Is a receiver bound by an arbitration agreement?

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Summary

On June 10, 2021, the Supreme Court of Canada (SCC) granted leave to appeal the decision of the British Columbia Court of Appeal in *Petrowest Corporation v Peace River Hydro Partners*, 2020 BCCA 339. The main issue in this case is the enforceability of arbitration agreements as against a court-appointed receiver. Here, the court-appointed receiver brought a claim against the appellants arising out of contracts between the appellants and the debtor. The appellants responded by applying for a stay of the litigation pursuant to section 15 of the (then) *Arbitration Act,* RSBC 1996, c. 55 (the *Arbitration Act*), on the basis that the contracts contained arbitration agreements. The chambers judge concluded the receiver was bound by the arbitration clauses, but exercised "inherent jurisdiction" to allow the litigation to proceed. The British Columbia Court of Appeal (BCCA) dismissed the appeal, but for different reasons, finding that the receiver was not bound by the arbitration agreements and could disclaim the arbitration agreements while still suing on the substantive provisions of the contracts. In arriving at such decision, the BCCA applied the well-established principle of separability in arbitration.

The SCC will now have the final word on:

- whether a receiver is bound by an arbitration clause, while adopting and suing on the balance of the contract;
- whether a receiver's disclaimer power applies to arbitration clauses; and/or
- whether inherent jurisdiction applies to override a binding arbitration agreement.

As such, this case will have important implications for insolvency and arbitration practitioners alike.

Background

Before the insolvency proceedings, Peace River Hydro Partners (PHRP) subcontracted certain work for a construction project to Petrowest Corporation (Petrowest). Petrowest became insolvent and the Alberta Court of Queen's Bench appointed Ernst & Young Inc

as receiver (the Receiver). The Receiver then sued PHRP, claiming that amounts were owing under contracts between Petrowest and PHRP. The contracts contained mandatory arbitration agreements. The litigation was commenced in British Columbia where the project was located.

In response, PHRP applied to the BC Supreme Court for an order staying the court action pursuant to section 15 of the *Arbitration Act*, which states that if a party to an arbitration agreement commences court proceedings, the other party may apply to that court to stay the court proceedings. Pursuant to section 15, the court "must" make an order staying the court proceedings, unless the arbitration agreement is found to be void, inoperative or incapable of being performed.[1]

In reasons indexed at 2019 BCSC 2221, Madam Justice Iyer of the BC Supreme Court (the Chambers Judge) dismissed PHRP's stay application, and allowed the Receiver to continue the court action.

The Chambers Judge found that the receiver was a party to the arbitration agreements, which were valid and thus that section 15 of the *Arbitration* was "engaged".

Despite this, the Chambers Judge concluded that the court had discretion to refuse to stay the court proceedings, pursuant to section 183 of the *Bankruptcy and Insolvency* Act, RSC 1985, c. B-3 (BIA). That provision provides that Canada's superior courts are vested with "such jurisdiction at law and in equity" as will enable them to exercise jurisdiction in proceedings under the BIA. The Chambers Judge concluded that section 183 gave the court the "inherent jurisdiction" to control its own processes and to avoid the operation of section 15 of the *Arbitration Act*. The Chambers Judge reasoned that such a result was appropriate, given that there was a benefit to the insolvency proceedings as a whole, through avoiding multiple proceedings and the related delay and cost.

BCCA decision

PHRP then sought and was granted leave to appeal the decision of the Chambers Judge to the BCCA. The BCCA began its analysis by cautioning that "inherent jurisdiction" under the BIA should not be used to negate express legislative requirements, such as section 15 of the *Arbitration Act*.

However, the BCCA focused its analysis on whether section 15 of the *Arbitration Act* was engaged at all. Unlike the Chambers Judge, the BCCA explained that the Receiver is an officer of the court and owes fiduciary duties to all stakeholders. Thus, the Receiver does not bring litigation on behalf of or as agent for the debtor, but rather in "fulfillment of its own court-authorized and fiduciary duties". Accordingly, the BCCA held that the Receiver is not party to and not bound by arbitration agreements entered into by the debtor pre-insolvency.

Further, the BCCA held that even if the Receiver seeks to sue on contracts containing arbitration agreements, as was the case here, the Receiver is still not required to arbitrate. Rather, the Receiver is entitled to disclaim an arbitration agreement and rely on the substantive provisions of the contracts. According to the BCCA, this follows from

the well-established doctrine of “separability”, namely that arbitration clauses are independent agreements that are not merged into the underlying contract.

Ultimately, the BCCA concluded that the Receiver was entitled to litigate the claims against PHRP and upheld the Chamber Judge’s decision. Unlike the Chamber’s Judge, the BCCA did not rely on the court’s “inherent jurisdiction” and continued the trend of appellate courts limiting the scope of “inherent jurisdiction” under the BIA.

Looking ahead

On June 10, 2021, the SCC granted leave to appeal the decision of the BCCA. It is expected that the SCC will now clarify such issues as when a receiver may disclaim an arbitration agreement, the role of the receiver as an officer of the court, and the doctrine of separability in Canada, among other things. Although the SCC had the opportunity to explain disclaimers in the context of regulatory obligations in *Orphan Well Association, et al. v. Grant Thornton Limited*, 2019 SCC 5, this case will be an important opportunity for the SCC to opine on the disclaimer power outside of the environmental context. It is also an opportunity for the SCC to comment on “inherent jurisdiction”.

In the meantime, receivers appear at liberty to disclaim pre-insolvency arbitration agreements. This approach is persuasive given that arbitration is fundamentally premised on party autonomy and a court-appointed receiver is a stranger to that agreement.

[1] As a result of BC enacting a new arbitration legislation after this litigation arose (the *Arbitration Act*, SBC 2020, c 2) section 15 is now section 7 of the new BC *Arbitration Act*.

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