

**BEFORE THE APPEAL BOARD OF THE FINANCIAL SERVICES BOARD**

In the matter between

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|------------------------------|------------------|
| WAYNE ASHLEY GRAY            | First Appellant  |
| QUANTUM LEAP FOREX (PTY) LTD | Second Appellant |
| and                          |                  |
| IAN GEORGE BUCHANAN SCOTT    | Respondent       |

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**DECISION**

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[1] The Ombud for Financial Services Providers made a determination upholding a complaint by the respondent, Mr I.G.B.Scott (Scott) against the first appellant, Mr W.A.Gray (W.A.Gray) and the second appellant, Quantum Leap Forex 181 (Pty) Ltd (QL). He found that in the course of their business as financial services providers in terms of the Financial Advisory and Intermediary Services Act 37 of 2002 (“the Act”), the appellants had been negligent in relation to the initiation and subsequent conduct of an investment by Scott, through them, in foreign currency (“forex”) trading, via persons and/or entities, the probity and reliability of which were unproven and open to question. In respect of net losses sustained by Scott as a result of so investing, the appellants were ordered jointly and severally to compensate him in the sum of R100 174.75 with interest. They appeal, with the necessary leave, against the finding that they were negligent and therefore liable to pay compensation.

[2] Scott made three separate investments : R270 000 in August 2004, R130 000 in January 2005 and R200 000 in July 2005. The first predated the Ombud's authority to determine such complaints. In all three instances Scott's funds were applied to forex trading, that is to say until 7 September 2005. On that date, according to the evidence put before the Ombud by the appellants, his funds, as also the funds of QL's other forex trading clients, were switched to bullion trading. A short position having been taken, the gold price failed to sustain the fall that was necessary to make the short position profitable. Instead it rose intermittently. Major losses occurred. In an attempt to stem the losses it was decided on several occasions to lock the trade by buying long but each time the position was unlocked the price went on climbing and more severe losses were suffered. Eventually Scott terminated the relationship with QL and called for repayment of his funds. He received approximately one-fifth of the amount that had stood to his credit when the switch to gold trading occurred.

[3] In his determination the Ombud expressed disbelief that Scott's loss had been sustained in this way. As a result, the appellants applied in terms of s 26B (12) (a) (i) of the Financial Services Board Act 97 of 1990 for an order that an affidavit by Mr J.J. van As, a forex and commodities trader, be introduced into the appeal record. No evidence by him was before the Ombud when the determination was made.

[4] The application was dealt with as part of the appeal hearing. In the course of the argument on the application counsel on both sides indicated their respective clients' wishes to have the hearing before us dispose of the appeal irrespective of the fate of the application. Neither side sought reversion of the matter to the Ombud as provided for by subsection (12) (b) of the last mentioned Act if the evidence were included in the record. The latter provision reads peremptorily and whether the rights it creates can be waived we need not decide. It was open to us to admit the evidence subject to our deciding its relevance as part of this decision. The

subsection could never have been intended to require reversion to the Ombud in the case of evidence admitted but ultimately found not to be relevant. We admitted the evidence on that basis and the argument on appeal proceeded accordingly. It is appropriate to deal with Van As's evidence right away.

[5] The facts on which he relies are those provided to him by the appellants. That does not include evidence by the person who allegedly made the gold trades, Krishnamoorthy Thiruvenkadam, referred to in the record by the name Kiran. The latter, to whom we shall refer again in due course, could apparently not be traced by the appellants for the purposes of securing a statement from him.

[6] What Van As says, in summary, is that the prices at which the appellants contend the gold trades were taken were prices that were available in the market at the relevant times; that Kiran used a generally acceptable method of trading to decide what trades to make; and that the quantum of the losses was attributable to trades taken and not some other cause such as theft. Whether it was reasonable to switch from forex to bullion – the crucial question in the case – Van As ventures no opinion. The most he says as to reasonableness on Kiran's part is that –

“The position taken by the trader was reasonable given the method used by him at the time...the trader had an acceptable basis to activate the sell trade ...based on the trading history and the methodology he used.”

The trading history he refers to is that pertaining to bullion, not forex. What he is in effect meaning is that, on the assumption that it was reasonable to switch into gold on the date in question, the decision to take a short position, given the relevant levels at which gold had been trading, was reasonable. But that is not the issue. Plainly, Van As's evidence cannot take the case further on what we have called the crucial question. It would assist the

appellants on the matter, already mentioned, of the Ombud's disbelief but in our view the case must be approached on the basis that there is no sound ground to reject the appellants' allegation that Kiran switched their clients' investments into gold trading. We therefore conclude that Van As's evidence is not relevant to the advancement of their case on appeal.

