CACV 611/2018
[2019] HKCA 873

IN THE HIGH COURT OF THE

HONG KONG SPECIAL ADMINISTRATIVE REGION

COURT OF APPEAL

CIVIL APPEAL NO 611 OF 2018

(ON APPEAL FROM HCSD NO 5 OF 2017)

IN THE MATTER of an application to set aside a Statutory Demand under Rule 47 of the Bankruptcy Rules (Chapter 6A)

BETWEEN

BUT KA CHON	Applicant
and	
INTERACTIVE BROKERS LLC	Respondent

Before: Hon Kwan VP, Cheung JA, Chu JA in Court
Date of Hearing: 23 July 2019
Date of Judgment: 2 August 2019

J U D G M E N T

Hon Kwan VP:

1. This is an appeal by the applicant But Ka Chon against the decision of Deputy High Court Judge Yee handed down on 4 December 2018. By the decision, the judge dismissed

Mr But's application to set aside the statutory demand issued by Interactive Brokers LLC ("IB") against him on 23 November 2016 for a debt of $79,334,912.39.

2. After the dismissal of Mr But's application, IB presented a bankruptcy petition against him on 21 December 2018 (HCB 7426/2018). Upon the joint application of Mr But and IB by way of consent summons, Deputy High Court Judge Leung made an order on 6 March 2019 that all further proceedings in the bankruptcy of Mr But be stayed pending the determination of this appeal.

Background

3. The relevant background matters may first be stated as follows.

4. IB is an online broker-dealer providing a platform for online trading in, among other things, currency futures. Mr But was and is an experienced trader, and had dealt in securities and the like, including futures, as an individual investor since 1994. His records with the Hong Kong Monetary Authority showed that he has been a licensed professional in various areas including dealing in securities under the Securities and Futures Ordinance, Cap 571.

5. In July 2012, he visited the website of IB and entered into a customer agreement dated 18 July 2012 ("the Customer Agreement"), by which he opened an online portfolio margin account ("the Account") with IB. He was then invited by IB to attend its Hong Kong office for IB to verify his personal data including his identity and income proof. He did

so on 31 July 2012 and signed a document known as "Acknowledgment by Customers" ("the Acknowledgment").

6. After opening the Account, Mr But traded in Euro/Swiss Franc ("CHF") futures. He opened his RFH5 positions, ie March 2015 futures traded under the symbol "RHF5" on the Chicago Mercantile Exchange ("CME") on margin through IB. Those positions were established with a view to a profit from the relationship between the Euro and CHF and were long positions, meaning that he purchased them to open the positions. With those positions, he would profit if the Euro increased in value compared to CHF and suffer loss if CHF increased in value compared to the Euro.

7. On 15 January 2015 at around 17:20 hours Hong Kong time, the Account had, *inter alia*, 440 long position RHF5 and the Account had an equity or net liquidation value of approximately $19,930,000. At around 17:30 hours, the Swiss National Bank unexpectedly cancelled its 2011 policy which placed a ceiling of 1.2000 CHF per Euro after the Eurozone debt crisis saw investors rush to CHF assets. The unpegging of the CHF/Euro exchange rate ("the Unpeg Event") resulted in a record high for CHF against the Euro in the cash market. After the Unpeg Event, the net liquidation value of the Account was at negative $83,480,610.18. Due to the volatility of the market, CME halted trading of RFH5 contracts and took other emergency measures a few times. At 18:22 hours, IB sent an email to Mr But[1] informing him that the equity in the Account was insufficient to satisfy Maintenance Margin[2]. At 19:47

[1] Mr But was apparently aware of the Unpeg Event. He had logged into the Account immediately after the Unpeg Event (at 17:32:55 and at 17:33:31) and after IB's first email to him that day (at 18:24:09).

[2] The minimum amount of margin equity that must be maintained for an investor to maintain his positions in his account.

hours, IB informed him by email there had been a substantial move in CHF assets due to the Unpeg Event and liquidation had been disabled. Mr But did not deposit any funds into the Account to resolve the margin deficit.

8. On 16 January 2015, IB sent an email to notify Mr But that the margin deficit rose to $92,078,384.27 and that IB would attempt to liquidate positions in the Account. By a subsequent email from IB the same day, he was informed that the available capital in the Account was negative $73,888,802.50. IB started liquidating Mr But's Hong Kong stocks in the Account.

9. On 21 January 2015, with the permission of CME pursuant to its rules, IB started liquidation of the RFH5 positions held by Mr But and those of its other margin clients by transferring the positions to an affiliate of IB.

10. Mr But sent an email to IB on the same day complaining of improper handling of its liquidation policy to the Account, thereby causing the huge loss of his portfolio. IB responded by letter on 18 February 2015 stating that his complaint was not factually or legally justified in that he had misstated its liquidation policy and ignored the nature of the market event that caused his losses. The letter ended with the statement that if Mr But was dissatisfied with IB's response, he "may escalate [his] complaint to the Financial Dispute Resolution Centre or to the Hong Kong Securities and Futures Commission."

11. On 23 November 2016, IB issued a statutory demand to Mr But for $79,334,912.39, being the deficit in the Account and interest at margin interests rates. It was served on him on 12 December 2016.

12. On 16 December 2016, Mr But's solicitors wrote to IB's solicitors disputing the debt in the statutory demand and stating that they "further note clause 33 of the [Customer Agreement] contains a Mandatory Arbitration Clause on any and all disputes between the parties arising out of the Customer Agreement. As per the said clause, we are further instructed to initiate arbitration between the parties on the said disputes." IB's solicitors were requested to withdraw the statutory demand and revert as to whether they had instructions "to accept service of our client's Notice of Arbitration".

