SALFORD ESTATES TEST IN MALAYSIA: THE FINAL BLOW?

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The insolvency regime comes face-to-face with the arbitration regime in cases where a debt is disputed but is subject to an arbitration agreement. In such cases, Malaysian courts have previously followed the English position in Salford Estates (No 2) Ltd *v.* Altomart Ltd (No 2)*, namely, that a court should not order the liquidation so long as the disputed debt is 'prima facie' disputed. The Privy Council's decision in* Sian Participation Corp (In Liquidation) *v.* Halimeda International Ltd *has now rejected the* Salford Estates *test and imposed a higher threshold, namely, that the debt must be disputed on genuine and substantial grounds as demonstrated by the debtor. Fortuitously, just two weeks prior to* Sian, *the Malaysian Court of Appeal had also rejected the* Salford Estates *position and imposed the higher threshold of a bona fide dispute on substantial grounds. The Privy Council's decision in* Sian *is thus now the final blow to the Salford Estates test in Malaysia. Further, the astute reasoning of the panel in* Sian *will helpfully inform future judicial deliberations on the interaction between the domestic insolvency and arbitration regimes.*

Keywords: insolvency law, arbitration agreement, Fortuna injunction, winding up petition, liquidation, disputed debt

In *Sian Participation Corp (In Liquidation) v. Halimeda International Ltd*[1] ('***Sian***'), the Privy Council was faced with the question: Where a debt is said to be disputed but is subject to an arbitration agreement, what is the correct test for

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1 [2024] UKPC 16.

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the court to apply to the exercise of its discretion to order the liquidation of the company?

A. Pre-*Sian*: The prima facie test in *Salford Estates*

The previous test that had been applied in England and in several other jurisdictions based on a similar insolvency regime, was established in the English Court of Appeal case of *Salford Estates (No 2) Ltd v. Altomart Ltd (No 2).*[2] It was held there that, whilst the winding up proceedings were not subject to a mandatory stay in favour of arbitration under the English Arbitration Act 1996 ('**English Act**'), a court should nevertheless exercise its discretion to dismiss winding up proceedings where there is a prima facie disputed debt that is subject to resolution via arbitration pursuant to a previously agreed arbitration agreement, save in wholly exceptional circumstances.

B. *Sian*: The *Bona Fide* test

This was the state of law, until the recent Privy Council decision in *Sian.* The Privy Council declared that *Salford Estates* was wrong and should no longer be followed in English law. Instead, the test to be applied in granting or dismissing the winding up petition is whether the debt is disputed *on genuine and substantial grounds* as demonstrated by the debtor to the court when applying to dismiss or resist a winding up petition.[3]

C. *Quo vadis Malaysia: Sian or Salford Estates?*

This article examines the impact of *Sian* on the future development of the line of authority in Malaysia on the issue. The Privy Council alluded to Malaysia as a jurisdiction in which the insolvency courts have 'largely followed *Salford Estates*'.[4] In particular, the Privy Council referred to the Malaysian High Court cases of *Awangsa Bina Sdn Bhd v. Mayland Avenue Sdn Bhd*[5] ('***Awangsa Bina***') and *V Medical Services M Sdn Bhd v. Swissray Asia Healthcare Co Ltd*[6] ('***V Medical Services***'). Those cases had followed *Salford Estates* in holding that the test to be applied is whether there is a prima facie dispute over a debt that is subject to an arbitration agreement.

2 [2014] EWCA Civ 1575; [2015] Ch. 589.
3 *Sian,* at [122].
4 *Sian,* at [80]; *see also* [47] where s. 9 of the Cayman Islands Arbitration Law of 2012 follows the wording of s. 9 of the English Act.
5 [2019] MLJU 1365.
6 [2023] 7 MLJ 155.

Outside the knowledge of the Privy Council's consideration of the issues in this area and ahead of the time the judgment in *Sian* was delivered, and in a curious coincidence of events, the Malaysian Court of Appeal allowed an appeal against the High Court's decision in *V Medical Services* on 6 June 2024, just two weeks before the judgment in *Sian* was given. The Malaysian Court of Appeal's judgment, *Swissray Asia Healthcare Co Ltd v. V Medical Services M Sdn Bhd*[7] ('***Swissray Asia***'), rejected *Salford Estates* and held that the test to be applied was whether there was a *bona fide* dispute on substantial grounds – i.e., the higher threshold later declared in *Sian*.

