In The Supreme Court of Bermuda

COMPANIES (WINDING-UP)

COMMERCIAL COURT

2012: No. 243

IN THE MATTER OF TITAN PETROCHEMICALS LIMITED

AND IN THE MATTER OF THE COMPANIES ACT 1981

REASONS FOR RULING ON SUBSITUTION APPLICATION

(In Court)[1]

Date of Ruling: July 23, 2013
Date of Reasons: July 26, 2013

Mr Cameron Hill, Sedgwick Chudleigh, for KTL Camden Inc ("KTL Camden"), the Substituted Petitioner

Mr. Mark Diel and Mr. Kevin Taylor, Marshall Diel & Myers, for the Company

Introductory

[1] The present Judgment was circulated to the parties to save the costs of a purely formal hearing to hand down judgment.

1. On May 10, 2013, I ruled that the Petition presented on July 10, 2012 by Saturn Petrochemicals Holdings Limited ("Saturn") was liable to be struck-out. This was on the basis of standing grounds belatedly raised by the Company and supported by KTL Camden, which foreshadowed the present substitution application. In paragraph 54 of the May 10, 2013 Ruling, I stated as follows:

> "*54. Accordingly, I find that I should exercise my discretion to strike-out the Petition. However if the parties are not ready to proceed with the substitution application which Mr. Hill said his client was willing to make at today's hearing, I would propose to make the following Order. I will adjourn rather than immediately strike-out the Petition to a date to be fixed after the handing down of this Judgment to afford to facilitate the hearing in Chambers during the adjournment of KTL Camden's application for substitution. This is an application which Mr Hill has already demonstrated has very good prospects of success.*"

2. Saturn's Petition was accordingly adjourned to July 23, 2013 when KTL Camden's application to be substituted as Petitioner was listed for effective hearing.

3. On June 5, 2013, Saturn applied *inter partes* for leave to appeal against Court's determination it lacked standing to petition and the exercise of the discretion to strike-out either at all or at the interlocutory stage. According to its draft Notice of Appeal, the following relief was sought from the Court of Appeal:

> "*3.1 An order setting aside the decision of the Supreme Court dated 10 May 2013;*
>
> *3.2 Such other orders as may be just and appropriate in the event that KTL Camden's application to substitute as a petitioning creditor is granted.*"

4. According my notes of the hearing, I made the following Order on the leave to appeal application:

> "*Leave to appeal application adjourned to the hearing of the substitution application. Costs in the application.*"

5. At the July 23, 2013 hearing when the Company was represented for the first time by its current attorneys, I granted leave to appeal. This was on the basis that I proposed on that same date to both strike-out Saturn's Petition and adjudicate KTL Camden's substitution application so that either there would be no petition before the Court at all, subject to Saturn's appeal, or the Petition would be amended so as to substitute the

new Petitioner. Saturn's application was not opposed by the Company. Although I may have omitted to pronounce any order in relation to the costs of the leave to appeal application and counsel may also have omitted to avert to the issue, I intended to make the usual order that the costs of the application should be in the appeal.

6. At the end of the hearing of KTL Camden's substitution application, I decided to grant the application for leave to amend the Petition substantially in terms of the draft placed before the Court. However, I refused leave to rely on the claims two other related creditors which I considered the Company had clearly shown to be disputed in tangible terms. These are the reasons I promised to give for my decision to accede to the substitution application.

7. Mr. Diel for the Company invited the Court to consider as part of the substitution application the point that any substitution order should be stayed to avoid potential confusion and prejudice to the Company flowing from the pending Saturn appeal. My provisional view was that this issue could best be determined in the context of the Company's application for an extended adjournment of the Petition with a view to developing and promoting a scheme of arrangement as an alternative to a winding-up.

8. Accordingly, I reserved my decision on this aspect of the substitution application and indicated that I would include my decision in the present judgment if required. Having considered the matter further, however, the appropriate course appears to me to be to include my decision on the stay argument in the present judgment in any event for the following reasons.

9. It was or ought to have been obvious that to the extent that the Company sought to advance a technical argument that the substitution application ought not to be granted at all because of the fact that Saturn had already been granted leave to appeal, that narrow submission was rejected when the substitution application was granted. It was somewhat unclear to what extent this technical point was still pursued as it appeared to be premised on the mistaken assumption that the Court granted leave to appeal before hearing the substitution application.

