Anti-suit injunction granted by Grand Court to restrain Cayman liquidators from continuing New York litigation

In a judgment delivered on 13 February 2018, the Grand Court of the Cayman Islands granted an anti-suit injunction to restrain the joint official liquidators of Argyle Funds SPC (in Official Liquidation) (**"Argyle"**) from continuing litigation commenced in the Supreme Court of the State of New York against Argyle's former statutory auditor (BDO Cayman) and three related parties.

The Hon. Justice Parker held that the audit engagement letters between Argyle and BDO Cayman required disputes to be resolved via arbitration in the Cayman Islands. The Court also enforced *"sole recourse"* provisions in the engagement letters, restraining the liquidators from continuing their claims in New York against the three related parties.

The Court applied well-established principles as to the primacy of arbitration agreements, and rejected novel arguments raised by Argyle concerning the interpretation of the Cayman Islands' *Arbitration Law, 2012*. The judgment confirms that the Grand Court will restrain parties from continuing proceedings commenced in breach of their contractual dispute resolution obligations, and reinforces confidence in the Cayman Islands as a pro-arbitration jurisdiction.

The judgment, which will be of particular interest to insolvency practitioners, auditors and other Cayman professional service providers delegating work internationally, provides a salutary lesson to litigants about the risks of commencing legal proceedings in breach of arbitration, exclusive jurisdiction and other dispute resolution clauses.

Background

Argyle was a Cayman Islands mutual fund with significant exposure to debt factoring via investments made through two separate credit advisors which each perpetrated multi-million dollar frauds at Argyle's expense, leading to Argyle's liquidation in April 2016.

Argyle's liquidators obtained judgments in the United States against the credit advisor companies, their principal Donald Barrick and Mr Barrick's wife. However, by the time the liquidators obtained these judgments, there were no assets against which the judgments could be enforced. This led the liquidators to consider pursuing claims against Argyle's auditors.

In June 2017, after having obtained the sanction of the Grand Court on an *ex parte* application, Argyle's liquidators commenced proceedings in the Supreme Court of the State of New York (the **"New York Proceedings"**) against four entities: BDO Cayman, BDO Trinidad and Tobago, BDO USA and Schwartz & Co, seeking damages in excess of US$280 million. The allegations advanced by Argyle in the New York Proceedings concerned the audit years 2010 – 2013, and went beyond the 'usual' allegations of professional negligence to include fraud and wilful misconduct.

In August 2017, BDO Cayman applied to the Grand Court for an anti-suit injunction to restrain the liquidators from continuing the New York Proceedings in breach of the audit engagement letters between Argyle and BDO Cayman for the relevant audit years (the **"Engagement Letters"**), which were expressly governed by the laws of the Cayman Islands.

In seeking to restrain the claims in the New York Proceedings against itself, BDO Cayman relied upon the dispute resolution clauses in the four Engagement Letters, which included clauses providing for the resolution of disputes by arbitration seated in the Cayman Islands. In addition to the arbitration agreements, the Engagement Letters each contained a clause providing that the courts of the Cayman Islands would have exclusive jurisdiction in relation to any claims or matters arising from the Engagement Letters.

As regards the other defendants to the New York Proceedings, the application was brought by BDO Cayman to enforce "sole recourse" provisions in the Engagement Letters to the effect that BDO Cayman alone would be responsible to Argyle for the performance of the audits, even if BDO Cayman delegated work in respect of these engagements to one or more of its affiliates, and that Argyle would not bring any claim against any such third parties.

The evidence adduced on behalf of BDO Cayman was that certain work was delegated to BDO Trinidad and Tobago in accordance with the Engagement Letters, but that neither BDO USA nor Schwartz had any involvement in the relevant audits. Unusually, Argyle relied upon affidavit evidence from its New York attorneys, which asserted that BDO USA and Schwartz were (or speculated that they must have been) involved in the relevant audits.

Following a two day hearing in January 2018, Mr Justice Parker delivered judgment in February 2018 dismissing all of the arguments advanced by Argyle and granting the anti-suit injunction in the terms sought by BDO Cayman against all four of the defendants to the New York Proceedings.

The Court's decision: anti-suit injunction to restrain the New York Proceedings

Justice Parker had no hesitation in restraining the liquidators from continuing the New York Proceedings, saying:

"This case concerns the audits of a Cayman fund by Cayman statutory auditors pursuant to Cayman law under Engagement Letters governed by Cayman law with Cayman jurisdiction and arbitration clauses. For the reasons I have given litigation in New York is not the regime that was agreed to in the contractual documents. The clear contractual scheme cannot be conveniently side-stepped to obtain procedural or other strategic advantages secured in a chosen forum. There are no strong reasons that have been shown to me as to why the parties should not be held to their contractual agreements…"

Although it was not necessary for the purposes of BDO Cayman's application for there to be a detailed assessment of the merits of the claims advanced in the New York Proceedings, Justice Parker was critical of the overwrought claims in the New York proceedings and the manner in which they had been advanced by Argyle on the evidence. His Lordship said:

"On the evidence before me I have not seen material that would need to be adduced in order to persuade an English or Cayman court to find that fraud or wilful misconduct by a reputable professional international firm (in the ways alleged in the Amended Complaint and with the motivations suggested), would be likely to be proven. Suffice it to say that I find the way the case has been put in New York against BDO Cayman and the other entities is inherently implausible. Broad assertions have been made with no particularity or supporting evidence and no specific collusion by the auditors with anyone else has been pleaded. Neither has cogent evidence of fraud been pleaded and the motivations alleged are inherently implausible".