Against this background of Malaysian jurisprudence, and particularly the fresh rejection of *Salford Estates, Sian* now provides a reasoned nail in the coffin for *Salford Estates* in Malaysia. It cements the position that the courts will not dismiss a winding up petition (or, as the case may be, grant an injunction to restrain the presentation of a winding up petition) on the lower threshold of whether there is a prima facie dispute to be referred to arbitration pursuant to an arbitration agreement. Instead, as held in *Swissray Asia*, the respondent or applicant (i.e., the debtor) must show the existence of a *bona fide* dispute and not merely a *prime facie* dispute, that merits the dismissal of a winding-up petition in favour of arbitration.[8]

In the sections that follow, we will map out and analyse the Privy Council's reasoning in *Sian* alongside the Malaysian authorities, in regard to each of the following steps: (1) whether the statutory provision for a mandatory stay in favour of arbitration applies to a winding up petition, and (2) the implications of a pro-arbitration policy on the court's discretion. We conclude that the position in *Sian* with regard to these steps would be accepted wholly in Malaysia, especially now with the rejection of *Salford Estates* in the independent appellate authority of *Swissray Asia.*

D. An analysis of *Sian*

Faced with a winding up petition and a disputed debt subject to an arbitration agreement, the first step considered by the Privy Council was whether a mandatory stay applies to the winding up petition under domestic arbitration legislation, i.e., section 18(1) of the British Virgin Islands Arbitration Act (which incorporates Article 8(1) of the UNCITRAL Model Law). The provision states:

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7 [2024] CLJU 1358.

8 *Swissray Asia,* at [66].

> (1) 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 than 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]

The Privy Council had recently held, in *FamilyMart China Holding Co Ltd v. Ting Chuan*[9] ('***FamilyMart***'), that the word 'matter' in the equivalent Cayman Islands legislation denotes 'a substantial issue that is legally relevant to a claim or a defence, or foreseeable defence, in the legal proceedings, and is susceptible to be determined by an arbitrator as a discrete dispute'. Notwithstanding this definition of 'matter' in *FamilyMart*, the Privy Council in *Sian* noted that a winding up petition was not in any case an 'action' (or 'claim') within the statutory language of the BVI Arbitration Act. As such, the above mandatory stay provision was inapplicable.

In any event, the Privy Council held that the definition of 'matter' in *FamilyMart* was clearly concerned with the 'determination of disputed rights and obligations'.[10] A winding up petition however 'does not seek to, and does not, resolve or determine anything about the petitioner's claim to be owed money by the company', and '[n]or is the existence or amount of the debt a matter or issue for resolution in those proceedings'.[11] Construing the mandatory stay provision as a whole then, winding up petitions were not subject to a mandatory stay. This conclusion in *Sian* echoed the English Court of Appeal's holding in *Salford Estates.*[12]

The second step – having determined that the mandatory stay provision does not apply – was to determine the correct test for the court's *discretionary (versus mandatory)* stay of a winding up petition. It was on this question that the Privy Council in *Sian* diverged from *Salford Estates.* In *Salford Estates*, it had been held that 'the court should, save in wholly exceptional circumstances […] exercise its discretion consistently with the legislative policy embodied in the 1996 Act'.[13] It 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' if a court were to grant a winding up petition based on a dispute debt which is subject to an arbitration agreement save in wholly exceptional circumstances.[14] As such, in accordance with a pro-arbitration policy, the low threshold of the existence of a merely non-admitted

9 [2023] UKPC 33; [2024] Bus LR 190.
10 *Sian,* at [58].
11 *Ibid.*, at [88].
12 *Ibid.*, at [73].
13 *Salford Estates,* at [39].
14 *Ibid.*

debt should apply. Wherever a debt is not admitted, and regardless of the substance of the grounds of the non-admission, the winding up petition ought to be dismissed.

