CACV 347/2023, [2024] HKCA 352
On Appeal From [2023] HKCFI 2065

IN THE HIGH COURT OF THE

HONG KONG SPECIAL ADMINISTRATIVE REGION

COURT OF APPEAL

CIVIL APPEAL NO 347 OF 2023

(ON APPEAL FROM HCCW NO 175 OF 2017)

IN THE MATTER OF Section 327 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance, Chapter 32 of the Laws of Hong Kong ("**CWUMPO**")

and

IN THE MATTER OF Shandong Chenming Paper Holdings Limited

BETWEEN

ARJOWIGGINS HKK 2 LIMITED Petitioner

and

SHANDONG CHENMING PAPER HOLDINGS LIMITED Respondent

Before: Hon Kwan VP, Barma and G Lam JJA in Court

Date of Hearing: 21 March 2024

Date of Judgment: 23 April 2024

J U D G M E N T

Hon G Lam JA (giving the Judgment of the Court):

1. In his decision dated 10 August 2023 ("**Decision**"),[1] Harris J stayed the petition presented by Arjowiggins HKK 2 Ltd ("**Petitioner**") for the winding up of Shandong Chenming Paper Holdings Ltd ("**Company**"), pending determination of an arbitration between the parties. The Petitioner appeals against this order with leave granted by the judge. The principal question arising is whether or not the approach adopted in *Re Lam Kwok Hung Guy, ex p Tor Asia Credit Master Fund LP* (2023) 26 HKCFAR 119 ("***Guy Lam***" or "***Guy Lam CFA***"), where the court dismissed a bankruptcy petition on the ground that the dispute over the petition debt should be determined in the New York court in accordance with the exclusive jurisdiction agreement between the parties, should be applied in this case where the Company has raised a cross-claim against the Petitioner which is being arbitrated pursuant to an arbitration agreement between the parties.

Background

2. The relevant factual and procedural background may be set out as follows (based in part on the account in this court's judgment of 5 August 2020 referred to below).

3. The Company is a company incorporated in Mainland China. Its shares are listed on the Shenzhen Stock Exchange, in the form

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1 [2023] HKCFI 2065.

of both A and B shares. It also has a primary listing of H shares on the Stock Exchange of Hong Kong. It is registered as a non-Hong Kong company under Part 16 of the Companies Ordinance (Cap 622). Its main businesses include paper manufacturing, forestry, finance and real estate.

4. In October 2005, the Petitioner and the Company entered into an agreement pursuant to which they established a joint venture company in the Mainland, with equity holding of 70% and 30% respectively. The joint venture agreement is governed by the laws of the People's Republic of China and contains an arbitration clause which provides:

> " 24.2.1 Any dispute arising out of or in connection with this Contract, including any question regarding its existence, validity or termination or as to rights or obligations of the Parties hereunder which is not settled by friendly discussions pursuant to Article 24.1 shall be referred to and finally resolved by arbitration in Hong Kong in accordance with the Arbitration Rules of the Hong Kong International Arbitration Centre … The arbitral award shall be final and binding on the Parties."

5. When the joint venture first started, the Petitioner, a company incorporated in Hong Kong, was wholly owned by a French conglomerate, Arjowiggins SAS, but in September 2009, ownership was transferred to Lilywoods Holdings Ltd, a BVI company owned apparently by Mr Tong Chong ("**Mr Tong**") and Mr Liu Gongting. From that time onwards, they had been the Petitioner-nominated directors of the joint venture company and, in particular, Mr Tong had been its chairman and legal representative.

6. Disputes subsequently arose between the parties, and in October 2012, pursuant to the arbitration clause in the joint venture agreement, the Petitioner commenced an arbitration against the Company, alleging that the Company was in breach of contract in failing to supply

steam to the joint venture company in accordance with the joint venture agreement. We shall refer to this as the "**first arbitration**". The arbitral tribunal rendered its award in November 2015, ordering the Company to pay damages of RMB 167,860,000 to the Petitioner. Soon afterwards, the Petitioner obtained leave (in HCCT 53/2015) to enforce the award in Hong Kong. The Company applied to set aside the award, but on 12 October 2016, this application was dismissed by Mimmie Chan J. There was no appeal against this decision.

7. On 18 October 2016, the Petitioner served a statutory demand on the Company, for (1) RMB 273,450,830.10 in respect of damages (including interest); (2) US$3,807,956.09 in respect of legal fees, costs and interest thereon; and (3) HK$3,545,075.02 in respect of fees payable to the HKIAC and the arbitral tribunal, plus interest thereon.

8. The Company did not pay any part of the amounts demanded. Instead, on 7 November 2016, it applied to Harris J for, and obtained, an injunction to prevent the Petitioner from presenting a petition to wind it up. An originating summons was issued the next day which, after amendment, sought a declaration that the Petitioner would not be able to satisfy the three threshold requirements for the Hong Kong court to exercise its jurisdiction to wind up the Company as an "unregistered company" under section 327(3) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32). These requirements are: "(1) There must be a sufficient connection with Hong Kong, but this did not necessarily have to consist in the presence of assets within the jurisdiction; (2) There must be a reasonable possibility that the winding-up order would benefit those applying for it; and (3) The court must be able to exercise jurisdiction over

one or more persons in the distribution of the company's assets." See *Shandong Chenming Paper Holdings Ltd v Arjowiggins HKK 2 Ltd* (2022) 25 HKCFAR 98 at §3.