Legal findings: principles governing substitution applications

10. The basic principles governing substitution were not in controversy. Rule 27 of the Companies (Winding-Up) Rules 1982 provides as follows:

> "***Substitution of creditor or contributory for withdrawing petitioner***
> *27 When a petitioner for an order that a company be wound up by the Court is not entitled to present a petition, or whether so entitled or not, where he (1) fails to advertise his petition within the time prescribed by these Rules or such extended time as the Registrar may allow or (2) consents to withdraw his petition, or to allow it to be dismissed, or the hearing adjourned, or fails to*

appear in support of his petition when it is called in Court on the day originally fixed for the hearing thereof, or on any day to which the hearing has been adjourned, or (3) if appearing, does not apply for an order in the terms of the prayer of his petition, the Court may, upon such terms as it may think just, substitute as petitioner any creditor or contributory who in the opinion of the Court would have a right to present a petition, and who is desirous of prosecuting the petition. An order to substitute a petitioner may, where a petitioner fails to advertise his petition within the time prescribed by these rules or consents to withdraw his petition, be made in chambers at any time." [emphasis added]

11. Mr. Hill referred the Court to the following passage in McPherson, '*The Law of Company Liquidation*'[2] (at 3.077) commenting on the scope of the discretion conferred by the English counterpart of this Bermudian rule:

> "*The court has a discretion whether or not to allow substitution. In deciding whether to exercise the discretion given by r.4.19 the court must balance two competing policies. First insolvent companies should not be allowed to continue to trade to the detriment of existing and future creditors, but should be wound up as expeditiously as possible. Secondly, a court should not allow winding up to be used as a debt collecting mechanism or as an instrument of oppression by a creditor whose debt is subject to a genuine dispute.*"

12. Mr. Diel did not dissent from these broad principles. However, in my judgment, the first policy operating in favour of substitution is somewhat broader than *McPherson's* classical formulation derived from the pre-corporate rescue era. Substitution is appropriate not just where it is clear that an insolvent company should be wound up as soon as possible, but also where it is clear that an insolvent company will be liable to be wound up unless some alternative restructuring can be implemented. Winding-up proceedings, with or without provisional liquidators in place, can serve a useful purpose in practically (if not technically) 'holding the ring' while an alternative to a liquidation is explored. Where an insolvent company attempts to implement an out of court restructuring without presenting its own winding-up petition, it will always be vulnerable to an unpaid creditor's petition being validly appointed. Whether or not a winding-up order ought in fact to be made is a distinct and separate question.

13. The second competing policy against substitution is where controversy lay in the present case; because the Company contended that the alleged Petition debt was genuinely disputed. In this regard, Mr. Hill relied upon the test applied by this Court in another substitution case, *Re Gerova Financial Group Ltd.* [2012] Bda LR 20:

> "*51.The relevant principles applicable to deciding whether or not a petition cannot be presented or pursued because the debt upon which it was based is disputed are well settled. They were helpfully summarised by Justice Indra*

[2] It was unclear from the extract which edition was reproduced.

Hariprasad-Charles in Metalloyd Ltd.-v-Burwell Resources Ltd., Eastern Caribbean High Court (BVIHCV2006/0083), Judgment dated July 17, 2006 (unreported) as follows:

> *'[55] The principles of law are clear that if the Company has genuine and substantial grounds for disputing the debt, this court sitting as a Company Court should not allow the application to continue but should instead dismiss it so that the parties can determine any dispute in a civil court. The onus of proof that there are genuine and substantial grounds for disputing the debt lies on the Company. In Re a Company (No 001946 of 1991), ex parte Fin Soft Holding SA13, Harman J. at page 740 said: "In my view, the true test is: Is there a bona fide dispute? Meaning thereby: Is there a real dispute? That is, a real and not fanciful or insubstantial dispute about the debt. Alternatively, the test can be defined as: Is the debt disputed upon substantial grounds?…'Bona fides', in the sense of good faith, has nothing to do with the matter. I therefore, believe that the true question is, and always is: Is there a substantial dispute as to the debt upon which the petition is allegedly founded?'"*

> *52. Re a Company (No 001946 of 1991), ex parte Fin Soft Holding SA[1991] B.C.L.C. 737 was case where no substantial dispute was found to exist in relation to a petition debt based on a promissory note. The dispute was raised 'late in the day and the evidence indicated that the company was desperately seeking any defence which might justify its non-payment of the claim': McPherson, paragraph 3.037. Whether a dispute is substantial is a question of judgment based on the facts of each case.*"