13. IB's solicitors replied by letter dated 22 December 2016 stating there were no grounds for a bona fide dispute to be resolved by arbitration and that if a dispute did exist such that it should be referred to arbitration, the arbitration must occur in one of the five specified forums. IB's solicitors attached the rules of arbitration of all five forums for the reference of Mr But's solicitors.

14. On 13 January 2017, Mr But took out his application to set aside the statutory demand. It was heard by the judge a year later on 13 February 2018. He directed the parties to file further submissions in April 2018 after his attention was drawn to a judgment handed down by Harris J in *Re Southwest Pacific Bauxite (HK) Ltd* [2018] 2 HKLRD 449 ("the *Lasmos* case") on 2 March 2018.

The decision below

15. Two broad grounds were relied on to set aside the statutory demand.

16. First, Mr But alleged that IB made misrepresentations relating to its risk management policies or obligations on its webpage. He had relied on such misrepresentations to enter into the Customer Agreement and they turned out to be false. Had the risk management policies been put into practice, the alleged debt would not have been incurred. Hence, the alleged debt is disputed on substantial grounds and he has a cross-claim for the net liquidation value in the Account, thereby meeting the requirements of rules 48(5)(a) and (b) of the Bankruptcy Rules, Cap 6A[3].

17. Second, Mr But relied on the arbitration clause in clause 33B of the Customer Agreement[4]. The parties' dispute should be arbitrated and the arbitration clause provides a ground for the court to exercise its residual discretion to set aside the statutory demand pursuant to rule 48(5)(d) of the Bankruptcy Rules, by which the court is empowered to do so upon being "satisfied, on other grounds, that the demand ought to be set aside." The circumstances which normally will be required before a court can set aside a demand under rule 48(5)(d) are circumstances which would make it unjust for the demand to give rise to those consequences in a particular case[5].

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[3] The relevant provisions in rule 48(5) read as follows:
"The court may grant the application if – (a) the debtor appears to have a counterclaim, set-off or cross demand which equals or exceeds the amount of the debt or debts specified in the statutory demand; (b) the debt is disputed on grounds which appear to the court to be substantial; … or (d) the court is satisfied, on other grounds, that the demand ought to be set aside."

[4] The relevant part of clause 33 reads: "B. Customer agrees that any controversy, dispute, claim, or grievance between IB, … on the one hand, and Customer … on the other hand, arising out of, or relating to, this Agreement, or any account(s) established hereunder in which securities may be traded; any transactions therein; any transactions between IB and Customer; any provision of the Customer Agreement or any other agreement between IB and Customer; or any breach of such transactions or agreements, shall be resolved by arbitration, in accordance with the rules then prevailing of any one of the following: (a) The American Arbitration Association; (b) The Financial Industry Regulatory Authority; or (c) any other exchange of which IB is a member, as the true claimant-in-interest may elect. If Customer is the claimant-in-interest and has not selected an arbitration forum within ten days of providing notice of Customer's intent to arbitrate, IB shall select the forum. …"

[5] *Re a Debtor (No 1 of 1987)* [1989] 1 WLR 272 at 276

18. On the misrepresentation claim, the judge took the view it is "thoroughly bad and has no merit". Mr But failed to show that he has a bona fide defence by way of misrepresentation with credible and cogent evidence to the claim of IB in respect of the debt, and his cross-claim based on the same complaint is "equally illusory." He held that Mr But is unable to meet the thresholds in rules 48(5)(a) and (b)[6].

19. For the arbitration issue[7], the judge noted that the decision of Harris J in the *Lasmos* case made a substantial departure from previous authorities at first instance in Hong Kong (*Hollmet AG & Anr v Meridian Success Metal Supplies Ltd* [1997] HKLRD 828, Rogers J; *Re Sky Datamann (Hong Kong) Ltd*, HCCW 487/2001, 29 January 2002, Yuen J; *Re Jade Union Investment Ltd*, HCCW 400/2003, 5 March 2004, Barma J; *Re Southern Materials Holding (HK) Co Ltd*, HCCW 281/2007, 13 February 2008, Kwan J; and *Re Quiksilver Glorious Sun JV Ltd* [2014] 4 HKLRD 759, Harris J) and followed the approach of the English Court of Appeal in *Salford Estates (No 2) Ltd v Altomart Ltd (No 2)* [2015] Ch 589.

20. By the new approach in *Lasmos*, which was set out in §31 of that case, it was held that a petition to wind up a company on insolvency grounds should "generally be dismissed" when these three requirements are met:

> "(1) if a company disputes the debt relied on by the petitioner;
>
> (2) the contract under which the debt is alleged to arise contains an arbitration clause that covers any dispute relating to the debt; and

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6 Decision, §45

7 As noted in the Decision at §46, there is no controversy that the dispute about the liability of Mr But arising from the Account falls within the ambit of the arbitration clause and there is no dispute about the validity of this provision.

> (3) the company takes the steps required under the arbitration clause to commence the contractually mandated dispute resolution process (which might include preliminary stages such as mediation) and files an affirmation in accordance with r 32 of the Companies (Winding-up) Rules, Cap 32H, demonstrating this".

21. The effect of this approach is that the company is entitled to have the petition dismissed without having to show that the petitioning debt is bona fide disputed on substantial grounds. Where there is an arbitration clause, it is sufficient to show that the debt is "disputed" and for that it is sufficient to show the debt is not admitted (*Eco Measure Market Exchange Ltd v Quantum Climate Services Ltd* [2015] BCC 877 at §10).