9. Harris J dismissed the Company's originating summons on 14 June 2017, with reasons handed down on 7 July 2017,[2] holding that the second threshold requirement was met (it being common ground that the first and third requirements were satisfied). On 15 June 2017, the Petitioner presented a petition to wind up the Company on the ground that it was unable to pay its debts as it had failed to pay the sums demanded by the Petitioner. In light of the Company's appeal relating to the second threshold requirement, and upon the Company's agreement to procure payment of approximately HK$389 million into court, at the hearing of the petition on 28 August 2017 it was adjourned *sine die* with liberty to restore.

10. The Company's appeal against Harris J's decision on the question of the second threshold requirement was dismissed by the Court of Appeal on 5 August 2020,[3] and its further appeal to the Court of Final Appeal was dismissed on 14 June 2022,[4] with an order for the money in court to be paid out with interest to the Petitioner. The funds, totalling over HK$401 million with interest, were paid out to the Petitioner on 30 June 2022. A sum of over HK$53 million has however remained outstanding on the petition debt, with daily interest accruing. By summons

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2 *Shandong Chenming Paper Holdings Ltd v Arjowiggins HKK 2 Ltd* [2017] 4 HKLRD 84.

3 *Shandong Chenming Paper Holdings Ltd v Arjowiggins HKK 2 Ltd* [2020] HKCA 670.

4 *Shandong Chenming Paper Holdings Ltd v Arjowiggins HKK 2 Ltd* [2022] HKCFA 11; (2022) 25 HKCFAR 98.

dated 18 July 2022, the Petitioner applied for the petition to be restored for hearing.

11. Meanwhile, believing that the Petitioner had, through Mr Tong, withheld from the Company the books and records of the joint venture company ("**JV documents**"), the Company commenced a second set of arbitral proceedings against the Petitioner in October 2018, seeking recovery of the JV documents. We shall refer to this as the "**second arbitration**". This resulted in a Partial Final Award dated 19 May 2020 whereby the arbitrators found that the JV documents had indeed been transferred away by Mr Tong and continued to be in the Petitioner's possession through Mr Tong. The arbitrators found however that the Company itself was not entitled to obtain the JV documents which belonged to the joint venture company. By a Final Award dated 5 August 2020, the arbitrators ordered the Petitioner to deliver the JV documents to the "compulsory liquidation group" (a body constituted under PRC laws equivalent in function to liquidators under Hong Kong law) of the joint venture company.

12. The Final Award was however set aside by Mimmie Chan J on 12 January 2022, on the ground that the arbitral tribunal had exceeded its jurisdiction in the particular reference, which concerned the Company's own right to recover the JV documents, by ordering delivery instead to the liquidation group of the joint venture company.[5] Leave to appeal was refused by the judge on 24 March 2022.[6]

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5 [2022] HKCFI 128.

6 [2022] HKCFI 859.

13. In response to this development, the Company commenced a third set of arbitral proceedings against the Petitioner on 20 June 2022 ("**third arbitration**"). As set out in the amended notice of arbitration and the statement of claim, the Company seeks to (1) utilise the findings made in the second arbitration to obtain the relief in the Final Award that was set aside, i.e. delivery up of the JV documents to the liquidation group of the joint venture company; and (2) recover damages from the Petitioner in relation to, *inter alia*, six transfers of funds out of the joint venture company between June 2010 and December 2012 totalling some RMB 147.8 million. The Company claims that those transfers of funds were procured by the Petitioner but never properly approved by the joint venture company. It is said that as a result, the Petitioner was in breach of the joint venture agreement and its duties as controlling shareholder under PRC laws, with the consequence that the Company is entitled to claim damages in the amount of RMB 44.3 million representing the diminution in value caused to its 30% stake in the joint venture company, as well as interest accrued in the amount of RMB 38.1 million, totalling RMB 82.4 million (approximately HK$97.1 million). On this basis, the Company says that it has a cross-claim against the Petitioner in an amount exceeding the remainder of the petition debt.

14. On 25 October 2022, the Company issued a summons seeking an order that the petition be dismissed, or adjourned pending the third arbitration. Having heard the parties in July 2023 after the Court of Final Appeal gave its judgment in *Guy Lam* on 4 May 2023, Harris J issued his Decision ordering that the petition be stayed pending determination of the

third arbitration. The judge granted the Petitioner leave to appeal on 25 October 2023.[7]

15. The third arbitration has progressed and we are told that the substantive hearing will take place in May 2024. Given this it is not clear what practical purpose this appeal serves. The notice of appeal seeks an order that the Company's summons be dismissed, with the result, it seems, that the petition will simply proceed in the Court of First Instance. At the hearing, however, Mr Laurence Li SC, appearing on behalf of the Petitioner, said even if the appeal is allowed, the Petitioner will not ask the Court of First Instance to determine whether the Company has a cross-claim of substance, presumably because by then the cross-claim will either be being heard by the arbitrators or will have already been determined by them. Nevertheless, Mr Victor Joffe SC, appearing for the Company, has not suggested the appeal is academic, and we shall adjudicate on it accordingly.

The decisions in Guy Lam

16. In *Guy Lam*, a Hong Kong resident, Lam, was the founder of certain companies providing aged care services in Mainland China and the United States. He had given a personal guarantee for loans extended by a lender, Tor, to a company in his group. Tor alleged that the borrower company had defaulted on the loans and presented a petition in Hong Kong for a bankruptcy order against Lam based on his guarantee. The parties' agreement contained an exclusive jurisdiction clause in favour of the courts of New York, pursuant to which Lam brought an action in New York against Tor, whilst the petition was pending in Hong Kong. In that action

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7 [2023] HKCFI 2731.

