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The Danger of Striking Blindly: Bermuda Court Rejects Strike-Out Application and Denies Arbitral Stay in Valuation Dispute

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*Walkers Bermuda, acting for a former shareholder of Meritus Trust Company Limited (the "**Defendant Company**"), successfully defended an application brought by the Defendant Company to strike out the Statement of Claim or, alternatively, to stay the proceedings in favour of arbitration.*

*The Supreme Court of Bermuda (the "**Court**") ruled in the former shareholder's favour, dismissing the Defendant Company's application in its entirety and ordering it to pay the former shareholder's costs.*

*Acting Justice Attride-Stirling's judgment[1] provides a helpful analysis of the factors which will be taken into account by the Court in exercising its jurisdiction to strike out a pleading pursuant to Order 18, Rule 19 of the Rules of the Supreme Court 1985 (the "**RSC**"). Attride-Stirling AJ's examination of the circumstances in which the Court will deem a litigant to have taken a "step" in proceedings, thereby depriving it of its right to seek an arbitral stay, is also instructive, as is the analysis of the circumstances in which a party may seek to challenge a valuation, notwithstanding an agreement to be bound by it.*

Striking out Pleadings under the RSC

In its Summons, the Defendant Company had sought orders pursuant to Order 18, Rule 19(1) of the RSC that the entirety of the Plaintiff's claims against it should be struck out, on the basis that they allegedly (i) disclosed no reasonable cause of action; (ii) were scandalous, frivolous or vexatious; and (iii) were an abuse of process of the Court.

Attride-Stirling AJ began his analysis of the relevant legal principles by referring to the Court of Appeal's examination of the approach to be taken, both as regards evidence and the consideration of the actual merits of the action, in *Broadsino Finance Company Limited v Brilliance China Automotive Holdings Ltd.*[2m] The general principles governing applications to strike out pleadings were recited by Stuart-Smith JA at pages 4 and 5 of that judgment, and for present purposes can be summarised as follows:

1. Randall Krebs v Meritus Trust Company Limited [2018] SC (Bda) 72 Civ (23 October 2018).
2. [2005] Bda LR 12.

1. if an application is made to strike out a pleading under only Order 18, Rule 19(1)(a) of the RSC (i.e. on the basis it discloses no reasonable cause of action), it is permissible only to look at the pleadings;
2. if the application is brought under the remaining, broader provisions of Order 18, Rule 19(1), the Court can admit and examine affidavit evidence;
3. the Court's jurisdiction to strike out a claim should only be exercised in "*plain and obvious cases*", particularly in circumstances where there has been no discovery or oral evidence given; and
4. the relevant test is whether there is a "*fair and reasonable probability of the defendants having a real or bona fide defence*" - the approach is the same as when a plaintiff is seeking summary judgment.

While Attride-Stirling J had little difficulty finding that the Defendant Company had failed to make out the first two grounds of its strike-out application, the question of whether the claim could be struck out on the basis it was an abuse of process required more consideration. Essentially, the Court was being asked to decide whether there had been a departure from the contractually agreed basis for the valuation of the Plaintiff's shares which were to be repurchased by the Defendant Company. The evidence before the Court was conflicting, with the Plaintiff's affidavit claiming there had been a departure, and the Defendant Company's affidavits claiming there had not. Recognising that there was a serious question of fact to be tried, Attride-Stirling AJ held:

> *"…[T]here is clearly a real dispute as to whether or not Canadian valuation principles were complied with. Given this, the valuation is not binding at this point. This type of factual determination should not be made on a strike out application. This is an issue to be determined by the trial judge having heard all the relevant evidence, including possibly expert testimony…The application to strike out is denied" (*emphasis added*).*

Challenging Share Valuations

At the heart of the dispute between the parties was a disagreement as to the price to be paid by the Defendant Company to the Plaintiff for the repurchase of the Plaintiff's shares in the Defendant Company. The parties had agreed that the purchase price for the shares was to be "*fair market value*", determined in accordance with "*Canadian generally accepted valuation principles*". The Plaintiff's case was that the valuation procured by the Defendant Company was not fair market value and had not been conducted in accordance with the standards of the Canadian Institute of Chartered Business Valuators (the "CICBV Standards").

Counsel for the Defendant Company relied on *Campbell v Edwards*[3] and *Jones & Ors v Sherwood Computer Services*[4] for the proposition that a party who agrees to be bound by a valuation is bound by it even if it is wrong, absent fraud. Counsel for the Plaintiff sought to distinguish those decisions from the case at bar. For example, unlike in *Campbell*, where the parties had agreed on the identity of the valuator, in this case there was a dispute as to the qualifications of the valuator chosen by the Defendant Company. Further, in *Campbell* there had been no agreement as to valuation methodology, whereas in this case the parties had agreed that the valuation be conducted in accordance with "*Canadian generally accepted valuation principles*", which the Plaintiff contended meant in accordance with the CICBV Standards.

