SOUTH CHINA MORNING POST

18 Nov. 1988

500 may be sued over futures deals

6.1

BY LINDY COURSE

A HIGH Court judge yesterday declared that trading in Hang Seng Index Futures contracts was legal, paving the way for Hongkong brokers to sue hundreds of their clients who defaulted on their margin calls in the wake of last year's market crash.

A vegetable wholesaler, Mr Keung Chak-kiu, had hoped to persuade the judge that investing in futures contracts was gambling, which was illegal under the 1710 Gaming Act.

Mr Keung was being sued by his broker, Richardson Greenshields of Canada (Pacific) Limited, for $537,000 plus interest. He had argued the payment of margin by cheque brought the transaction within the Gaming Act so the contract was void.

If the judge had ruled in his favour it would have allowed hundreds of investors to escape paying their debts to their brokers.

But yesterday Judge Raymond Sears ruled that payment of margins by cheque did not mean trading was gambling.

After ruling that contracts were legal the judge then lifted a stay on all actions where brokers were suing their clients for losses after the crash on the world stock markets in October 1987. In all the cases the defendants had lodged the same defence as Mr Keung.

More than 500 cases involving millions of dollars, which had been stayed pending the outcome of the test case, could now proceed to trial.

Hongkong has strict rules covering gambling and punters are only allowed to bet on horse racing and buy lottery tickets.

Before last year's crash, thousands of people invested heavily in the futures market, often buying without having the full amount for settlement available.

When the market crashed, many were caught short and more than 30 commission houses defaulted. The Government was forced to put together an emergency $4 billion rescue package with the help of British merchant bankers.

● Market reaction – Business Post

In futures trading, investors buy or sell a commodity at a future date, but fix the price at the time of the deal.

In the feverish atmosphere of the month preceding the October crash, 601,005 lots were traded. Now the monthly average is 15,000 lots.

While it was agreed the defendant was a pure speculator, and therefore was gambling, the judge said the contracts were genuine commercial transactions conducted openly on a controlled exchange where what was being traded was known to everyone.

He went on to say paying the margin by cheque in no way invalidated contracts between brokers and clients.

"If the client's account is in debit he can be sued for the balance and if he is in credit he can sue the broker," he said.

He said what occurred either on the exchange floor or between broker and client was not gaming, nor could it be classified as gambling.

The judge added that provision of regulated financial markets was of fundamental importance in communities such as Hongkong. This particular market had been conducted in an open, well publicised manner.

He pointed out it was only after the October market crash that investors began to look for ways to escape paying their margin calls and came up with the gambling defence.

The element of risk involved did not convert a financial transaction into gambling, the judge said.

"Similarly an uninformed person might describe activities on the exchange as a casino because there is a risk of losing as well as the opportunity of winning but that doesn't mean what is actually occurring is gambling," he said.

The ruling was applauded by futures Exchange chief executive Douglas Ford and futures brokerages.

They said a major obstacle to the revival of the local futures market was now removed.

Said Mr Ford: "Obviously the judgement, which is very clearly in favour of the exchange and the contract, will remove any cloud or concern that the new members or even the present members have in promoting the futures contracts of the exchange."