Lam complained that he was not given notice of any event of default prior to the enforcement actions taken by Tor, and alleged that no extant default could be relied on by Tor because of waiver or estoppel. He claimed that Tor took the enforcement actions in bad faith and conspired with one or more of his employees to facilitate the wrongful takeover of the companies in violation of their fiduciary duties. By way of relief Lam sought, *inter alia*, declarations that no event of default existed that had not been waived, and that Tor was not entitled to replace the existing managers and directors of the group companies; an injunction to prevent Tor from taking any action in breach of its contractual duties under the agreement; and damages for breach of the covenant of good faith and fair dealing.[8]

17. In the proceedings in Hong Kong, the judge at first instance made a bankruptcy order against Lam. On appeal, this court[9] unanimously allowed the appeal and dismissed Tor's petition, holding (by a majority in reasoning) that where the petition debt is disputed and the dispute is subject to an exclusive jurisdiction agreement between the parties in favour of another forum, the petition should not be allowed to proceed, in the absence of strong reasons, pending the determination of the dispute in the agreed forum. See *Re Lam Kwok Hung Guy, ex p Tor Asia Credit Master Fund LP* [2022] 4 HKLRD 793 at §86 ("***Guy Lam CA***").

18. The Court of Final Appeal dismissed Tor's appeal against the Court of Appeal's decision. Giving the principal judgment with which the other members of the court agreed, French NPJ said:

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8 See Guy Lam CFA §§17-18.

9 Barma, G Lam and Chow JJA.

" 97. The determination by the court of whether it is satisfied with the proof of the petitioning creditor's debt is an exercise of the court's bankruptcy jurisdiction. So is the determination whether there is a bona fide dispute about the debt on substantial grounds. And so too, is the decision by the court to grant, dismiss or stay the petition.

98. Although the determination of whether the debt is bona fide disputed on substantial grounds is an element of the jurisdiction conferred on the court, it is a threshold question. If the debt is disputed in a petition, then the engagement of the bankruptcy process in that case is on hold – for the rationale, referred to in the Appellant's public policy arguments, is not yet engaged.

99. Those public policy considerations may be relevant in an attenuated form, to prevent a debtor from mounting a completely frivolous defence – an abuse of process designed to put off the evil day.

100. The threshold character of a dispute about indebtedness leaves room for the exercise of a discretion by the court to decline to exercise the jurisdiction to determine that question. 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.

101. 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.

102. But where, as in this case, the court has undertaken the equivalent of a summary judgment determination, it has assumed the jurisdiction to decide a question which the parties had agreed would be determined in another forum. The significance of the public policy of the legislative scheme for bankruptcy jurisdiction is much diminished where the petition is brought by one creditor against another and there is no evidence of a creditor community at risk. Where that factor exists it may be evidenced by another creditor presenting a petition.

103. It is relevant in this case that it was always possible for the Appellant to sue on the debt in New York and to apply there for summary judgment. While there may be some effect on the timing of the instigation of any consequential bankruptcy proceedings in Hong Kong, the absence of other creditors pursuing the Respondent is an indicator that the public interest is unlikely to be adversely affected by such a delay.

> 104. The above approach to the exercise of the discretion to decline jurisdiction to determine the *bona fides* and substance of a dispute about a petition debt is in some sense multi-factorial. While a 'strong cause' test is indicative it should not obscure the range of considerations relevant to the court's discretion.
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> 105. It is clear however, that the so-called 'Established Approach' 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. On that basis this appeal should be dismissed.
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> ……
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> 107. The majority in the CA was correct in its approach. The appeal should be dismissed with costs."

19. Although the contract in that case contained an exclusive jurisdiction clause in favour of a foreign court, there was no dispute before Harris J, or before this court, that the approach laid down in *Guy Lam* applies by analogy where the dispute over the petition debt is subject to an arbitration clause. The Petitioner says however that that approach is not applicable where the debtor relies, as in the present case, on a cross-claim, even though it is subject to an arbitration agreement. Instead of applying *Guy Lam* and dismissing or staying a winding-up petition where the company has raised a cross-claim subject to an arbitration agreement and its opposition is neither frivolous nor an abuse of process, it is submitted that the court should assess whether there is a genuine cross-claim based on substantial grounds, as in the ordinary case without an arbitration clause, and wind up the company if there is none.

The Judge's Decision

20. In his Decision, Harris J first explained the principles that the court applies generally in determining whether or not a winding-up petition

should be dismissed or stayed where the debtor asserts that it has a cross-claim.[10] The rule of practice in Hong Kong is that where the debtor shows it has a genuine and serious cross-claim or, in other words, a cross-claim that has substance, the winding-up petition will be stayed or dismissed. The test is essentially the same as that where the petition debt is disputed, to wit: whether there is a *bona fide* dispute on substantial grounds. Harris J noted that those principles apply equally where the petition is based on a judgment debt.[11] He observed that as a general principle of insolvency law, there is no distinction between a claim and a cross-claim when considering whether a defence to a winding-up petition has been established.[12]

21. Harris J then referred to the judgments of this court and the Court of Final Appeal in *Guy Lam*, noting that the dispute raised by the debtor in that case concerned both defences to the debt and cross-claims. The judge concluded that both judgments must be read as reflecting an understanding that there is no difference of approach to disputed debts and cross-claims generally and that as a consequence, when considering the impact of an arbitration clause, there is no distinction to be drawn between them.[13]

22. Finally the judge noted that the Petitioner did not go so far as to suggest that the present case was sufficiently obviously an abuse to bring it within that rare category in which the court will consider rejecting the debtor's opposition despite the existence of an arbitration clause.[14] In the

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10 Decision, §6.

