5-Bench Court of Appeal clarifies interplay between winding-up proceedings & arbitration

***AnAn Group (Singapore) Pte Ltd v VTB Bank (Public Joint Stock Company)* [2020] SGCA 33 ("*AnAn*")**

In recent years, creditors have been exploring avenues to avoid arbitration proceedings, partly due to the growing concerns over the associated time and costs.

One oft-seen approach is the commencement of winding-up proceedings by creditors. There have been occasions where this has been done by a creditor seeking to pressure a debtor into settling the dispute, in order to avoid facing a potential winding up. This has made the winding-up regime vulnerable to abuse by creditors in situations where an arbitration agreement rightfully governs the dispute between the parties.

In a bid to stem such abuse, and regulate the interplay of arbitration and court-based insolvency proceedings, a 5-bench Singapore Court of Appeal ("**CA**") has now clarified the applicable standard of review when a winding-up court is asked to determine whether there is a *bona fide* disputed debt that falls within the scope the arbitration agreement.

This update sets out the salient learning points arising from the case of *AnAn*.

Brief Facts

In *AnAn*, the creditor served a statutory demand for the sum of approximately US$170 million on the debtor.

After the 3-week statutory period expired, and the debtor failed to repay the debt, the creditor commenced winding-up proceedings in the Singapore courts. The contract between the parties contained an arbitration agreement providing for disputes to be resolved in accordance with the arbitration rules of the Singapore International Arbitration Centre.

The debtor sought to resist the winding up hearing by disputing the debt.

The debtor argued that because the contract contained an arbitration agreement, the applicable standard was to demonstrate a *prima facie* dispute which fell within the scope of that arbitration agreement.

The creditor argued to the contrary: that the debtor was required to establish triable issues in relation to the debt and that this is an exacting standard which requires a thorough examination of the evidence.

The High Court's Decision

In the court below, the High Court judge reluctantly held that the standard of review that a debtor had to meet when disputing a debt was that a triable issue had to be shown, as he considered himself bound by a previous decision in *Metalform Asia Pte Ltd v Holland Leedon Pte Ltd* [2007] 2 SLR(R) 268 ("**Metalform**").

However, the judge observed in obiter that if he was not bound, he would have preferred the *prima facie* dispute standard as the higher triable issue standard invariably necessitated a consideration of the merits of the disputed debt, thereby allowing parties to circumvent their arbitration agreement by presenting a winding-up application. The judge held that adopting the lower standard of review when the debt is subject to an arbitration clause would align with the judicial policy of facilitating and promoting arbitration.

The CA's Decision

The CA sympathized with difficulty of the court below and held that that when a court is faced with either a disputed debt or a cross-claim that is subject to an arbitration agreement, the prima facie standard should apply, such that the winding-up proceedings will be stayed or dismissed as long as:

(a) there is a valid arbitration agreement between the parties; and

(b) the dispute falls within of the arbitration agreement, provided that the dispute is not being raised by the debtor in abuse of the court's process.

The CA's analysis was as follows.

First, the CA distinguished *Metalform* by holding that the significance of the arbitration clause was not directly engaged in that case. No arguments were raised by parties regarding whether the applicable standard of review ought to be the same as that applicable for disputes (in a non-insolvency context) subject to arbitration.

Second, the CA affirmed the decisions of Aedit Abdullah JC (as he was then) in *BDG v BDH* [2016] 5 SLR 977 ("**BDG**") and Valerie Thean J in *BWF v BWG* [2019] SGHC 81 ("**BWF**"). The two cases stood for the following propositions:

- The objective of the triable issue standard (in non-arbitration cases) is to ensure that winding-up is not staved off on flimsy or tenuous grounds. This ensures that remedies are readily obtained when nothing much can be said against the claim or application. This helps to oil the machinery of commerce and trade, and helps promote certainty and efficiency.

- However, this objective is less pressing and dominant when one is confronted with an arbitration clause as the countervailing concern is to hold parties to their agreement. The lower standard coheres with the importance of party autonomy in the field of arbitration.

- It may be that the debtor's case is weak, and would be readily dismissed by the arbitrators; but such weakness of the case would be a matter for the arbitration tribunal to decide. The court should not generally step in, even if the arbitration may lead to a different result from the court's assessment.

- There is also the desirability of achieving coherence in the law, by aligning the law governing exclusive jurisdiction clauses, *forum non conveniens*, and stay applications under the International Arbitration Act ("**IAA**"). Across these areas, the merits of the defence are irrelevant to the issue of whether a stay ought to be granted.