14. The Company's counsel relied upon similar statements of principle in *McPherson's*, 1st edition in England and Wales, at pages 110-111. One legal controversy centred on the impact of the arbitration clause in the guarantee which forms the basis of the Petitioner's debt. Mr. Diel submitted that the existence of this clause lightened the test the Company had to meet in demonstrating the existence of a substantial genuine dispute. He referred the Court to cases dealing with traditional applications to stay ordinary civil litigation in favour of arbitration in this regard: *Halki Shipping Corp.-v-Sopex Oils Ltd.* [1998] 2 All ER 23 (CA) at 56; *Wealands-v-CLC Contractors* [2000] 1 All ER (Comm) 30 (CA). Counsel rightly submitted that the question of the interaction between Article 8 of the UNCITRAL Model Law and the question of a creditor's standing to petition had been considered by this Court in *Discover Reinsurance Company-v-P.E.G. Reinsurance Company Ltd.* [2007] SC (Bda) 19 Com; [2007] Bda LR 20. But in that case I explicitly held that the standard test for determining a creditor's standing to petition applied to a claim based on a contract containing an arbitration clause:

"*51.In light of the findings that I have made with respect to the traditional abuse of process strike-out application, I would be bound to find that this Court has no jurisdiction to grant a stay under Article 8 of the Model Law, as regards the insubstantial defences which I have held do not deprive the Petitioner of the right to present and prosecute the present Petition. In summary, this is because there is no substantial defence to the Petition debt, and the prosecution of the Petition does not involve the determination of any dispute which is arbitrable under the Contract.*"

15. It appeared to me to be well settled that it is only if there is a genuine or bona fide dispute which is based on substantial grounds that a winding-up Court is required to consider staying or dismissing the winding-up proceedings on the grounds that the relevant dispute ought to be determined in arbitration proceedings or in some other contractually agreed forum. The scope of an unpaid creditor's access to the winding-up jurisdiction of the Court is defined by a single test and is not materially reduced simply because its claim happens to be based on a contract containing an arbitration or exclusive jurisdiction clause mandating the adjudication of disputes by some other tribunal.

Findings: was the Petition debt bona fide disputed on substantial grounds?

16. In my judgment it was clear that there was no genuine dispute based on substantial grounds as to KTL Camden's status as a net creditor of the Company. When a demonstrably insolvent company can find no clear support for an alleged dispute in relation to a mature debt in contemporaneous documents, and first raises the dispute in material prepared in opposition to a substitution application, the belatedly raised argument must be viewed with a somewhat sceptical eye. After all, the burden rests on the Company to satisfy the Court that the existence of what appears to be a valid debt is in fact subject to a genuine and well-founded dispute.

17. KTL Camden owns a ship, Titan Venus (formerly Camden), which was chartered to Titan Storage Ltd, a subsidiary of the Company ("the Charterers"), under a Bareboat Charter Agreement ("the Contract"). The Company guaranteed the Charterer's obligations to KTL Camden under the Contract under a guarantee ("the Guarantee"). The Guarantee is governed by English law and incorporates the arbitration clause in the Contract. By letter dated April 13, 2012, KTL Camden demanded in excess of $4 million under the Contract from the Charterers and when they failed to pay made demand on the Company by letter dated May 4, 2012.

18. By Addendum No. 2 dated September 27, 2012, the Charterer expressly confirmed its pre-existing obligations to KTL Camden and agreed to redeliver the Titan Venus on or about October 9, 2012, which occurred. Shortly thereafter, disputes arose in relation to two other ships managed by the same agents, referred to in the evidence as Edinburgh and Mayfair which were each owned by separate companies. The agents are referred to in the evidence as Frontline.