[7] In the application for further evidence to be introduced, reference was made to various alleged disputes of fact which, so it was contended, should have been resolved by the Ombud either by hearing oral evidence or by resort to the rule laid down in **Plascon-Evans Paints Ltd v Van Riebeck Paints (Pty) Ltd 1984 (3) SA 623 (A)**. For reasons to be given presently there was, and is now, no reason to require oral evidence. And the Plascon-Evans rule applies to conflicting affidavit evidence in litigation on motion. It is a way of dealing with the problem of resolving disputes on paper involving oath against oath. It has no place in proceedings like these in which the Ombud must determine the probabilities either by using the procedure applicable to commissions and hearing oral evidence or, as in this case, by using the procedure provided for in the Rules made in terms of the Act and resolving the case on the papers.

[8] Turning from matters procedural to matters substantive, at the time of the first investment Scott signed a document embodying terms falling under the heading "Authorisation", on which terms the appellants rely. The purported authorisation empowered QL to manage Scott's funds and to carry out certain speculative operations "through registered International Brokers". It stated that his funds would be placed in an account with Reymount Investment Ltd, Jersey, (Reymount) and managed and traded by QL, the latter having a discretion at all times in regard to such management. The authorisation then reads :

"The Client hereby expressly approves of all investment decisions of management and or abstention thereof by [QL]; that the Client shall bear the risk of gain or loss in

the Account and all expenses, if any and accepts that no assurance or guarantee is given that the account will always be profitable or that it will not incur losses and further agree that [QL] shall not under any circumstances be held to be liable for any transaction performed under this agreement providing that there has been no willful misconduct or grievous negligence on the part of [QL] or its authorized agents, assignees, officers or employees.”

[9] It was argued for the appellants that there was no evidence of willful misconduct or grievous negligence and on the strength of the terms of the Authorisation it was contended that they were not liable for ordinary negligence. The short answer on the latter point is that the vital premise from which the disclaimer proceeds is that QL’s activities on behalf of Scott were to be undertaken on QL’s behalf by registered International Brokers. Counsel for the appellants correctly conceded that Reymount and Kiran did not meet that qualification. There is no evidence that this misrepresentation was either explained to Scott or that it was immaterial to him. Therefore he cannot be bound to the limitation or any other terms of the document on which the appellants seek to rely.

[10] The next point sought to be emphasised by the appellants was that Scott made the second and third investments against their advice. However they did not refuse to place the investments or record their disapproval. They accepted the investments and from then on were as responsible to exercise care and skill as they were in relation to all the other investments placed with QL.

[11] This is an appropriate stage at which to point out that when making the second investment Scott signed a document recording his confirmation

“that my Forex Investment with [QL] was explained to me and I am prepared to invest in Forex Speculation.”

The document goes on to list seven terms which he acknowledged being aware of. Clearly they all concern his investing in forex. They say nothing about trading in bullion. And it was the appellants' case after all that Scott was determined to invest in forex. Neither side has ever said he expressed any interest in gold trading. Absent a valid and binding authority to invest his funds in gold trading – and for reasons already stated, there was none – it was not the action of a reasonable person in the appellants' situation to switch his investment into gold trading without getting his consent.

[12] As to his funds being exposed to being dealt with by Kiran, Kerford (Pty) Ltd (Kerford) and Reymount, we have already made mention of Kiran and Reymount. Kerford employed Kiran. The record contains a statement by him that he was a branch manager of Kerford and his duty there was to manage clients' portfolios. Kerford's letterhead declared its business as "Financial Monetary Intermediaries" and stated that QL was an introducing broker to Kerford and that funds entrusted to Kerford would be placed with Reymount, an international clearing house. Despite Kiran's being an employee of Kerford, QL appointed him as its key individual. The Act defines a key individual as the person responsible for managing or overseeing an entity's financial service activities. QL's appointment of Kiran evinced a disregard for the fact that he had responsibilities and duties to Kerford which could well have confronted him with a conflict between the interests of QL's clients and those of Kerford. The fact that Kiran had experience and even ability in forex trading appears to have overshadowed, in the appellants' outlook, the need that he also be trustworthy, of sound judgment and susceptible to the control which QL would have had over its own employee.

[13] In so far as Reymount was concerned, the appellants became aware in April 2004 of a public statement by the Financial Services Commission of Jersey that Reymount, a company incorporated there, was not registered under the island's financial services laws and that it

was conducting unauthorised and unlawful investment business. Through Mr G.Gray (G.Gray) the appellants made two enquiries. The first was directed to Kerford. The remarkable answer obtained was that the Commission's warning only applied to Jersey residents. Patently that was nonsense. It was clearly stated by the Commission that Reymount was acting unlawfully. The second enquiry was directed by G.Gray during a week in London in May 2004. He said in a statement in the record that he flew there "to speak to someone (I do not recall the name of the gentleman I spoke to) at their Reymount 'Administration office'." This evidence is also remarkable. The journey was apparently important enough to justify the expense and a week's absence yet no record was kept of the person's name, his authority to speak on the subject of the enquiry or, most importantly, of what he had to say. It is also unexplained why an enquiry was not directed to the Jersey Commission itself or to Reymount personnel on the island. Despite that state of affairs it was to Reymount that Scott's funds were, unreasonably, to be entrusted when he invested in January 2005. In that instance the money was deposited into a Reymount account in Chicago.