In *Sian*, the Privy Council held that this was wrong. Instead, the correct test is 'whether the debt is disputed on genuine and substantial grounds'.[15] On the issue of whether this accorded with a pro-arbitration policy, the Privy Council held that the winding up proceedings did not offend the 'negative obligation' embodied in an arbitration agreement 'not to have [disputes] resolved by any court process'.[16] Liquidations do not 'resolve anything about the debt'.[17] Nor do winding up proceedings offend the 'policies underlying the arbitration legislation', because:

(1) Article 8 of the Model Law delineated the reach of the mandatory stay provision, which simply did not extend to winding up petitions.[18]
(2) Where a debt is not disputed on genuine or substantial grounds, it would 'just add … delay, trouble and expense for no good purpose' if creditors were required to go through arbitration as a prelude to seeking liquidation.[19]
(3) The principles of 'party autonomy' and 'pacta sunt servanda' were also 'not offended because seeking a liquidation is not something which the creditor has promised not to do'.[20]
(4) As suggested in academic commentary:

> to apply *Salford Estates* is liable to hinder rather than promote a pro-arbitration policy, since prospective creditors might resist the inclusion of an arbitration clause in their contracts if this has the effect of reducing, or making slower and more expensive, their remedies in the event of an insolvency of the debtor.[21]

In the sections that follow, we will analyse these two steps of (1) whether a mandatory stay applies, and (2) the demands of a pro-arbitration policy in the Privy Council's finding, on the basis of which we conclude that *Sian* is entirely consistent with the latest Malaysian appellate authority on both counts.

15 *Sian,* at [99].
16 *Ibid.*, at [89].
17 *Ibid.*
18 *Ibid.*, at [91].
19 *Ibid.*, at [92].
20 *Ibid.*
21 *Ibid.*, at [87].

E. The Impact of *Sian in the Development of Authority in Malaysia*

1. *Mandatory Stay Provision*

The holding in *Sian* (affirming *Salford Estates*) that section 9 of the English Act did not apply to a winding up petition, and as such, no mandatory stay applied, entirely reflects the long-established position in Malaysia in relation to its mandatory stay provision in section 10(1) of the Malaysian Arbitration Act ('**Malaysian Act**'), set out below:

> A court before which proceedings are brought in respect of a matter which is the subject of an arbitration agreement shall, where a party makes an application before taking any other steps in the proceedings, stay those proceedings and refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

Malaysian authorities are clear, in line with *Salford Estates* and now *Sian*, that winding up petitions are not subject to the mandatory stay provision in section 10 of the Malaysian Act. The High Court in *NFC Labuan Shipleasing I Ltd v. Semua Chemical Shipping Sdn Bhd*[22] provided three reasons for this reading of the Malaysian Act:

(1) *First*, winding up proceedings are '*sui generis*', 'primarily regulated by the provisions of the law enacted specifically to govern such proceedings'. Winding up proceedings 'activate' the process that enables 'the collective enforcement of proven debts of the company […] for the benefit of not just the petitioner but instead the general body of unsecured creditors, all on [a] *pari passu* basis'. The crucial upshot is that 'a winding-up petition is not a claim for payment' and the reliefs granted upon an arbitration *versus* a winding-up petition 'are miles apart'.[23] As such, '[a] winding-up petition is not in the nature of a substantive claim before the Court as contemplated by section 10'.[24]

(2) *Second*, 'the legislative scheme of winding-up does not promote stay of winding-up proceedings'.[25] The Court appears to have meant that the overall legislative scheme of winding-up did not seem to provide for stays readily or often. Stays under sections 243 and 222 of the Companies Act 1965 were not applicable to winding up petitions.[26]

22 [2017] CLJU 943.
23 *NFC Labuan*, at [34].
24 *Ibid.*, at [35].
25 *Ibid.*, at [37].
26 Section 243 provides for a stay 'after an order for winding up has been made […] on the application of the liquidator or of any creditor or contributory'.