22. The judge found the new approach in *Lasmos* to be "inapplicable in any event", as his conclusion on the bona fides of Mr But's dispute over the alleged debt was "sought by both parties". He had found against Mr But on this issue and there was no genuine dispute to be arbitrated, it follows that the arbitration clause should have no relevance and it was unnecessary to comment on the soundness of the reasons supporting the new approach[8].

23. If he was wrong about this and the new approach should be taken, he found that the application to set aside the statutory demand should still be refused for want of the fulfilment of the third requirement in *Lasmos*, in that Mr But had not taken any steps to commence the contractually mandated dispute resolution. The judge did not accept that Mr But has any genuine intention to commence arbitration[9].

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[8] Decision, §§65 to 69, 82
[9] Decision, §§70, 78, 82

24. For these reasons, whichever approach was adopted the mere existence of the arbitration clause cannot assist Mr But and the judge declined to exercise the residual discretion to set aside the demand under rule 48(5)(d)[10].

This appeal

25. Mr Tony Ko[11], who appeared for Mr But here and below, sought to challenge the decision on all the above holdings. He raised three broad grounds of appeal.

26. The first two grounds concern the judge's evaluation of the evidence on the misrepresentation claim. The first relates to the contention that a reasonable person would have understood the alleged representations to mean that IB had an obligation and not a discretion to liquidate positions without notification to the investor. The second attacks the finding of the absence of cogent evidence that IB could have liquidated the positions of Mr But earlier.

27. The third ground relates to the contention that the judge should have exercised the residual discretion in rule 48(5)(d) on the ground that the dispute should go to arbitration and the approach in *Lasmos*, which followed *Salford*, should be adopted, and that the judge was in error in finding that Mr But had failed to take steps to commence arbitration.

28. Mr Ko confirmed his reliance on rules 48(5)(a) and (b) as independent and separate grounds to set aside the statutory demand, in addition to rule 48(5)(d). He also accepted that to meet the threshold

[10] Decision, §83
[11] With Mr Kong Cheuk Wing

test for rules 48(5)(a) and (b), it is incumbent on the applicant to establish a bona fide dispute on substantial grounds in that there is actually a defence of substance and that there is a genuine and serious cross-claim. So whatever may be the standard in establishing a dispute for the purpose of seeking the exercise of the residual discretion under rule 48(5)(d), it is still necessary to consider the misrepresentation claim with regard to the test of bona fide dispute on substantial grounds.

The misrepresentation claim

29. There is no dispute as to the law regarding what is required to establish misrepresentation in the present context. The court has to consider what a reasonable person would have understood from the words used in the context in which they were used, and this may depend on the nature and content of the statement, the context in which it was made, the characteristics of the maker and of the person to whom it was made, and the relationship between them. It is also necessary for the statement relied on to have the character of a statement upon which the representee was intended, and was entitled, to rely. In some cases, the statement in question may have been accompanied by other statements by way of qualification or explanation which would indicate to a reasonable person that the putative representor was not assuming a responsibility for the accuracy or completeness of the statement or was saying no reliance can be placed upon it. The claimant must show that he in fact understood the statement in the sense which the court ascribes to it and that, having that understanding, he relied on it. And the claimant must show that the

representation played a real and substantial part in inducing him to enter into the contract[12].

30. These statements on the IB webpage ("the Representations") were relied on to mount a case in misrepresentation:

> "Risk Management … Real-time monitoring systems help you understand and manage your own trading risk at any moment of the day so you can react quickly to changes in the market. *Real-time margining continuously enforces limits for each account, automatically liquidating positions if any individual account violates its limits at any time*."
>
> "Securities Initial and Maintenance Margin … *IB generally will not issue margin calls and will liquidate account positions in order to satisfy Margin Requirements without prior notice*. … IBHK Real-Time Margining. We use real-time margining to allow you to see your trading risk at any moment of the day. Our real-time margin system applies margin requirements throughout the day to new trades and trades already on the books and enforces initial margin requirements at the end of the day, with *real-time liquidation of positions instead of delayed margin calls*. This system allows us to maintain our low commissions because we do not have to spread the cost of credit losses to customers in the form of higher costs."
>
> "Soft Edge Margining. *We will automatically liquidate when an account falls below the minimum margin requirement*. However, to allow a customer the ability to manage risk prior to a liquidation, we calculate Soft Edge Margin (SEM) during the trading day. From the start of the trading day until 15 minutes before the close of the trading day, Soft Edge Margin allows for an account's margin deficit to be within a specified percentage of the account's Net Liquidation Value, currently 10%. … *If an account falls below the minimum maintenance margin, it will not be automatically liquidated until it falls below the Soft Edge Margin*."
>
> (Emphasis supplied.)

31. In gist, it was contended on behalf of Mr But that a reasonable person would have understood from the Representations that IB had a risk management policy and an obligation to liquidate positions

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[12] *Raiffeisen Zentralbank Osterreich AG v Royal Bank of Scotland* [2011] 1 Lloyd's Rep 123 at §§82, 83, 86, 87, 153

automatically if any account violates its limit at any time and would perform auto-liquidation to assist its customers to manage risk and exposure. The Representations were untrue in that IB had failed to auto-liquidate his positions on 15 January 2015, when his account fell below the CME and IB's Maintenance Margin or the Soft Edge Margin. Had IB carried out its obligation to auto-liquidate between 17:30:49 and 17:31:29 on 15 January, the Account would have been left with a net liquidation value above $2,903,613 and the debt in the statutory demand would not have arisen[13].