Attride-Stirling AJ ultimately found the Plaintiff's arguments more compelling. Overall, the judge concluded that the question of whether the Defendant Company's valuator, Mazars, had performed the valuation correctly and in accordance with the terms of the contract with the Plaintiff was a question to be resolved at trial, including possibly with the benefit of expert testimony:

> *"…the Defendant was asking the court to decide, on the merits, whether the decision of the Valuator was binding. In order to decide this, the court would have to first decide whether all the conditions precedent for the Valuator's decision to be binding had occurred, including complying with the relevant binding Canadian valuation principles. Whether Duff & Phelps are correct in their statements and criticisms of the Mazars valuation is a question of fact which turns on a detailed consideration of the evidence and the law".*

3. (1976) 1 WLR 403.
4. (1992) 1 WLR 277.

The Alternative Application for an Arbitral Stay

An important question before the Court was whether the Defendant Company was debarred from relying upon what it said was a contractual agreement to arbitrate the dispute by virtue of it having already applied to strike out the Statement of Claim, which the Plaintiff argued constituted the taking of a "step" in the action.

Counsel for the Defendant Company relied heavily upon *Eagle Star Insurance Co Ltd v Yuval Insurance Co Ltd*, where a very strong English Court of Appeal led by Lord Denning MR opined that an application to strike out a statement of claim (on the facts of that particular case) was not to be held as taking a step in the action such as to preclude a party from applying to stay proceedings in favour of an arbitration, pursuant to an arbitration agreement[5].

Counsel for the Plaintiff also relied on *Eagle Star*, but sought to distinguish it from the case at bar. Specifically, it was noted that in *Eagle Star* the applicant had sought to strike out the claim only on the basis that the pleading itself disclosed no cause of action, and had not filed any evidence in support thereof. This was in stark contrast to the case which was before the Court, where the Defendant Company had sought to strike out the Statement of Claim based on the omnibus provisions of Order 18, Rule 19 of the RSC, and had filed multiple affidavits which addressed the perceived merits of the case.

Counsel for the Plaintiff also relied on *L Capital Jones Ltd v Maniach Pte Ltd*, i`n which the Singapore Court of Appeal conducted an exhaustive analysis of the various litigious manoeuvrings which could be said to constitute the taking of a "step" in an action.[6] Attride-Stirling AJ found the following passage of the 1992 English decision of *Blue Flame Mechanical Services Ltd v David Ford Engineering Ltd*, cited in L Capital, particularly instructive:

> *"(1) a step in the action which bars the defendant is something actually done or acquiesced in by him which is a significant procedural act in the case;*
>
> *(2) done with the intention of electing to litigate rather than stand on the right to arbitrate".*[7]

Having considered the relevant authorities, Attride-Stirling AJ concluded that in prosecuting its strike-out application, the Defendant Company had taken a "step" in the proceedings which precluded it from subsequently seeking a stay pending arbitration:

> *"So it seems that the correct legal position is that generally speaking, an application to strike out on technical grounds, including where a Statement of Claim clearly discloses no cause of action on its face, will not be a step in the action (see Eagle Star), but an application to strike out where the court is invited to consider evidence and make a decision on the merits, is to be considered taking a step in the action".*[8]

Practice Points

Strike-out applications are an important tool in a litigator's armoury, but they should be treated as a double-edged sword. While the achievement of a technical knock-out through a procedural shortcut can seem inviting at first glance, a strike-out which is brought without due consideration is likely to only delay proceedings and lead to adverse cost consequences. The remedy can cut both ways.

As a general rule, it is only the most exceptionally deficient cases - those which could be said to have only 'fanciful' prospects of success at best - which are liable to be struck out for failure to disclose a reasonable cause of action. Strike-out applications brought on the grounds that a pleading is vexatious or an abuse of process of the Court must be carefully thought out and properly particularised - while the Court will act to prevent its

5. [1978] 1 Lloyd's Rep 357.
6. (2017) 1 SLR 312 at [80].
7. [1992] 8 Const LJ 266, cited at paragraph 58 of Attride-Stirling AJ's decision.
8. Paragraph 65

machinery from being used as a means of vexation and oppression, it will do so only in the face of cogent evidence that the continuation of the proceedings would be manifestly unfair to a party to the litigation before it.

Litigants should also take care to avoid the situation where they deprive themselves of the opportunity to refer a dispute to arbitration by their engagement with the merits of the action in a strike-out application. As a general proposition, if a stay pending arbitration is the ultimate outcome sought, involvement with the litigious proceedings should be kept to a bare minimum.

Contacts

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