

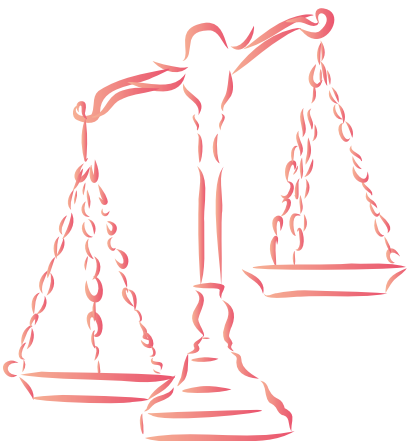
TO STAY OR NOT TO STAY

RE LAM KWOK HUNG GUY (2023) 26 HKCFAR 119, [2023] HKCFA 9 AND THE ENGLISH APPROACH TO (NOT) STAYING PETITIONS PRESENTED DESPITE EXCLUSIVE JURISDICTION CLAUSE (“EJC”)

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Introduction

How should the English Courts decide a bankruptcy or winding-up petition based on a disputed debt which is contractually subject to resolution in another forum? Does it matter if that forum is arbitration or a foreign court? This article reviews – and exposes the diametric contradistinction between – the current respective legal positions vis-à-vis the two fora, expressing the hope that they will be harmonised in due course.



Arbitration Clause: Salford Estates (No 2) Ltd v Altomart Ltd (No 2) [2015] Ch 589 (CA)

Starting with arbitration, Salford concerned a winding-up petition presented despite an arbitration clause. Although the petition was based on an arbitral award, the debtor company contended that the outstanding amount was disputed and had to be referred to arbitration. The English Court of Appeal (“CA”) discretionarily stayed the petition under section 122(1)(f) of the Insolvency Act 1986 so as to compel the parties to resolve their dispute by arbitration, holding (at [40]) that, otherwise:

“[It] would inevitably encourage parties to an arbitration agreement—as a standard tactic—to bypass the arbitration agreement and the 1996 Act 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 presentation or advertisement of a winding up petition, of satisfying the Companies Court that the

debt is bona fide disputed on substantial grounds. That would be entirely contrary to the parties’ agreement as to the proper forum for the resolution of such an issue and to the legislative policy of the 1996 Act.”



EJC: Guy Lam

What about EJCs? The latest Hong Kong Court of Final Appeal (“CFA”) case of Guy Lam involved an EJC contained in a Credit and Guaranty Agreement, in the New York courts’ favour. Under the Agreement, the creditor T would advance loans to a company C, and the debtor G agreed to guarantee the full payment of all amounts due. T petitioned for G’s bankruptcy in Hong

Kong on the outstanding debt owed by C, while he commenced proceedings in New York against it, claiming that there had been no event of default, under the Agreement.

The CFA held that:

- **The Hong Kong Court, like the English Court in Salford, could discretionarily refuse to determine whether the debt was bona fide disputed on substantial grounds, taking into account (inter alia) the EJC ([100]–[101]):**

“... A circumstance enlivening that discretion is the fact that the parties agreed to have all their disputes under the agreement giving rise to the debt be determined exclusively in another forum.

It is at this stage that the public policy interest in holding parties to their agreements comes into play. It is not the only consideration. The public policy underpinning the legislative scheme of the court’s bankruptcy jurisdiction is still present. The more obviously insubstantial the grounds for disputing the debt, the more it comes into prominence.”

- **The Court further clarified (at [104]–[105]) that:**

“The above approach to the exercise of the discretion to decline jurisdiction... is in some sense multi-factorial....

It is clear... that the so-called ‘Established Approach’ [namely, absent the EJC or an arbitration provision, a petitioner will ordinarily be entitled to a bankruptcy / winding-up order if the petition debt is not subject to a bona fide dispute on substantial grounds] is not appropriate where an EJC is involved. And in the ordinary case of an EJC, absent countervailing factors such as the risk of insolvency affecting third parties and a dispute that borders on the frivolous or abuse of process, the petitioner and the debtor ought to be held to their contract.”

Therefore, Hong Kong’s apex Court adopted, in the EJC’s context, a discretionary approach similar to Salford in the arbitration provision’s context, although it also highlighted its multi-factorial character, particularly embracing the fundamental policy underlying the legislative scheme of the Court’s bankruptcy jurisdiction, as well as the seriousness of the debtor’s grounds for disputing the petition debt.



Post-Guy Lam: What Now for England?

Thus considered, would England follow Guy Lam, which, after all, is consistent with Salford, for cases with an EJC? The author would hope so; there is only one problem: contrary binding English CA authority exists. In *BST Properties Ltd v Reorg-Apport Penzugyi RT* [2001] EWCA Civ 1997, a two-judge CA held (at [31]) that “whether or not proceedings raising a dispute as to the effect of the loan agreement could be stayed on the basis of clause 18 [an EJC], that does not... affect the question which was facing the Companies Court, namely whether the petition debt is bona fide disputed on substantial grounds.” The effect of this was, as the recent decision in *City Gardens Ltd v DOK82 Ltd* [2023] EWHC 1149 (Ch) explained ([42]):

“[BST] is binding authority for the proposition that the Companies Court, in considering the exercise of its power to wind up under section 122 of the Insolvency Act 1986, is itself charged with determining whether the petitioner is genuinely a creditor. For that purpose, it has to determine whether the alleged debt is disputed in good faith on substantial grounds. Even where the alleged debt is based upon a contract which has an

[EJC] in favour of a foreign jurisdiction, the judgment as to the exercise of the winding up power remains that of the domestic court. It follows that the petition should not have been dismissed on the grounds of the existence of the [EJC]”.

This is clearly in diametric contradistinction to the Salford approach for arbitration agreements – without any apparent reason identified. Accordingly, we must await a suitable occasion for the UK Supreme Court to determine whether Guy Lam should now be followed in England instead of BST in cases involving an EJC. It is hoped that Guy Lam will prevail, thereby harmonising the approach for EJCs with the Salford approach for arbitration agreements.