32. The Representations must be read in context with regard to other statements on the webpage as a whole. I set out below the entirety of the relevant paragraphs on the same webpage to give proper context to the second of the Representations relied upon:

> "Securities Initial and Maintenance Margin
>
> …
>
> Once an investor has started buying a stock on margin, it is required that a minimum amount of equity be maintained in the investor's margin account. This is called the maintenance margin. When the balance in the margin account falls below the maintenance requirement, *the broker can issue a margin call* requiring the investor to deposit more cash, or the broker can liquidate the position. IB *generally* will not issue margin calls and will liquidate account positions in order to satisfy Margin Requirements without prior notice. If you are trading in a Margin Account, you must ensure that you have sufficient equity in the account at all times.
>
> Not all securities can be bought on margin. Buying on margin is a double-edged sword that can translate into bigger gains or bigger losses. *In volatile markets, investors who borrowed from their brokers may need to provide additional cash if the price of a stock drops too much for those who bought on margin* or rallies too much for those who shorted a stock. In such cases, brokers are also allowed to liquidate a position, even without informing the investor. Real-time position

[13] 1st affirmation of But Ka Chon, §36; 3rd affirmation of But Ka Chon, §24

> monitoring is a crucial tool when buying on margin or shorting a stock."
>
> "Disclosures
>
> In the interest of ensuring the continued safety of its clients, *the broker may modify certain margin policies to adjust for unprecedented volatility in financial markets.* The changes will promote reduction of leverage in client portfolios and help ensure that clients' accounts are appropriately capitalized."
>
> (Emphasis supplied)

33. In respect of the third of the Representations under the heading "Soft Edge Margining", it is pertinent to note this paragraph which follows immediately the parts quoted:

> "Please note that we reserve the right to restrict soft edge access on any given day, and may eliminate SEM completely in times of heightened volatility."

34. Even without taking into consideration the other documents to be mentioned, the judge took the view that on a fair reading of the Representations in context with other relevant statements on the webpage as set out above, a reasonable person would have understood the Representations to mean that IB can either issue a margin call or liquidate the position when the balance in a margin account falls below the maintenance requirement. The Representations cannot reasonably be understood to mean that with the right to liquidate positions automatically without prior notice, IB gives up its right to make margin calls altogether[14]. And it is absurd for margin traders to expect or even insist when they cannot meet the maintenance margin, there should never be margin calls and the broker will be obliged to liquidate their positions without prior notice, because if traders are able to deposit extra funds into their accounts pursuant to margin calls, their margins can be brought in line with the maintenance requirement so if the market should go up later

[14] Decision, §32

they may suffer no loss in the end whereas financial loss will be incurred if their positions are automatically liquidated without notice[15].

35. The judge further held[16] that Mr But could not possibly and reasonably have relied on the Representations in view of the terms of the Customer Agreement, which Mr But was allowed to read at his leisure before he signed it online[17].

36. There is express provision in the Customer Agreement that makes it clear IB has the right, in its sole discretion, not to carry out the liquidation of positions in a customer's account[18]. The provision concerning the liquidation of positions appears under "Margin" in clause 11 and the relevant parts read as follows (with certain parts printed in block letters and in bold as per the document):

> "**B. Requirement to Maintain Sufficient Margin Continuously**: … **IB MAY MODIFY MARGIN REQUIREMENTS FOR ANY OR ALL CUSTOMERS FOR ANY OPEN OR NEW POSITIONS AT ANY TIME, IN IB'S SOLE DISCRETION**. …
>
> …
>
> **D. Liquidation of Positions and Offsetting Transactions**:
>
> **i. IF AT ANY TIME CUSTOMER'S ACCOUNT HAS INSUFFICIENT EQUITY TO MEET MARGIN REQUIREMENTS OR IS IN DEFICIT, IB HAS THE RIGHT, IN ITS SOLE DISCRETION, BUT NOT THE OBLIGATION, TO LIQUIDATE ALL OR ANY PART OF CUSTOMER'S POSITIONS IN ANY OF CUSTOMER'S IB ACCOUNTS, INDIVIDUAL OR JOINT, AT ANY TIME AND IN ANY MANNER AND THROUGH ANY MARKET OR DEALER, WITHOUT PRIOR NOTICE OR MARGIN CALL TO CUSTOMER. CUSTOMER**

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15 Decision, §35

16 Decision, §41

17 The Customer Agreement was executed by Mr But electronically on 18 July 2012 at 02:39:46.0 by clicking the relevant button on the IB website, typing his signature and sending it via the internet.

18 For present purpose, the judge did not take into account clauses 1 (which provides that in the event of disparity between the Customer Agreement and the IB website, the agreement controls) and 32B (the entire agreement provision), see Decision §44.

> **SHALL BE LIABLE AND WILL PROMPTLY PAY IB FOR ANY DEFICIENCIES IN CUSTOMER'S ACCOUNT THAT ARISE FROM SUCH LIQUIDATION OR REMAIN AFTER SUCH LIQUIDATION. IB HAS NO LIABILITY FOR ANY LOSS SUSTAINED BY CUSTOMER IN CONNECTION WITH SUCH LIQUIDATIONS (OR IF THE IB SYSTEM DELAYS EFFECTING, OR DOES NOT EFFECT, SUCH LIQUIDATIONS) EVEN IF CUSTOMER RE-ESTABLISHES ITS POSITION AT A WORSE PRICE.**
>
> …
>
> iii. If IB does not, for any reason, liquidate under-margined positions, and issues a margin call, Customer must satisfy such call immediately by depositing funds. Customer acknowledges that even if a call is issued, IB still may liquidate positions at any time."

