 18(1) of the BVI Arbitration Act 2013[7] which mandates a stay of court proceedings where there is an arbitration agreement was of no relevance.

In the first of his three decisions, *Lenox v Rangecroft,* Jack J sought to distinguish *Jinpeng*. He did so on a number of bases. First that the creditor in *Lenox* had not served a statutory demand before issuing its winding up application. The Judge noted that although there is no obligation to serve a statutory demand, that is not something the court encourages, save in appropriate cases, and that no good reason for not serving a statutory demand had been given. Since no statutory demand had been served, the debtor had not had the opportunity of applying to set the demand aside, an application which would have involved the mandatory stay provisions in the BVI Arbitration Act. The second point of distinction was that the debtor had only one creditor, such that the weight to be attached to the collective nature of the remedy was comparatively low.

IS Investment Fund Segregated Portfolio Company v Fair Cheerful was also a case in which no statutory demand had been served. The Judge repeated his view that not issuing a statutory demand meant that the creditor was potentially interfering with the debtor's rights to have disputes referred to arbitration, and that no proper reason for not serving a demand had been given. Yet again there was no evidence of there being any other creditors.

[6] [2015] 1 Ch 589
[7] Equivalent to section 9(4) of the Arbitration Act 1996

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The trilogy of cases is completed by *A Creditor v Anonymous Company Ltd*. There the Judge accepted that insofar as his earlier decision in Lennox had suggested that following service of a statutory demand, an automatic stay would follow, that arguably overstated the position in light of the decision in *C Mobile v. Huawei Technologies (Statutory Demand) 2015 BVIHCMAP 2014/0006*. The Judge reserved for another case the question of whether or not C Mobile should be confined to a case decided under the Arbitration Act 1976, rather than the Arbitration Act 2013.

The Judge conducted a review of all of the major authorities decided in this area, and noted that each of them emphasized the Court's discretion to stay winding up proceedings for arbitration. The Judge held that where there are no other creditors, it would (as a general rule) undermine the policy in the Arbitration Act 2003 if the Court were to apply the *Sparkasse v. Bregenz* test. However, that discretion was not to be exercised blindly: the Court should nevertheless still examine whether the proposed defence was being advanced by the debtor with a real belief in its substance. Applying that principle, the Judge concluded that the defence had no substance, was simply a "put-up job". In those circumstances, the discretion fell to be exercised in favour of the creditor.

Panel Discussion

The decisions created some controversy among the BVI legal community and the goal of the webinar was to discuss the issues that were raised by that judgment.

<u>The need for a statutory demand</u>

There is no authority for the view that a statutory demand ought to be served save in appropriate cases or if it is not, an explanation given. And no guidance was given as to when it might be appropriate not to serve one (for example where there is no arbitration clause in the underlying agreement). Practitioners will no doubt take the safer course of serving a statutory demand, even in circumstances where they might previously not have done so. There is therefore a need to clarify this issue.

<u>The approach in Jinpeng</u>

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It was argued that the decisions are contrary to the long standing Court of Appeal authority in *Jinpeng* which confirmed that the court has jurisdiction to conduct a preliminary investigation of the facts in order to determine whether there is a *bona fide* dispute. Attempts to distinguish *Jinpeng* on the basis that there the application to wind up was made on the just and equitable ground and that there was an urgent need to protect the creditors were not seen as particularly convincing. Concerns were also voiced that such a sudden change of position may in fact not promote arbitration but encourage parties, particularly lenders or those in a stronger negotiating position, to insert an exclusive jurisdiction clause in favour of the courts. Arbitrations nowadays are expensive and rarely swift. Why would a creditor agree to an arbitration clause if otherwise the creditor could get a swift decision from the Court without exposing itself to expensive costs and delay?

Should an enforcement order be a pre-requisite to winding up?

One of the panelists raised the concern that the Court's practice was to sidestep the formal enforcement procedure for an arbitral award, where the award gives rise to a debt[8]. It was suggested that the Court should as a minimum recognise an arbitral award and thereby apply a checklist of defences set out in Article 2 of the New York Convention before proceeding to a conclusion that the debt is not disputed on genuine and substantial grounds. It was suggested that such checklist could be incorporated in the BVI insolvency law. The Court's rationale is of course that seeking to appoint liquidators is not an enforcement process but a collective remedy, and the Court has acknowledged that if any Convention grounds of opposition were reasonably arguable it would dismiss the winding up application and leave the creditor to register the judgment in the usual way. This was not a view accepted by all panelists; in particular, Section 84(1) of the Arbitration Act 2003 provides that a Convention Award is enforceable either by invoking the formal enforcement procedure "or by instituting an action in the Court." It was also noted that the invocation of the class remedy is not typically treated as "enforcement" for these purposes.

[8] See for example BVIHC(COM) 2019/0149 *Daselina Investments Ltd v Kirkland Intertrade Corp*; BVIHC(COM) 2018/231 & BVIHC(COM) 2018/230 *Donna Union Foundation v Koshigi Limited & Svoboda Corporation Limited*

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Take-Away Message

Although the current case law creates some uncertainty, since the Court did recognize that there might be circumstances when the defence is so hopeless that it would be a waste of petitioners resources and time to refer the dispute to arbitration, perhaps the landscape has not changed so much after all.

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