In reaching these conclusions, His Lordship rejected various procedural arguments advanced on behalf of Argyle, and two novel arguments made in respect of sections 7 and 8 of the Arbitration Law which will be of interest to parties to Cayman Islands arbitration agreements.

Section 7 of the Arbitration Law: Adoption of contracts by a liquidator

Section 7 of the Arbitration Law provides:

"A contract in which the director of an insolvent body corporate has agreed to refer to arbitration any dispute arising from the contract shall be enforceable against the liquidator, receiver or administrator if either of them adopts the contract."

Argyle argued that the liquidators had not "adopted" the Engagement Letters within the meaning of section 7, however Justice Parker held:

"*I can deal with this very shortly. I do not believe that any special procedure or formality is required in relation to 'adoption'....* [Leading counsel for Argyle] *sought to persuade me that the contracts in this case for audit services had been performed and that her client was suing for losses suffered by past breaches. She submitted that it was not right to equate the reliance on the contracts made in the New York Proceedings with* "adoption" *for the purposes of section 7....I do not agree. In my view if a liquidator sues on a contract which has within it an arbitration agreement the section makes it absolutely clear that he is bound by the arbitration agreement as well."*

Section 8 of the Arbitration Law: Consumer arbitration agreements

Section 8 of the Arbitration Law concerns consumer arbitration agreements. By subsection 1, where a contract contains an arbitration agreement and a person enters into that contract as a "consumer" (as defined), the arbitration agreement is enforceable against the consumer only if, after a dispute has arisen, the consumer enters into a separate written agreement certifying that he has read and understood the arbitration agreement and agrees to be bound by its terms.

Argyle's position was that it had entered into the Engagement Letter as a consumer within the meaning of section 8. It was common ground that Argyle had not entered into any separate agreement to affirm the arbitration agreements contained in the Engagement Letters, and on that basis Argyle argued that the arbitration agreement was unenforceable.

Section 8 provides that "consumer" in relation to *"any services or facilities, means any person who employs or wishes to be provided with the services or facilities"*. Argyle's leading counsel argued that, by enacting this definition, the Cayman Islands legislature chose not to adopt the conventional definition of consumer (*i.e.* a natural person contracting outside the scope of their business), and that this interpretation made commercial sense because additional protection is required in a *"services economy"* such as the Cayman Islands.

Leading counsel for BDO Cayman argued that this interpretation would result in the absurd conclusion that every party that contracted for services would be treated as a consumer for the purposes of section 8 and, as such, could elect in the event of a dispute whether or not they wished to resolve disputes by arbitration. If Argyle was correct, the practical effect would be that arbitration agreements in contracts for services in the Cayman Islands would be unenforceable. This would have significant consequences for parties to Cayman law governed arbitration agreements.

Justice Parker agreed with BDO Cayman, observing that it was "*most unlikely… that the draughtsman would have intended businesses to be treated as consumers for the purposes of section 8."* He held that this *"… would remove any distinction between consumers and non-consumers which was plainly not the intention behind the provision…. If Argyle was right every business in Cayman that contracted to obtain services would be treated as a consumer and could obtain the protection afforded by that section…".*

No "strong reasons" to refuse grant of an injunction

In accordance with the House of Lords decision in *Donohue v Armco Inc* [2001] UKHL 64, the court will ordinarily restrain proceedings in foreign courts commenced in breach of arbitration or exclusive jurisdiction clauses unless the respondent can establish that there are *"strong reasons"* for suing elsewhere.

Argyle argued that, even if it was bound by the arbitration agreements in the Engagement Letters, those agreements were between BDO Cayman and Argyle alone. Argyle argued that no injunction should issue because the New York Proceedings would continue in any event against the third parties, thereby giving rise to a multiplicity of proceedings and a risk of inconsistent judgments, which Argyle contended was a strong reason for the Grand Court not to exercise its discretion to restrain Argyle.

This argument also failed. Justice Parker held that the agreed dispute resolution procedure required that any claims against BDO Cayman or the third parties were required to be brought by arbitration against BDO Cayman alone in accordance with the Engagement Letters.

Argyle also argued that the New York Proceedings should be allowed to continue because Argyle could enter into conditional or contingent fee arrangements with its New York attorneys that would be impermissible in Cayman (which maintains the common law doctrines of maintenance and champerty). The judge held that this was not a proper basis upon which to commence proceedings in breach of an agreed dispute resolution procedure.

Conclusion

This judgment represents a robust and orthodox application of established principles whereby the Grand Court will enforce arbitration and exclusive jurisdiction clauses by injunction in the absence of strong reasons not to do so.

The judgment will be welcomed by auditors and other parties which routinely delegate responsibility for the performance of part of a contract within a group while seeking to maintain a single point of responsibility for the services via the use of a "sole recourse" or similar clause.

For Cayman liquidators, the judgment confirms they must have due regard to any agreed dispute resolution procedure in the contract on which they seek to sue. The Grand Court is alive to attempts to circumvent an agreed dispute resolution procedure with a view to achieving a strategic advantage and will hold parties to their contractual bargain.

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Campbells represented the successful applicant, BDO Cayman, in these proceedings. Please do not hesitate to contact the authors should you have any questions.

For more information concerning arbitration in the Cayman Islands, and its potential advantages, please click here.

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