19. The averment is made in Seventh Wong affirmed on July 19, 2013 that various disputes have arisen about KTL Camden's debt and it implies that the exhibited correspondence confirms this fact. I find that it does not. There is no reference in that correspondence to the Titan Venus, which had at that point already been redelivered. There is mention of the Edinburgh and Mayfair. While the correspondence potentially supports the argument Frontline promised to negotiate new terms reference ships other than KTL Camden's, the shadowy claim seemingly articulated for the first time on July 19, 2013 is not reflected in any prior or contemporaneous correspondence placed before the Court. The Notice of Arbitration dated July 20, 2013 (substantially based on Seventh Wong) makes the following material averments:

    (a) in September 2012, Frontline as agents for various vessels including KTL Camden's began to discuss accelerated redelivery;

    (b) the Charterer agreed to redeliver to KTL Camden because Frontline represented or agreed that if this was done it would negotiate suitable time charters for other vessels. These new arrangements were essential for the preservation of the Charterer's oil storage business;

    (c) on or about October 24, 2012, the Frontline reneged on the new arrangements and (on an unspecified date) wrongfully terminated the Edinburgh and Mayfair Charters;

    (d) this wrongful termination, and the conduct of KTL Camden, Edinburgh and Mayfair caused the Company huge losses amounting to $21 million;

    (e) as the Guarantee is expressed to be "*subject to all defences, setoffs, and counterclaims of the Charterer now or hereafter existing under the Contract or under any applicable law*", the Charterer's losses can be relied upon by the Company to extinguish its obligations under the Guarantee.

20. On their face, I found these allegations said to support a genuine and substantial dispute about the liability of the Company to KTL Camden under the Guarantee wholly lacking in substance for, *inter alia*, the following reasons:

    (a) having regard to the commercial context, the terms and the separate character of the contractual arrangements entered into in respect of each separately owned vessel, it seems inherently improbable that the redelivery agreement concluded by Frontier on behalf of KTL Camden in September was made conditional upon unrelated agreements being negotiated with third parties who happened to be represented by the same agent;

    (b) the implicit proposition that, in breaching a representation or an agreement to enter into fresh agreements between Edinburgh and

Mayfair and the Company and/or in directing the wrongful termination by Edinburgh and Mayfair of their Charters with the Company, Frontier was acting as agent of KTL Camden which is liable for all consequential loss, is legally and factually unintelligible;

(c) no legally coherent allegations are made against KTL Camden in the Notice of Arbitration (or in Seventh Wong) in any event; and

(d) whilst I found no reason to reject the narrow submission that any counterclaims, defences or setoffs which the Charterer might have in respect of its losses under the Contract or otherwise could be potentially relied upon by the Company to reduce or extinguish its liability under the Guarantee, it did not appear to me to be arguable that this clause in the Guarantee was intended to operate so as to potentially extinguish the Company's liability to KTL Camden altogether based on defences, etc., which were wholly unrelated to the Contract and/or the conduct of KTL Camden.

21. For these reasons I found that the Petition debt of KTL Camden was not genuinely disputed on substantial grounds.

Findings: the Company cannot be forced to fight on two fronts

Narrow submission

22. The Company made the narrow submission that substitution should be refused because it would be absurd to construe rule 27 as contemplating second creditor being substituted while the first petitioner was appealing the determination that it lacked standing to petition. This argument was unsupported by relevant authority and in my judgment was wholly inconsistent with the underlying rationale of the substitution process, particularly in the context of a clearly insolvent company. It was implicitly rejected when I decided to grant the substitution application.

23. The point might have had greater weight if, as the Company's new counsel initially believed, the Court had implicitly struck-out the Saturn Petition and granted leave to appeal before entertaining the substitution application. Rule 27 does envisage a simultaneous process whereby the substituting creditor enters the stage as the original petitioner departs. However, the Court studiously attempted to avoid creating this sort of legal muddle by adjourning the leave to appeal application to be heard on the same date as the substitution application.

24. On the day of the 'joint' hearing, for administrative convenience, the leave to appeal application was heard before the substitution application. But this was on the explicit basis that all Orders made (striking-out, leave to appeal and adjudication of substitution application) would be dated as of the same date in any event.

Broader submission

25. I construed the argument that the Company should not be required to fight on two fronts more broadly as an adjunct to the argument that rather than proceeding with a hearing of the Amended Petition, the Court ought to grant a generous adjournment to permit the Company to pursue a scheme of arrangement. To the extent that the outcome and impact of Saturn's appeal was unclear, and Mr. Hill plausibly argued that it would not be likely to impact on his client's right to pursue the Amended Petition at all, this was a matter of case management.

26. This broader question in my judgment ought properly to be addressed, if still contentious, at the next hearing of the Petition when directions for the further conduct of the Petition are likely to be given.

Conclusion

27. For the above reasons on July 23, 2013 I granted KTL Camden leave to be substituted as Petitioner under an Amended Petition.

Dated this 26th day of July, 2013 _____
IAN R.C. KAWALEY CJ