37. What is more, Mr But had signed these additional documents either manually or electronically:

(1) When he attended the office of IB on 31 July 2012, he signed the Acknowledgment manually to acknowledge *inter alia* that he had "read carefully the IB Customer Agreement", that he had received the Customer Agreement, and that he agreed to electronically sign additional documents included during the account opening process.

(2) Of the documents he signed electronically during the account opening process on 18 July 2012, there was a document headed "Legal Acknowledgment" "Essential Legal Terms for your IB Account". Mr But clicked the box for "Accept" under each term[19] and one of them read as follows:

> "IB generally does not make margin calls, and IB maintains the right to immediately close out positions, without notice or

[19] The document was acknowledged by Mr But electronically on 18 July 2012 at 02:39:47.0.

> liability, in any account that does not have sufficient funds to meet the margin requirements imposed by it or regulatory authorities. At its sole discretion given the market or other factors, IB may choose to make a margin call and/or may not liquidate account positions. If you receive a margin call you are required to immediately deposit funds to cover the deficiency."

38. Whether Mr But can recall the documents he signed or whether he had read the documents before he signed is immaterial, and it is unnecessary for Mr But's assertion to be tested by oral evidence, as Mr Ko has contended. As a person of full age and understanding, the signatures Mr But appended to those documents which purported to have legal effect signified his assent or adherence to what the documents stated.

39. Mr Ko submitted that when the Representations are read with the other statements on the webpage as a whole, this should reinforce his contention that a reasonable person would think that IB would perform auto-liquidation to assist its customers to manage risk and exposure. Nowhere on the webpage was it stated that IB has a discretion not to perform auto-liquidation even when the Soft Edge Margin was not met. And he argued that the flexibilities are explicitly for ensuring the continued safety of the customers, not of the broker, by reducing leverage in performing auto-liquidation earlier.

40. I do not accept his submission. I agree with the judge that a reasonable person, let alone an experienced trader with Mr But's qualifications, would have understood the Representations in the proper context to mean that IB had an absolute obligation and not merely a discretion to liquidate positions without prior notice regardless of the circumstances. It is immaterial that unlike clause 11 of the Customer Agreement, the webpage did not actually say that IB had a discretion but

not an obligation to liquidate positions. Nor do I think it significant that the modification of margin policies was stated to be "in the interest of ensuring the continued safety of its clients" and was to "promote reduction of leverage in client portfolios".

41. The language used in the webpage is sufficiently clear. IB had a discretion whether to make a margin call or liquidate positions, and would "generally" exercise the discretion to liquidate positions, but it was given flexibility as to the approach to margin in expressly stating that IB "may modify margin policies to adjust for unprecedented volatility in financial markets". The stated objectives of modifying margin policies are to ensure the continued safety of its clients, to promote reduction of leverage in client portfolios and to help ensure that clients' accounts are appropriately capitalized. But this is not to say that such objectives are envisaged to be met in all circumstances by performing auto-liquidation of positions without prior notice. There was no clear or unequivocal representation that upon a margin deficit arising, IB was obliged to liquidate positions automatically and immediately.

42. Clause 11 of the Customer Agreement and the relevant legal term accepted by Mr But would make the position even clearer, as they spelt out expressly that IB had sole discretion to make margin calls and might not liquidate account positions without notice. Mr Ko submitted that the provisions of the Customer Agreement are irrelevant because if the court should find a case of misrepresentation, this would be a vitiating factor and the agreement would not be binding.

43. I also reject this submission. It is tantamount to saying that having read the margin webpage and having been induced by some of its

contents to enter into contractual relationship with IB, Mr But could simply ignore the contents of the legal terms he was requested to accept or decline as well as the contents of the Customer Agreement, notwithstanding that the relevant parts of the agreement on modifying margin requirements were printed in block letters and in bold. The proposition has only to be stated to be rejected. It is difficult to see what the misrepresentation was in this instance.

44. Mr Ko sought to attack the judge's finding that Mr But could not possibly have relied on the Representations, given his qualification and experience and the fact that he was allowed to read the terms of the Customer Agreement at his leisure before he signed. He cited *Ming Shiu Chung & Ors v Ming Shiu Sum & Ors* (2006) 9 HKCFAR 334 for his proposition that a person can rely on misrepresentation to vitiate a contract even where he signed without reading the full terms.

45. The case cited is no support for this startling proposition, see §§84 to 87. Ribeiro PJ was at pains to emphasise that even though it is an everyday occurrence that people sign documents without reading or without actually knowing the terms or the full terms, they are held to the documents they have chosen to sign unless there is a recognised legal basis for concluding that their apparent consent has been in some way vitiated. The facts constituting the vitiating factor must be established. If Mr But chose not to read or to read carefully the documents he signed (he acknowledged clause 11 is contrary to the Representations[20]), it is difficult to see how the parts of the webpage he did read would constitute misrepresentation.

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[20] Decision, §20

46. In passing, I note that there have been a number of arbitration and court proceedings[21] brought by other customers of IB and its affiliates, alleging failure to liquidate positions in a timely manner after the Unpeg Event. All of them have been resolved in IB's favour, upholding the broad authority of IB to manage margin trading accounts under the Customer Agreement.

47. The above deals with the first ground of appeal. It is not necessary to deal with the second ground of appeal which sought to address the finding of the lack of cogent evidence that IB could have ever liquidated the positions in the Account any earlier and that there is no substance in Mr But's complaint about IB's commencement of liquidation on 21 January 2015 but not any earlier[22]. As I am in agreement with the judge the misrepresentation claim is without merit, there is no need to resolve the issue whether it was feasible for IB to liquidate Mr But's positions more quickly than it did.