11 Decision, §7.

12 Decision, §10.

13 Decision, §§13-16.

14 Decision, §17.

result, given the "long and torrid history" of this matter, the judge stayed the petition rather than dismissing it.[15]

The parties' contentions

23. In this appeal, Mr Li accepts that the approach in *Guy Lam* applies by analogy to a case where the petition debt is disputed and the dispute falls within an *arbitration agreement* rather than an *exclusive jurisdiction agreement*. We consider that the concession is correct, for the reasons set out in this Court's judgment in *Re Simplicity & Vogue Retailing (HK) Co Ltd* [2024] HKCA 299, which is handed down on the same date as this judgment.

24. The principle does not however, Mr Li submits, apply in relation to a cross-claim. His argument may be broadly summarised as follows:

(1) First, there are two questions arising in a petition: at the threshold, whether the petitioner has *locus standi* to present the petition, and if so, whether the company is insolvent and should be wound up. *Guy Lam*, properly understood, is concerned with the prior, threshold question of *locus*. In seeking to establish the alleged debt at the threshold stage, the petitioner should be held to the forum agreement between the parties. For cross-claims, however, because the petitioner is recognised to have *locus*, the question is the company's solvency where the court may in its discretion consider a wide range of matters. *Guy Lam* cannot be transposed to apply here.

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[15] Decision, §19.

(2) Secondly, the reason underlying the principle in *Guy Lam* is that the petitioner should be held to his bargain. In a cross-claim case, it is not the petitioner who is asserting a cross-claim in circumvention of the forum agreement. The justification for the principle is not engaged.

(3) Thirdly, if a company raises a cross-claim to invoke the court's discretion to dismiss a petition, it bears the burden of showing its cross-claim has substance. The logic and rationale of *Guy Lam* mean that where the cross-claim is subject to an exclusive forum agreement, the winding-up court should defer to the agreed forum and decline to enter into that question, with the consequence that there is nothing to prevent the petition from proceeding.

(4) Fourthly, applying *Guy Lam* to cross-claims would be unworkable and create a debt dodger's charter. It would encourage companies, when faced with an indisputable petition debt, to search for some cross-claim subject to an exclusive jurisdiction clause or arbitration clause, perhaps under an old agreement, to delay the day of reckoning.

(5) Fifthly, basic principles dictate that the established approach in ordinary cross-claim cases should apply. Abuse of process is the foundation for the practice for dismissing a petition where there is a genuine and serious cross-claim. For the court to find an abuse in the petition because of a cross-claim, it has to take a view about the cross-claim so as to be satisfied it has some merits.

25. On behalf of the Company, Mr Joffe advances his argument in opposition at several levels.

(1) First, he submits that *Guy Lam* itself is a case concerning, *inter alia*, cross-claims brought by the debtor against the creditor, and that as a matter of *stare decisis* it is binding authority against the Petitioner's contention. The appeal therefore fails *in limine*.

(2) Secondly, he submits that the Petitioner's arguments rest on three fundamental suppositions: (i) it espouses a rigid, two-stage approach to petitions – *locus* and discretion; (ii) that the issue of cross-claims falls within the discretion stage and not the *locus* stage; and (iii) that the *Guy Lam* principle should only apply to the *locus* stage, not the discretion stage. None of these suppositions is sound. He submits that there is no rigid division of a petition into the two stages of *locus* and discretion and that it is wrong to say that the issue of cross-claims falls only within the discretion stage and not the *locus* stage. It is a false dichotomy to suggest that the *Guy Lam* principle applies only to the *locus* stage.

(3) Alternatively, if one has to fit the principle within this dichotomy, the validity of cross-claims is an issue that goes to the *locus* of the petitioner to pursue insolvency proceedings.

(4) Finally, and in any event, the petition debt and the Company's cross-claim in the present case arose out of the same joint venture agreement and are closely connected, giving rise to an equitable set-off which extinguishes the petition debt. The cross-claim here thus goes to the Petitioner's *locus*.

Disputed debts, set-offs, and cross-claims in winding-up petitions

26. To put the arguments in their proper context, it is necessary to explain first how the three different concepts of disputed debts, set-offs and cross-claims respectively are dealt with when raised in opposition to a winding-up in petition, in the absence of any forum agreement.

27. Where the debt on which the petition is founded is itself disputed, the established rule of practice in winding-up, as in bankruptcy, is to ask whether there is a bona fide dispute of the petition debt on substantial grounds. If there is, the petition is usually dismissed, leaving it to the petitioner to establish itself as a creditor by a judgment obtained in a civil action. See *Guy Lam CFA*, §35.