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As such, '[i]t would be an unmitigated anomaly under the law if despite the specific winding-up provisions not permitting stay of winding-up petition, the petition could still be stayed under the general stay provisions pursuant to [section 10 of the Malaysian Act]'.[27] Section 221(1) of the Companies Act 1965 offers no statutory support either, notwithstanding that it confers a discretion to the Court to grant a stay in exceptional circumstances. This is because the Court of Appeal had previously held in respect of that provision that 'a winding-up petition ought to be disposed of expeditiously and generally no stay or lengthy adjournment of the petition should be entertained'.[28] Even a 'limited stay or a short adjournment' of the winding up petition would not be granted, as the applicant in this case had not shown 'exceptional circumstances which would warrant the exercise of [the court's] discretion' in this regard.[29] Further, even applications to strike out winding up petitions were 'not generally encouraged' (as apparent from previous decisions of the Courts) and, along with stays, had been 'shown to be inimical to winding-up proceedings in the context of the law governing such winding-up petitions'.[30]

(3) *Third* – and this being 'a greater and more fundamental premise' – section 10 does not apply to winding-up proceedings because of 'the very character of a winding-up petition'.[31] A winding up petition 'is not to determine whether the respondent in the instant case is legally indebted to the petitioner', and '[w]hatever averments of differences or disputes between the parties as may have been set out in the petition serve only to support the essence and substance of the winding-up petition that the respondent was unable to pay its debts which had fallen due'.[32] As such, the winding up petition is not a 'matter' or 'proceeding' within the meaning of section 10 of the Malaysian Act. This reflects very much the reasoning in *Sian* on Article 8 of the UNCITRAL Model Law and section 9 of the English Act.[33]

Section 222 provides for a stay at 'any time after the presentation of a winding up petition and before a winding up order has been made' on the application of 'the company or any creditor or contributory' in the event that 'any action or proceeding against the company is pending'.

27 *Ibid.*, at [39].

28 *Ibid.*, at [41]; *see Maril-Rionebel (M) Sdn Bhd & Anor v. Perdana Merchant Bankers Bhd* [2001] 3 CLJ 248.

29 *Ibid.*, at [42].

30 *Ibid.*, at [44]–[45].

31 *Ibid.*, at [45].

32 *Ibid.*, at [46]–[47].

33 *Sian,* at [53]. Note that, although s. 10(1) of the Malaysian Act does not use the word 'claim', the heading of s. 10 is 'Arbitration agreement and *substantive claim* before court' (emphasis added).

In these premises, Mohd Nazlan J dismissed the application to stay the winding up petition under section 10. Although *obiter* as His Lordship was only hearing the application for a stay, Mohd Nazlan J accepted that the court would be able to hear and dismiss the winding up petition. Nevertheless, His Lordship only held for the purpose of this application that the stay sought, which was premised on section 10 of the Malaysian Act, could not be granted.

This position on the inapplicability of section 10 was re-adopted by the High Court in *Awangsa Bina*, where it was held that '[s]ection 10 of the [Malaysian Act] does not apply to winding up petitions' citing *Salford Estates*.[34] Subsequently, the High Court in *PRPC Utilities and Facilities Sdn Bhd v. PBJV Group Sdn Bhd*[35] also held that 'it is clear that a winding-up proceedings [sic.] are not subject to or caught by an arbitration agreement'.[36]

2. *Pro-arbitration Policy for the Exercise of Discretion*

Notwithstanding the established position that winding up proceedings are not proceedings to which a mandatory stay of arbitration would apply, the next question is how the court should exercise its discretion to grant or dismiss the winding up petition itself, and in particular, whether the lower threshold of a prima facie dispute or the higher threshold of a *bona fide* dispute applies in the face of an arbitration agreement.