48. For the above reasons, I uphold the ruling that the threshold requirements for setting aside the statutory demand under rules 48(5)(a) and (b) are not met.

49. I turn to consider the remaining ground to set aside the demand under rule 48(5)(d), which is on the premise that it would be unjust to allow a bankruptcy petition to be presented as the dispute should go to arbitration pursuant to clause 33B in the Customer Agreement. The judge had decided irrespective of which approach is followed

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[21] 1st affirmation of Daniel A Spector, §§42 to 47, who deposed to proceedings that had been concluded up to June 2017: an arbitration award of the Financial Industry Regulatory Authority in the USA entitled *Gregory Scott Cahill & Anr v IB* dated 5 May 2016; a decision of the Financial Ombudsman Service in England of a customer against Interactive Brokers (UK) Ltd dated 12 December 2016; a class action judgment of the United States District Court, District of Connecticut, in *Robert Scott Batchelor v IB & Ors* dated 28 September 2016.

[22] Decision, §§38, 39, 42

(whether *Lasmos* or the previous authorities), he would still exercise his discretion to dismiss the application to set aside the demand as he found that the third requirement in *Lasmos* is not satisfied in that Mr But had not taken any steps to commence arbitration and he had no genuine intention to commence arbitration[23]. I propose to consider this first.

The third requirement in Lasmos

50. The facts quite simply are that other than making a complaint to IB by email on 21 January 2015 (to which IB replied on 18 February 2015 that if Mr But was dissatisfied with its response, he "may escalate [his] complaint to the Financial Dispute Resolution Centre or to the Hong Kong Securities and Futures Commission") and, after the statutory demand was served on him on 12 December 2016, causing his solicitors to send the letter dated 16 December 2016 to IB's solicitors, Mr But took no steps to commence arbitration over a period of more than four years.

51. Mr Ko submitted that the third requirement in *Lasmos* has been complied with. He submitted that there is no requirement for the service of a "Notice of Arbitration" in clause 33B. The only requirement under that clause is to provide "notice of Customer's intent to arbitrate", and this was done by the letter of Mr But's solicitors dated 16 December 2016 and Mr But did mention this in his 1st affirmation at §38. It is provided in the penultimate sentence of Clause 33B that if the customer is the claimant-in-interest and has not selected an arbitration

[23] In contrast, arbitration had been commenced in a number of the cases cited: *Jade Union*, arbitration had been commenced and was stayed by consent pending the winding-up proceedings, §8; *Sky Datamann*, arbitration proceedings were commenced shortly after the petition was presented, §4; *Hollmet*, arbitration had been commenced before the petition was due to be heard, p 830H to I; *Salford*, arbitration had been commenced and concluded, the petitioning debt comprised the sum due under the award and further sums due which had not yet been referred to arbitration.

forum within ten days of providing notice of his intent to arbitrate, IB "shall select the forum". In this instance, as Mr But had not selected an arbitration forum within ten days of sending the letter dated 16 December 2016, IB was obliged to select a forum. Mr But could not be blamed for IB's failure to discharge its obligation of selecting a forum to commence arbitration.

52. This submission has no foundation in reality. The letter of 16 December 2016 stated that the solicitors were instructed "to initiate arbitration between the parties on the said disputes" and requested IB's solicitors to reply if they had instructions "to accept service of our client's Notice of Arbitration". Quite clearly, it was envisaged in that letter that another document which was to be a "Notice of Arbitration" was to be sent in time. There was no indication in that letter when any such "Notice of Arbitration" was to be sent, and when IB's solicitors did not respond to the inquiry if they had instructions to accept service of such "Notice of Arbitration" in the reply of 22 December 2016, Mr But's solicitors did not take that up with IB's solicitors ever again or effect service of any document on IB that may be regarded as a "Notice of Arbitration". In these circumstances, the letter of 16 December 2016 can hardly be regarded as proper notice of an intention to arbitrate.

53. As for the alleged obligation of IB to select a forum when Mr But had not done so within ten days of providing notice of intention to arbitrate, it cannot seriously be suggested that on a proper reading of clause 33B, the process of initiating arbitration would be brought to a complete halt where IB had not selected a forum upon the initial failure of the customer to do so[24]. Further, as submitted by Mr Stock SC for

[24] Decision, §§75, 76

IB[25], this point was not taken on behalf of Mr But for more than two years and was raised for the first time when supplemental submissions were lodged in April 2018 after the hearing. It speaks volumes as to the lack of any genuine intention to arbitrate on the part of Mr But. I do not accept Mr Ko's submission that this point was only taken in the supplemental submissions in light of *Lasmos*. He had advocated in his earlier submission that the approach in *Halki Shipping Corporation v Sopex Oils Ltd* [1998] 1 WLR 726 and *Salford* should be adopted. It would make no sense to dismiss or stay an insolvency petition on the mere existence of an arbitration agreement when the debtor has no genuine intention to arbitrate.

54. It is not necessary to discuss section 118(1)(b) of Cap 571 or the rules made thereunder being the Securities and Futures (Leveraged Foreign Exchange Trading)(Arbitration) Rules, Cap 571F, as there was no suggestion that Mr But had filed a request for arbitration in accordance with the then applicable version of the rules[26].

55. The judge is clearly right in holding that the third requirement of *Lasmos* has not been complied with. Regardless of whether the approach in *Lasmos* or the previous authorities is to be adopted, there is no basis to interfere with the exercise of his discretion under rule 48(5)(d) that the application to set aside the demand should be dismissed.