28. Where the company opposes the winding-up petition by relying on a claim that exceeds and constitutes a transaction set-off against the petition debt, it is treated as a dispute of the petition debt itself: *McDonald's Restaurants Ltd v Urbandivide Co Ltd* [1994] 1 BCLC 306; *L & D Audio Acoustics Pty Ltd v Pioneer Electronic Australia Pty Ltd* (1982) 7 ACLR 180, 184; *French, Applications to Wind Up Companies* (4th ed), §7.568. This is because a transaction set-off operates in complete or partial defeasance of the claim: see e.g. *Tin Lik v Deutsche Bank AG & others* (CACV 145/2016, 23 June 2017), §99; *Aectra Refining and Manufacturing Inc v Exmar NV* [1994] 1 WLR 1634, 1649B. Equitable set-off (a category of transaction set-off) "operates in equity to impeach the title to a demand … [and] to impugn the creditor's right to assert that any moneys are owing by the debtor to the extent of the debtor's cross-claim": *Derham on the Law of Set-off* (4th ed), §4.30 (footnotes omitted). A claim that can be set off against the petition debt *pro tanto* reduces the debt and, if equal

or greater in amount, extinguishes it altogether, though this effect is of course provisional until the final resolution of the debt and a cross-claim: *Delco Participation BV v Chiho Environmental Group Ltd* [2020] 5 HKLRD 712 at §34. The claim, as such, is tantamount to a denial of indebtedness to the petitioner. (We leave on one side independent set-off, which is based on statutes, for it is in one sense procedural rather than substantive, and does not automatically extinguish the smaller of the two debts until judgment is given for the balance: *In re Hiram Maxim Lamp Co* [1903] 1 Ch 70; *Aectra Refining and Manufacturing Inc v Exmar NV, supra*, at 1650C-E. See also *MacPherson & Keay, The Law of Company Liquidation* (5th ed), §3-082 and *Re City Top Engineering Ltd* [2006] 2 HKLRD 562 at §24.)

29. What is the position where the company opposing the petition raises a mere cross-claim, in the sense of a claim against the petitioner that cannot for some reason be invoked as a set-off to the petition debt? Strictly speaking, such a cross-claim does not affect the petitioner's standing to petition as a creditor, because the petition debt exists independently notwithstanding the existence of a cross-claim that overtops it. Nevertheless, it has been the settled approach of the courts in Hong Kong to treat such cross-claims in the same way as disputes of the petition debt, following the English practice confirmed by the decision in *In re Bayoil SA* [1999] 1 WLR 147: see e.g. this court's decisions in *Re S Y Engineering Co Ltd* (CACV 1896/2001, 20 February 2002); *Re Zhuang PP Holdings Ltd* (CACV 288/2005, 15 June 2006). In *Re Sinom (Hong Kong) Ltd* [2009] 5 HKLRD 487, summarising the position, Kwan J said:

> " 11. As with a petition where there is a bona fide dispute of the debt on substantial grounds ('a disputed debt petition'), where the company has a genuine and serious cross-claim against the

> petitioner greater than or equal to the petitioner's debt ('a cross-claim petition'), such a petition may be restrained from proceeding (*Re Pan Interiors Ltd*. [2005] EWHC 3241 (Ch), paras. [34] to [39]). It is an abuse of the process of the court to make a statutory demand or present a winding-up petition based on a claim to which there is a triable defence (*In re A Company (No. 0012209 of 1991)* [1992] 1 WLR 351). A cross-claim petition is regarded in the same way (*Southern Cross Group plc v. Deka Immobilien Investment GmbH* [2005] All ER (D) 374, paras. [29] & [30]; *Re Pan Interiors, supra,* para. [35]).
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> 12. To successfully resist a cross-claim petition, the company has the onus of establishing that its cross-claim is genuine, serious and of substance. There must be supporting relevant details to demonstrate that the cross-claim is based on substantial ground. The test is very much the same as the test for a disputed debt petition for deciding whether a debt is disputed in good faith and on substantial grounds (*Applications to Wind Up Companies,* by Derek French, 2nd edition, paras 6.10.7.2 and 6.10.7.3 and the cases there cited)."

30. The same approach is adopted in bankruptcy as in winding-up: see *Re Shang Lili* (HCB 5329/2014, 25 January 2016), §§24-25; *Popely v Popely* [2004] EWCA Civ 463, §117. It may also be noted that under rule 48(5)(a) of the Bankruptcy Rules (Cap 6A), the court may set aside a statutory demand if "the debtor appears to have a counterclaim, set-off or cross demand which equals or exceeds the amount of the debt or debts specified in the statutory demand."

31. It has been said that the dismissal of a petition where the debt is disputed is not a matter of discretion but is founded on the petitioner's inability to establish the *locus standi* to present a petition, whereas the stay or dismissal of a petition due to a cross-claim is different and can only be a matter for the discretion of the court: *In re Bayoil SA* [1999] 1 WLR 147, 150G. Nevertheless, the same rule of practice has been adopted. The reason is essentially that there is no difference in principle between the two situations. In *Malayan Plant (Pte) Ltd v Moscow Narodny Bank Ltd* [1980]

MLJ 53 at 55, Lord Edmund-Davies said: "There is no distinction in principle between a cross-claim of substance … and a serious dispute regarding the indebtedness imputed against a company, which has long been held to constitute a proper ground on which to reject a winding up petition." That statement was relied on in *In re Bayoil SA* by both Nourse and Ward LJJ (see pp 154H & 156F). Ward LJ himself said: "there seems to me to be little practical difference between the disputed debt and a cross-claim which does not constitute a set-off properly so called" (p 156E). In *Re R A Foulds Ltd* (1986) 2 BCC 99269 at 99275, Hoffmann J said that the distinction between a petition where the debt is disputed and a petition said to be overtopped by a disputed cross-claim is "somewhat technical".