The High Court in *Awangsa Bina* went further than *NFC Labuan* to hold that the applicable test for dismissal of the winding up petition was 'whether there is a prima facie dispute of the debt claimed by the Petitioner'.[37] This was on the basis of *Salford Estates, Bdg v. Bdh* (Singapore),[38] and *Lasmos Limited v. Southwest Pacific Bauxite (HK) Limited* (Hong Kong)[39] ('***Lasmos Limited***'). Assessing the facts, Wong Chee Lin J held that the respondent had not reached the higher threshold of a *bona fide* dispute on substantial grounds, but had met the 'lower threshold of merely showing a prima facie dispute', where 'a denial of the indebtedness constitutes a dispute'. The merits of the dispute would then be determined in arbitration. As such, Wong Chee Lin J dismissed the winding up petition.[40]

34 *Awangsa Bina,* at [12].
35 [2022] 2 CLJ 276.
36 *PRPC Utilities,* at [31].
37 *Awangsa Bina,* at [25].
38 [2016] 5 SLR 977.
39 [2018] HKCFI 426 [include cross-reference to HK paper when finalized].
40 *Awangsa Bina,* at [28].

The High Court in *V Medical Services* considered the inverse situation of an application for a Fortuna injunction, which is an injunction to restrain the presentation of a winding up petition.[41] Similarly to *Awangsa Bina*, the High Court held that the lower threshold of a 'prima facie' dispute applied to determine whether to grant the injunction sought. Additionally citing the foreign authorities that had featured in *Awangsa Bina* (including *Salford Estates*), the High Court held that the 'lower threshold prima facie test' applied.[42] The High Court quoted from *Salford Estates* on the pro-arbitration justification for this test, emphasizing party autonomy where the 'creditor ha[d] agreed to refer any dispute relating to the debt to arbitration' and the potential to 'encourage parties […] to bypass the arbitration agreement' by presenting a winding up petition.[43]

As alluded to under section C above, the Malaysian Court of Appeal allowed an appeal against the High Court decision in *V Medical Services.* In its judgment, *Swissray Asia*, the Court of Appeal rejected the lower threshold in *Salford Estates* and applied the higher threshold of a 'genuine or a bona fide dispute',[44] just as was held in *Sian* two weeks later.

Whilst the conclusion on the applicable threshold in *Swissray Asia* was the same as in *Sian*, the judgment of the Court of Appeal in *Swissray Asia* differed in at least three notable respects:

(1) The Court of Appeal in *Swissray Asia* justified the higher threshold on the grounds of preventing abuse of process. This arose from the particular facts of the case, where the respondent (i.e., injunction applicant; the debtor) had been found to have made 'repeated acknowledgments of the debts' and 'unequivocal admissions as to the sum due and owing'[45] notwithstanding the disputes it was now raising in support of its injunction application. The Court of Appeal did not dwell long on arbitration policy but more on the element of abuse of process. The Court of Appeal did nevertheless articulate a general position that the 'mere assertion of the existence of an arbitration clause cannot simply be recited as if it is some mechanical mantra'[46] – which suggests Malaysian courts would be wholly onboard with the Privy Council's reasoning in *Sian* that the lower threshold cannot be maintained merely on grounds of a pro-arbitration policy, and that the higher threshold would always apply.

41 *Swissray Asia,* at [5].
42 *V Medical Services,* at [36]–[40].
43 *Ibid.*, at [41].
44 *Swissray Asia,* at [67], [83].
45 *Ibid.*, at [49], [74], [76].
46 *Ibid.*, at [73].

(2) The Court of Appeal suggested that the existence of a *bona fide* dispute of debt would be demonstrated by one party having 'already referred the disputes to arbitration'. It was held that this very fact distinguished *Swissray Asia* from *Awangsa Bina* and *Bdg v. Bdh* (where the disputes had already been referred to arbitration).[47] The Court of Appeal nevertheless did not hold that this was a requirement in order to meet the threshold of a *bona fide* dispute. This diverges from the position in Hong Kong (as applied in *Lasmos Limited* and *But Ka Chon v. Interactive Brokers LLC*[48]) which imposes an additional requirement that the party seeking the stay had at least taken steps to commence arbitration.

(3) Finally, the Court of Appeal also justified granting the Fortuna injunction on the basis of the equitable principle of coming to the court with clean hands.[49] The respondent had admitted that the purchase order (on which the debt was allegedly based) had been a 'sham document' that it created 'in order to deceive and mislead the relevant authorities' for 'customs purpose only'.[50] This consideration of the 'clean hands' principle highlights potential additional inputs into deciding an equitable Fortuna injunction application.