56. This is sufficient for this appeal to be dismissed.

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[25] With Mr Val Chow
[26] Decision, §77

The Lasmos approach

57. In the circumstances, it is not strictly necessary to decide whether the approach in *Lasmos* should be adopted in an application to set aside a statutory demand. But in view of the importance of this issue to insolvency proceedings, I would make these observations on an *obiter* basis.

58. First and foremost, it is pertinent to note the wording of article 8 of the UNCITRAL Model Law (which has effect by virtue of section 20 of the Arbitration Ordinance, Cap 609), the relevant part of which reads as follows:

> "(1) A court before which *an action*[27] *is brought in a matter which is the subject of an arbitration agreement* shall, if a party so requests not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed."
>
> (Emphasis supplied.)

59. It is clear on the authorities that a petition (whether for winding up or bankruptcy) does not come within the wording of article 8(1) in that it is not "brought in a matter which is the subject of an arbitration agreement". As stated in *Hollmet* at p 831 lines H to I, what the court is concerned to see in an insolvency petition is whether the alleged debtor is insolvent. One sees from the wording of article 8(1) that the insolvency proceeding is not a matter which is the subject of an arbitration agreement. It is the underlying contract or transaction which is

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[27] In contrast, section 9(1) of the Arbitration Act 1996 in the UK reads: "A party to an arbitration agreement against whom legal proceedings are brought (whether by way of claim or counterclaim) in respect of a matter which under the agreement is to be referred to arbitration …". In section 82(1), "legal proceedings" is defined to mean "civil proceedings in the High Court or a county court …". It was held in *Sky Datamann* at §§10 and 11 that the concept of a winding-up petition does not conform to the language of article 8(1) of the Model Law, as a petition, which invokes a class remedy, is not an "action" between "parties".

the subject of an arbitration agreement. In *Salford*, it was held in §26 that section 9(1) of the Arbitration Act 1996 (the equivalent English provision to article 8(1) of the Model Law) does not apply to a winding-up petition where the ground of the petition is that the company is unable to pay its debts and what is in dispute is that issue generally or, more specifically, whether there is outstanding and due a particular debt mentioned in the petition.

60. It follows from the above that as an insolvency petition is not covered by article 8(1) of the Model Law, there is no automatic, mandatory or non-discretionary stay under that provision. See *Salford* at §§34, 38 and 39; *Jinpeng Group Ltd v Peak Hotels and Resorts Ltd*, BVI HCMAP 2014/0025 and 2015/0003, 8 December 2015, Eastern Caribbean Court of Appeal, at §§44 to 45.

61. Second, having found no automatic, mandatory or non-discretionary stay under the arbitration legislation, the courts consider that there is a discretionary power to be exercised under the insolvency legislation whether to dismiss or stay a petition where the alleged debt arises out of a transaction containing an arbitration agreement. This has been the position pre-*Lasmos*. In *Sky Datamann*, it was held at §12 that it is "a matter for the discretion of the court in each case. In exercising its discretion, the court will consider all relevant circumstances, including the financial position of the company, the existence of other creditors, and the position taken by them."

62. Third, *Lasmos* (which followed *Salford*) decided that the s discretion under the insolvency legislation should be exercised only one way: the petition should "generally be dismissed" save in "exceptional"

or "wholly exceptional" circumstances, upon satisfaction of these three requirements: if the petitioning debt is not admitted (it is settled law that this is regarded as a dispute sufficient for the purpose of arbitration, without regard to the quality of the dispute or substantive merits[28]); the dispute is covered by an arbitration clause; and the alleged debtor has taken steps to commence arbitration. Whereas Sir Terence Etherton C in *Salford* found it difficult to envisage what those exceptional circumstances may be (at §39), Harris J in *Lasmos* suggested the following circumstances that may qualify as exceptional: where the circumstances justify the appointment of provisional liquidators[29]; where it is sought to engage the referral back provisions[30] because of substantiated concerns there had been fraudulent preferences; where it is sought to engage the avoidance provisions[31] (at §§29 and 30).

63. A statutory right is conferred on a creditor to petition for bankruptcy or winding up on the ground of insolvency. It is contrary to public policy to preclude or fetter the exercise of this statutory right (*Re Greater Beijing Region Expressways Ltd* [1999] 4 HKC 807 at 816A to H; *Re Sit Kwong Lam (Debtor)* [2019] 2 HKLRD 924 at §§20 to 27). Even though the *Lasmos* approach may not be regarded as totally precluding a creditor from invoking the insolvency jurisdiction of the court, it is a substantial curtailment of his statutory right.

64. It is pertinent to note Etherton C also said this in §35 in *Salford*, in the context of holding that section 9(1) of the Arbitration Act does not confer a non-discretionary stay of a winding-up petition:

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[28] *Tai Hing Cotton Mill Ltd v Glencore Grain Rotterdam BV & Anr* [1995] 1 HKC 363

[29] In bankruptcy proceedings, there is power to appoint the Official Receiver to be interim trustee at any time after the petition is presented and before a bankruptcy order is made, section 13 of Cap 6.

[30] Section 184(2) of the Companies (Winding Up and Miscellaneous Proceedings Provisions) Ordinance, Cap 32; section 51 of Cap 6.

[31] Section 182 of Cap 32; sections 49, 50 of Cap 6.

> "Furthermore, it seems highly improbable that Parliament, without any express provision to that effect, intended section 9 of the 1996 Act to confer on a debtor the right to a non-discretionary order striking at the heart of the jurisdiction and discretionary power of the court to wind up companies in the public interest where companies are not able to pay their debts."