32. The same approach – which, we should add, is merely a rule of practice rather than rule of law – applies where the petition is founded on a judgment debt, as pointed out by Harris J. The ability to execute a judgment and to seek a winding up are treated as two different things. A stay of execution of a judgment against a company does not in law prevent the judgment creditor from petitioning for its winding up. Conversely, the refusal of a stay of execution does not prevent the Companies court from staying the winding-up petition where appropriate. See *French, Applications to Wind Up Companies* (4th ed), §§7.53 & 7.543; *Goodway Ltd v Pirelli Cables Ltd* [1997] HKLRD 1039, 1042J; *Credit Lyonnais v SK Global HK Ltd* [2003] 4 HKC 104 at §47; *Shun Loong Holdings Ltd v Profitex Investments Ltd* (HCMP 983/2004, 23 April 2004) at §17; *Hofer v Strawson* [1999] 2 BCLC 336, 342; *Popely v Popely* (*supra*), §§72 & 117.

Stare decisis

33. In light of the distinction referred to above, it can be seen that the treatment of mere cross-claims was not directly dealt with in *Guy Lam*. It is true that there are references to "cross-claim" in the judgments of this court and the Court of Final Appeal.[16] But the debtor in that case cross-claimed for declaratory relief that would negate the petition debt. In so far as the cross-claim was for damages, it could possibly be said to be so closely connected with the petition debt as to provide an equitable set-off. There was no argument advanced that a different principle should apply to cross-claims as opposed to a dispute of the petition debt. The question based on which leave to appeal to the Court of Final Appeal was granted focused on the situation where the petition debt is disputed.[17] The question of a mere cross-claim was not material to the courts' inquiry and analysis; nor was it a necessary part of their reasoning.

34. As noted by the Court of Final Appeal in *A Solicitor v The Law Society of Hong Kong* (2008) 11 HKCFAR 117 at §25, under the doctrine of precedent, it is only the *ratio decidendi* of a previous decision that is binding, such *ratio decidendi* being any ruling on a point of law expressly or impliedly treated by the court as a necessary step in reaching its conclusion, having regard to the line of reasoning adopted. It follows from the above that the *ratio decidendi* of *Guy Lam* does not cover a mere cross-claim. The question at hand must be determined by this court as a matter of principle.

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16 See *Guy Lam CFA* at §33; *Guy Lam CA* at §§15, 23 & 64.

17 See *Guy Lam CFA* at §21.

35. The question of the applicability of *Guy Lam* to cross-claims subject to an arbitration agreement has arisen in *Re NT Pharma International Co Ltd* [2023] HKCFI 1623. There, the company did not dispute the petition debt but resisted the winding-up petition brought against it on the ground that it had a cross-claim against the petitioner which exceeded the amount of the debt and was subject to an arbitration agreement. In her judgment given on 20 June 2023, Linda Chan J considered that the real issue before her was not whether the court should follow the *Guy Lam* approach, but whether the company should be allowed to withhold payment of the debt until determination of its cross-claim in the arbitration. Her Ladyship rejected the company's opposition to the petition, on the ground that the cross-claim arose out of a different agreement from that which gave rise to the petition debt, and that to recognize the company's ground of opposition would be "tantamount to conferring a right on the company to retain the petitioner's money as a security for the company's cross-claim". This decision was not cited to Harris J, but when it was drawn to his attention Mr Li stated that it supported his argument. With respect, however, its reasoning appears to have put a gloss on the rule of practice confirmed in *In re Bayoil SA* and subsequent authorities including those in this jurisdiction, by limiting its application to a situation where the cross-claim has arisen from the same contract as the petition debt. Mr Li has not made submissions supporting this gloss, which in any event is not material in this case. The reasoning appears also to have taken no account of the distinction drawn in the authorities between the questions of (i) whether a debt is due and payable by the company despite the existence of a cross-claim, and (ii) whether the company should be wound up notwithstanding it has a cross-claim. Accordingly we do not think the Petitioner can derive support for its contentions here from *Re NT Pharma International Co Ltd*.

Whether Guy Lam limited to question of locus

36. Mr Li submits on behalf of the Petitioner that in every winding-up petition the court is concerned with two questions: first, at the threshold, whether the petitioner has *locus* to petition; secondly, whether the company is insolvent and should be wound up. These are separate questions, to be considered at different stages and, possibly, even by different tribunals. It is submitted that the approach endorsed in *Guy Lam*, applicable where there is an exclusive jurisdiction agreement including an arbitration agreement, applies only to the first question, not the second.

37. It is true that the dispute over the petition debt is described in *Guy Lam CFA* as a "threshold" question (see §§98, 100),[18] but it is relevant to note that the reasoning in *Guy Lam CFA* is grounded in the wider context of the court's discretion to decline jurisdiction (see §§80-93). As French NPJ stated at §85, the parties' jurisdiction agreement "does not affect the jurisdiction of the CFI [in bankruptcy matters]. What it does inform is the court's discretion to decline to exercise its jurisdiction." In a bankruptcy case, the debt relied upon for the petition has to be established before the court can exercise its power to make a bankruptcy order. The bankruptcy court has jurisdiction to determine whether there is a debt if it is disputed. "The threshold character of a dispute about indebtedness leaves room for the exercise of a discretion by the court to decline to exercise the jurisdiction to determine that question."[19] The Court of Final Appeal concluded that, in the exercise of this discretion, where the parties have agreed to have all their disputes under the agreement giving rise to the debt

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[18] and described in *Guy Lam CA* as an "anterior" question (see §§78, 81).