Finally, the CA explained why the lower standard promotes coherence in the law, gives effect to the principle of party autonomy and helps to achieve cost savings and certainty in the law:

- Given that the prima facie standard has been adopted by the courts for stay applications under both the Arbitration Act and IAA, there is no principled basis to apply differing standards to what is essentially the same disputed debt. If the standards were different, then the creditor would be free to make a tactical decision – by pursuing an ordinary claim for debt, the *prima facie* standard would apply; on the other hand, if the creditor applies, on the basis of the same disputed debt, for the debtor to be wound up, the higher triable issue standard would apply. This would in turn encourage the abuse of the winding-up jurisdiction of the court, which is not the appropriate forum to adjudicate on disputed claims that are subject to arbitration.

- As a matter of principle, in an application to stay or dismiss a winding-up application on the ground that the dispute involving *pre-insolvency* rights and obligations ought to be determined by arbitration, the policies underpinning the arbitration and insolvency regime are not at odds. A statutory demand that is unsatisfied merely leads to the *presumption* that the debtor is insolvent; it does not determine that the debtor is in fact insolvent. Hence, when a dispute arises in relation to a pre-insolvency debt that is subject to an arbitration agreement, the policy concerns of the insolvency regime are not engaged. It is only when the debt is established to be due and owing by arbitration, and that debt remains unsatisfied, that it can be said that the company is insolvent. In other words, the arbitration of the dispute is a necessary precondition to

bringing the insolvency regime into the equation.

- By adopting the *prima facie* standard, parties will be discouraged from abusing the court's winding up jurisdiction as a means to avoid the parties' agreed method of dispute resolution. After all, the presenting of winding petitions can as a matter of practical reality put considerable pressure on the debtor to pay in lieu of arbitration, given the risk of reputational damage to the debtor arising from the commencement of the winding up process. To that extent, there is a risk of debtors being strong-armed into settling disputes.

- If the court adopts the triable issue standard, and winds up the debtor-company on the basis that its defences are unmeritorious, the court in effect takes the place of the arbitral tribunal, against the parties' agreement, thereby eroding any of the advantages which they sought to obtain in electing arbitration in place of other modes of dispute resolution (e.g. finality, confidentiality, ease of enforcement). Substantive prejudice may be caused to the parties if their choice of dispute resolution is not strictly adhered to, especially since arbitration may lead to a different result from the court's assessment. The debtor may lose any procedural advantages which he may otherwise have if the matter is determined by the courts.

- Ultimately, parties should be held to their bargains. There is no principled reason to depart from this settled position merely because the creditor elects to pursue his claim by way of a winding-up application.

Other observations

To check against potential abuses of the *prima facie* standard of review, the CA also made it clear that there is no question of an *automatic* stay. The *bona fides* of the debtor in raising the dispute remains a relevant factor in determining whether there has been an abuse of process in attempting to obtain the stay or dismissal of the winding up application. Examples where abuse may be found include:

- where the debt has been admitted as regards both liability and quantum;

- where the debtor has waived or may be estopped from asserting his rights to insist on arbitration, such as where the parties have agreed subsequently that disputes may be resolved by litigation; and

- where the debtor is seeking to stave off substantiated concerns which justify the invocation of the insolvency regime e.g. when assets have gone missing and there is an urgent need to appoint independent persons to investigate with a view of recovering the company's assets, or when there is a proper basis to conclude that there has been fraudulent preferences or the need to engage the avoidance provisions in the Bankruptcy Act.

The CA further observed that the winding up court has the discretion to stay, rather than dismiss winding up proceedings altogether, if the applicant creditor is able to demonstrate legitimate concerns about the solvency of the debtor as a going concern, and that no triable issues are raised by the debtor.

The creditor will then be given liberty to apply to court to proceed with the winding up if, for example, it can be shown that:

- the debtor has no genuine desire to arbitrate the dispute, and that it is taking active steps to stifle the arbitration; or

- when there is evidence to show that the debtor is paying off other creditors to stave off other winding-up proceedings, to the detriment of the applicant creditor, and there is no legitimate explanation for the different treatment of the creditors.

If you would like more information on this area of the law, please contact:

Nawaz Kamil
Director (Head of Restructuring & Insolvency)
(nawaz@providencelawasia.com)

Nawaz is an insolvency expert who has handled corporate restructuring and insolvency matters for more than a decade. At Providence Law, Nawaz continues to handle many high-profile and high-value cases, such as acting for the liquidators from Ernst & Young with respect to a joint venture company with assets over S$100 million and the liquidators of Six Capital Investments Limited, a BVI company with over US$143 million in debt.

Danny Quah
Counsel
(danny@providencelawasia.com)

Danny is a commercial litigator with a unique niche in tax disputes and a growing practice in insolvency & civil fraud matters. He was recently recognised as an up-and-coming litigator by the Singapore Academy of Law and has completed attachments with UK "magic circle" barrister sets Fountain Court Chambers and Pump Court Tax Chambers.