65. The above comments are in line with the principle of statutory interpretation that the court is reluctant to attribute to the legislature an intention to make a radical change by way of a side-wind (*Medical Council of Hong Kong v Chow Siu Shek* (2000) 3 HKCFAR 144 at 158D). We have not been referred to any legislative materials in the enactment of the Arbitration Ordinance in 2011 as indicative of any legislative intent to change the insolvency legislation.

66. I note in *Jinpeng Group Ltd v Peak Hotels and Resorts Ltd* at §47, the Eastern Caribbean Court of Appeal declined to adopt the *Salford* approach as the BVI court's statutory jurisdiction to wind up a company based on its inability to pay its debts as they fall due unless the debt is disputed on genuine and substantial grounds is "too firmly a part of BVI law" to now require a creditor exercising the statutory right to prove exceptional circumstances to establish his status to apply to wind up a company. The statutory jurisdiction is satisfied once the creditor is applying on the basis of a debt that is not disputed on genuine and substantial grounds. The position is the same as regards the insolvency legislation in Hong Kong.

67. For the above reasons, I have reservations if the discretion under the insolvency legislation should be exercised only one way to s substantially curtail the right of a creditor to present a petition.

68. Fourth, the justification for the *Salford* approach (followed in *Lasmos*) is to bring insolvency proceedings in line with the approach in an ordinary writ action, where it was held that the legislative intent in enacting the 1996 Act was to exclude the court's jurisdiction to give summary judgment[32] (*Halki Shipping Corporation v Sopex Oils Ltd* at 750G to H, 762H to 763A). "It would be anomalous, in the circumstances, for the Companies' Court to conduct a summary judgment type analysis of liability for an unadmitted debt, on which a winding-up petition is grounded, when the creditor has agreed to refer any dispute relating to the debt to arbitration", thus giving no weight to the policy underlying the arbitration legislation (*Salford*, at §40; *Lasmos* at §17).

69. To justify the apparent anomaly, the authorities in Hong Kong before *Lasmos* had given various reasons why insolvency proceedings should be treated differently from an ordinary writ action, see *Hollmet* at 831H; *Sky Datamann* at §§7, 11; *Jade Union* at §§18, 19, 26 – that insolvency proceedings are not the means of enforcing a contract, that the petitioner invokes a class remedy available to all of the creditors, that there is no adjudication as to the parties' respective rights and liabilities as between themselves. Harris J in *Lasmos* did not think those reasons are sufficient to justify the anomaly, see §§24 to 27.

70. Without going into that debate for my *obiter* observations, I would acknowledge that considerable weight should be given to the factor of arbitration in the exercise of the discretion. It is right to heed the words of caution that "exercise of the discretion otherwise than

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[32] By removing the court's power under section 1 of the Arbitration Act 1975 to refuse to stay proceedings where it was satisfied that "there is not in fact any dispute between the parties with regard to the matter agreed to be referred". There was not the same change in legislative wording in Hong Kong with the enactment of the Arbitration Ordinance in 2011, as since 1997 the relevant provision was based on article 8 of the Model Law.

consistently with the policy underlying the [arbitration legislation] would inevitably encourage parties to an arbitration agreement – as a standard tactic – to bypass the arbitration agreement and the [arbitration legislation] by presenting a winding up petition" (*Salford*, at §40). I also acknowledge it may well be that insufficient weight had been given to the arbitration factor pre-*Lasmos*.

71. Having said that, I do not think the court is powerless to deal with any such tactic that may be practised by a creditor seeking to apply improper pressure on the alleged debtor. Nor do I think that the discretion should invariably be exercised in favour of granting a winding-up or bankruptcy order where the court is satisfied there is no bona fide dispute on substantial grounds, thereby putting an end to any arbitration proceedings. In *Hollmet* at 832B to D, Rogers J (as he then was) suggested possible ways of exercising the discretion where there is no bona fide dispute on substantial grounds:

> "If a company wishes to obtain a stay of winding-up proceedings on the basis that the underlying debt upon which the statutory notice is founded is disputed, it must establish in the normal way that there is a bona fide dispute on substantial grounds. If it has not satisfied the court as to the bona fides and substantial nature of its claim it can only expect a short adjournment to enable it to commence the arbitration and then, if sufficient evidence to establish a genuine dispute is still absent it can expect to have to give an undertaking to proceed with the arbitration with all due dispatch. It cannot simply put up its hands and say: "You, the court, have no jurisdiction because of my contract." That is not what the contract says, and the Companies Court is entitled to be satisfied that there is a proper dispute."

72. *Jinpeng Group Ltd v Peak Hotels and Resorts Ltd* at §§50 to 52 was a further example how the discretion might be exercised where the court found the dispute between the parties was not on genuine and substantial grounds.

73. As this appeal is to be allowed, the discretion would be exercised by the judge hearing the petition upon the lifting of the stay of the bankruptcy proceedings when further directions are to be given by the Court of First Instance. This is not the occasion for us to decide on the appropriateness of the *Lasmos* approach.

Conclusion and orders

74. I would dismiss this appeal with an order *nisi* that Mr But is to pay the costs of IB, with a certificate for two counsel.

Hon Cheung JA:

75. I agree with the judgment of Kwan VP.

Hon Chu JA:

76. I agree for the reasons given by the Vice President that the appeal should be allowed. I also agree with Her Ladyship's *obiter* observations on the *Lasmos* approach.

(Susan Kwan) Vice President	(Peter Cheung) Justice of Appeal	(Carlye Chu) Justice of Appeal

Mr Tony Ko and Mr Kong Cheuk Wing, instructed by Lee Chan Cheng, for the Applicant (Appellant)

Mr Alexander Stock SC and Mr Val Chow, instructed by Tanner De Witt, for the Respondent (Respondent)