[19] *Guy Lam CFA*, §100.

be determined exclusively in another forum, the established approach in ordinary cases (i.e. declining jurisdiction only if the debtor shows a *bona fide* dispute of the debt on substantial grounds) is not appropriate. Instead, ordinarily, "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."[20]

38. In our view it is too narrow a reading of *Guy Lam* to confine its rationale to the question of *locus* to petition and to say that it is wholly irrelevant once it is accepted the petitioner has *locus* because he has a debt which is not subject to set-off. As established in the *In re Bayoil SA* line of authorities, the court also has a discretion to stay or dismiss a petition, thereby declining jurisdiction, where the petitioner has undisputed *locus* in the strict sense but is faced with a cross-claim. There is no reason in logic or policy to suggest that the parties' forum agreement has no relevance to the exercise of this discretion.

39. The authorities show that in exercising its bankruptcy or winding-up jurisdiction, the court does not wear blinkers and look only at the petition debt. The court has regard to the entire relationship between the parties. Although only the petition debt is relevant to the petitioner's *locus stricto sensu* (in the absence of set-off), it is only part of the overall picture that informs the exercise of the court's powers. The court does not ignore the debtor's cross-claims against the petitioner, and indeed regards them as practically equivalent to disputes of the debt. Also relevant, if they

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[20] *Guy Lam CFA*, §105.

exist, are "reverse cross-claims" by the petitioner against the debtor. Thus, in *Montgomery v Wanda Modes Ltd* [2002] 1 BCLC 289 at §39, Park J said:

> " I agree with the principle that, in exercising or refraining from exercising the power to order WML to be wound up which I have because of the existence of the debt, I ought to look at the entire relationship between WML and Mr Montgomery. Thus I agree that, if that relationship includes not just a cross-claim by WML against Mr Montgomery, but also one or more reverse cross-claims by Mr Montgomery against WML, I must take into account both aspects of it."

40. In *Re Jade Union Investment Ltd* (HCCW 400/2003, 5 March 2004) at §12, after referring to *Montgomery* and *Re Keen Lloyd Resources Ltd* (HCCW 1134/2002, 23 July 2003), Barma J noted that where cross-claims are raised, it is open to the petitioner to put forward reverse cross-claims in order to neutralise the cross-claims relied upon by the company, and held that this applies also where set-offs are raised by the company, because the applicable approach:

> " essentially involves a consideration of the overall relationship between the parties to see whether there is, at the end of the day, an undisputed or undisputable debt that is or will be due to the petitioner, so as to make it appropriate for the court to make a winding up order against the company. If that is right, it should not make any difference whether the matters relied upon by the company as grounds for disputing its liability to the petitioner are set-offs or cross-claims."

This approach was followed by Kwan J in *Re City Top Engineering Ltd* (*supra*) at §27.

41. Similarly, in Australia, in *Re Glenbawn Park Pty Ltd* (1977) 2 ACLR 288 at 291-292, Yeldham J said:

> " … whether or not the existence of such a genuine cross-action or cross-claim strictly deprives an alleged creditor of his status as

> such, it must be a highly relevant factor in the exercise of the discretion which the court clearly has to refuse a winding up order."

42. In these cases with claims in both directions, the question arises whether the petitioner is a net creditor having an interest in having the debtor wound up or bankrupted. The proper approach to the resolution of this question, though not necessarily strictly one of *locus* of the petitioner, is clearly a matter to which a forum agreement between the parties (if one exists) is likely to be relevant.

43. Where the cross-claim is subject to an arbitration clause, as in the present case, for the court to enter into its merits and determine that there is no genuine and serious cross-claim, or one that is of substance, would be against the parties' agreement. Such a determination, it seems to us, would be akin to giving summary judgment in favour of the defendant and against the claimant in respect of the cross-claim. (The procedural rules for ordinary actions in Hong Kong do not provide for summary judgment against a plaintiff, but such a determination is conceptually possible and indeed available under the procedural rules in England: see Civil Procedure Rules, Part 24, r. 24.2, where the test is whether the party has no real prospect of succeeding on the claim.) In *Re a Company (No 002272 of 2004)* [2005] EWHC 422 (Ch), [2005] BPIR 1251 at §12, Ferris J said that "it seems to me that the test for deciding whether a cross claim is genuine and serious is very much the same as the test for deciding whether a debt is disputed in good faith and on substantial grounds." That in turn was in practice indistinguishable from a summary judgment analysis: *Guy Lam CFA*, §§28, 35, 53 & 102. In *Hofer v Strawson* (*supra*) at p 343c, Neuberger J also said that the question of whether there is a genuine triable issue, which is the test in the UK for deciding whether to set aside a

statutory demand where the debtor disputes the debt or raises a counterclaim, set-off or cross-demand,[21] appears to be "very much the same test" as that laid down in *In re Bayoil SA*. A survey of the cross-claim cases in the law reports shows that the determination by the court is essentially a summary judgment type analysis.

44. It follows that, where the parties agreed to have all the disputes under the agreement giving rise to the cross-claim determined in another forum, the public policy in holding parties to their agreements comes into play, just as it does in a disputed debt case: *Guy Lam CFA*, §101.