Notwithstanding the above distinct factors in *Swissray Asia* such as a clear abuse of process and a Fortuna injunction being sought (rather than a winding up order), the Court of Appeal did turn a firm face against *Salford Estates.* The three distinct factors listed above do not detract from the general acceptance by the Court of Appeal of the higher threshold, especially given its clear expressions of a pro-insolvency policy (on which, *see* section F below). It is likely that the higher threshold will be upheld if appealed to the Federal Court (the apex Court of Malaysia), or otherwise affirmed in future cases, on the strength of the Privy Council's decision in *Sian*.[51] The Privy Council's additional detailed reasoning on insolvency policy and arbitration policy will indeed be illuminating for future appellate cases in Malaysia.

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47 *Ibid.*, at [76].

48 [2019] HKCA 873.

49 *Ibid.*, at [68]–[69], [77].

50 *Ibid.*, at [22], [78].

51 Very recently, the Court of Appeal had indeed cited *Sian* with favour in another case, *Peninsula Education (Setia Alam) Sdn Bhd v. Biaxis (M) Sdn Bhd (in liquidation)* [2024] CLJU 1662 ('***Peninsula Education***'). This was however strictly *obiter* as the debtor in that case was already in liquidation, and was not facing a winding up petition on grounds of a disputed debt.

F. *SIAN & BEYOND IN MALAYSIA*

Sian has decisively rejected the *Salford Estates* approach to winding up petitions on the basis of disputed debt subject to an arbitration agreement. Whilst jurisdictions similar to the English system around the world have largely adhered to *Salford Estates* – with some reservations, as were made explicit in Hong Kong[52] – Malaysia had for several years followed suit until June 2024 when it diverged at the appellate level in *Swissray Asia.*

In this context, *Sian* might effectively put *Salford Estates* to rest in Malaysia. Although the Federal Court has yet to deliver its final stance, and the higher threshold will be further defined in future cases (especially in winding up petitions themselves, as opposed to Fortuna injunction applications), *Sian* along with *Swissray Asia* signals that Malaysia is firmly shifting towards applying a higher bar of a bona fide dispute on substantial grounds.

As a matter of policy, this development appears to be a pro-creditor and pro-insolvency development on the part of Malaysia. This is rather clear from the Court of Appeal's critical remarks in *Swissray Asia* that the *Salford Estates* approach would afford undue indulgence to debtors and cause prejudice to creditors by frustrating the enforcement of the contract under which the debt is owed:

> To countenance the lower threshold test advocated by *Salford Estates*, would open the door to parties in breach of their contractual obligations subjecting the system to abuse by the mere assertion of a dispute no matter how frivolous in nature, just in order to derail or to defeat the legitimate presentation of a winding up petition and in so doing, abuse the process. […] This avenue also would not be in the best interests of oiling the machinery of the wheels of commerce that very much depend upon parties honouring the contractual bargain made between them.[53]

Nevertheless, as *Sian* is studied and applied more closely over time, perhaps a more nuanced treatment of the insolvency versus arbitration debate will emerge – one which does not pit insolvency against arbitration but holds them as categorically separate matters that simply serve different concurrent functions. Shades of this can be seen in the Court of Appeal's remarks in another case (alluding to the insolvency versus arbitration debate in *obiter*) to the effect that: '[l]iquidation does not change the mode of resolving a dispute [and] [n]either is liquidation opposed to arbitration for arbitration is nothing more than a way of determining if liability is established'.[54]

52 *Sian,* at [81].
53 *Swissray Asia,* at [84]–[85].
54 *Peninsula Education,* at [60].

To tie the threads of this concluding section together: it is now clear from *Swissray Asia* (and will likely be strengthened by *Sian*) that a higher legal threshold applies for the Malaysian courts to decide not to order the liquidation of a company where a disputed debt is subject to an arbitration agreement. The debt needs to be *bona fide* disputed on substantial grounds. Based on *Swissray Asia*, the underlying policy position appears to be pro-creditor and pro-insolvency; however, a more neutral and nuanced treatment of the debate (which does not pit insolvency against arbitration) may emerge over time. The debate in Malaysia will be illuminated by *Sian* and the judgments and commentary that will no doubt follow.