45. Mr Li argues that in a cross-claim case, it is not the petitioner, but the debtor, who asserts the cross-claim in the court – the non-agreed forum. This seems to us to be a distinction without a difference. It is true that it will be the debtor who has drawn the cross-claim to the court's attention, but the debtor is not seeking the court's determination of his cross-claim. It is the petitioner who is asking the court to reject the cross-claim as a ground of opposition to the petition on the basis that it is without substance. As Mr Joffe points out, the rights and obligations in an arbitration agreement apply once an arbitral dispute has arisen, whichever party is the protagonist, "because the mutuality of the agreement bites on arbitral disputes, not on claims": *Sea Master Shipping Inc v Arab Bank (Switzerland) Ltd* [2018] EWHC 1902 (Comm) at §37. Given that the basis of *Guy Lam* is upholding the parties' agreement for their disputes to be resolved in the agreed exclusive forum, the true question is not so much whether the petitioner should be prevented from abusing the process by

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[21] See *Practice Direction (bankruptcy: statutory demand: setting aside)* [1987] 1 WLR 119 at §4; *TSB Bank plc v Platts (No 2)* [1998] 2 BCLC 1 at 7.

making a petition to the court as whether there is a dispute, which is central to the proper disposal of the petition, that ought to be left to be resolved by the forum chosen by the parties. By undertaking the type of summary judgment determination of the cross-claim as would be appropriate in an ordinary cross-claim case, the court would have likewise "assumed the jurisdiction to decide a question which the parties had agreed would be determined in another forum."[22]

46. Mr Li's argument – his third point – is to say that in such a case, the court should indeed not go into the merits of the cross-claim at all, since the parties have agreed for it to be determined elsewhere, but equally the court should not stay or dismiss the petition, because there is nothing to overtop the petition debt. But this would be contrary to the whole rationale of the *In re Bayoil SA* line of authorities which sees no real difference in principle between cross-claims and disputes of debt as grounds of resistance to winding-up. Mr Li can point to no authority that supports his argument.

47. On the contrary, the Singapore Court of Appeal specifically held in *AnAn Group (Singapore) Pte Ltd v VTB Bank (Public Joint Stock Company)* [2020] SGCA 33 that the tests for both disputed debts and cross-claims must "necessarily mirror each other," and that in both cases winding-up proceedings will be stayed or dismissed where the dispute falls within a valid arbitration agreement between the parties, provided that dispute is not being raised in abuse of the court's process.[23]

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22 *Guy Lam CFA*, §102.

23 See §§55-60.

48. In his oral argument, Mr Li went so far as to say that *Guy Lam* does not apply to a set-off but only to a dispute that the debt has arisen in the first place. Given the discussion in §28 above, it seems to us contrary to principle and authority to treat set-off differently from other disputes of the debt. Nor is there any logical or normative basis to apply a different approach to cross-claims, not to mention the difficulties that may arise on the question whether a cross-claim raised by the debtor can be set off against the petition debt, and the potential argument that the question of set-off is one that should also be left to the agreed forum. In *Eco Measure Market Exchange Ltd v Quantum Climate Services Ltd* [2015] BCC 877, where there were disputes, *inter alia*, as to whether the company was bound by contract to pay the sums due first and to arbitrate any cross-claims later or the cross-claims could be set off against any payment due, the court dismissed the petition, holding that it was for the arbitrator to decide what the terms of payment were, whether there were sums indisputably due, whether there was any cross-claim against those sums, and whether any such cross-claim could be set off against the claim.[24]

49. We are not persuaded by Mr Li that applying the *Guy Lam* approach to cross-claims would create a debt dodger's charter. To rely on that approach the debtor would have to show a valid exclusive forum agreement between the parties that governed the cross-claim. In any event, the Court of Final Appeal in *Guy Lam* had built in a safety valve that allows the rule to be displaced where the dispute "borders on the frivolous or abuse of process".[25]

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[24] See §12.

[25] §105.

50. Delay in putting forward a cross-claim may in appropriate circumstances support a finding that it was raised in abuse of the court's process as a pretext to stave off a winding up. In the present case, whilst the Company's cross-claims were raised several years after the first arbitration, the Company has explained that it was unable to bring them earlier because of the failure by the Petitioner to make available the JV documents. The Petitioner has not contended either before the judge or this court that the cross-claims here have been raised in abuse of process.

51. For these reasons, we consider that the *Guy Lam* approach is applicable whether the dispute that falls within the scope of an exclusive forum agreement has been raised by a dispute of the petition debt, a claim of set-off, or a cross-claim that does not give rise to set-off. It follows that the Petitioner's appeal is to be dismissed.

Whether the Company's cross-claims give rise to equitable set-off

52. It is unnecessary to deal with Mr Joffe's submission that in any event, the Company's cross-claims in the third arbitration can be set off against the outstanding debt to the Petitioner. He submits that they both arose out of the joint venture agreement and are closely connected, triggering an equitable set-off which extinguishes the remaining petition debt. We heard no arguments from Mr Li on this point and neither the claim nor the award in the first arbitration was in the evidence before us. We express no opinion on this issue.

Disposition

53. For the foregoing reasons, the Petitioner's appeal is dismissed. The Petitioner is to pay the costs of the Company, with a certificate for two counsel, to be taxed if not agreed.

(Susan Kwan)	(Aarif Barma)	(Godfrey Lam)
Vice President	Justice of Appeal	Justice of Appeal

Mr Laurence Li S.C., Mr Chow Ho Kiu & Mr Sik Chee Ching, instructed by Messrs. C.L. Chow & Macksion Chan, for the Petitioner (Appellant)

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