[14] By the time of Scott's investment in July 2005 the Financial Services Board of this country (FSB) had declined to grant Kerford a licence as a financial services provider. The FSB had also warned the appellants that Reymount would not be recognised as a clearing house. Notwithstanding these developments the appellants, again unreasonably, went on using Kiran as their agent through whom they conducted forex trading for their clients, including Scott. There was a distinct risk involved in using the services of a person employed not by the appellants but by a company the FSB refused to approve. And they continued to use the services of Reymount. Their explanation was that they had to do so until they had a new clearing house. That was not reasonable. The safe course was to withhold further deposit until they had one.

[15] Then came the switch to trading in gold on 7 September 2005. It is important here to have regard to how forex trading had been progressing not only for Scott but QL's other investors among whom were G.Gray. In the first place it is necessary to erase the impression that the lack of forex trading from July to September was due to adverse market conditions. Scott says his monthly statement for July contained the statement on behalf of QL that there were conflicting trading indicators on the currency market and that "as a protection to your investment & to prevent potential losses of capital [QL] did NOT trade any accounts." He says W.A.Gray assisted him in early August to make the bank deposit of his July investment and made no mention of negative market conditions. What is more, an annexure (obviously emanating from the appellants) to Van As's affidavit relates to Scott's account and, having stated the June balance, says this:

"No activity and trades until Sep since both Gary and Kiran were completely absorbed in finding a suitable clearing house and improve the [QL] Forex Mandate as per Molefe at FSB.Clients drawing income were still being advanced."

It will be recalled that the FSB (and it was through Mr Molefe) had indicated that Reymount would not be accepted. The record reveals that the appellants' efforts were thereafter focused on trying to secure an arrangement that the Danish bank, Saxo, would be its new clearing house.

[16] The fact that Scott's third investment was placed in forex trading has an added significance. If the appellants were against his funds going into speculative investment that was the appropriate time to tell him that market conditions were adverse and contra-indicated. There was no such warning.

[17] Then there are the forex investments made by G.Gray. On 20 June 2005 he invested R269 427 and on 15 August 2005 R194 277. It is not in the least plausible that he would have

made those investments had the forex market been adverse. A statement by him is included in the record. It stresses the considerable gains achieved by forex investors up to and including July 2005, some at an annual interest rate near to 100% and some well in excess of that figure. His own account for the four months from March to July 2005 showed a profit of 188.03%.

[18] On those facts the intimations accompanying Scott's July statement as to the reason for an absence of forex trading were therefore simply disingenuous.

[19] Apart from the extent of the gains just referred to, the facts presented by the appellants to Van As reveal that the positive balance in Scott's account increased from 18 February 2005 until the first of June –some three and a half months – by some 40%.

[20] On the evidence before the Ombud there was no rational or reasonable ground for the wholesale switch to gold trading on 7 September 2005. Moreover all that the appellants have to say on this vital aspect is contained in the following virtual one-line offerings:

- By G.Gray : “At the time, graphs and technical analysis showed this trade to be very promising”;
- By W.A.Gray : “When [Kiran] took the gold trade, this looked like a very good trade at the time.”

[21] No evidence of a factual or expert analytical nature was put before the Ombud or this Board to show how gold trades had fared over the first seven months of 2005, compared with forex trades, so as to justify the conclusion that it was reasonable to eschew growth of the order that forex trading was achieving at that time and not only to switch to gold but heavily so. It is not altogether surprising that the Ombud was as sceptical as he was about this. On the basis of the evidence which the appellants presented we accept, as we have said, that the

switch was made but the very extraordinariness of the move warrants the finding that it was not reasonable. At least that is prima facie so and the absence of tenable, feasible explanatory evidence to point in the opposite direction renders that finding justifiable. Kiran was their trading agent and they were liable for his actions. In addition, they were themselves negligent in not stopping him when they knew, or must by necessary inference, have known that he was going to make the switch.

[22] Finally, there is an aspect of the evidence of Van As which does have relevance, not to the case for the appellants, who sought to rely on him, but rather to Scott's case. According to Van As, had Kiran closed the gold trades when the market returned to what he called the resistance level he would have minimised the loss. Significantly, a letter in the record written by G.Gray mentions his having insisted to Kiran that the trade be cut when QL's clients' accounts had suffered a loss of about 40%. But Kiran decided rather to lock the trade and losses ended at about 90%. That this was allowed to happen is but further evidence of unreasonable action by the appellants. Hindsight must, of course, be avoided as a yardstick. Locking the trade might not in all circumstances have been a blameworthy course to adopt. However, the appellants knew that Kerford and Reymount were not approved of by the FSB and ought to have realised that continuing to deal with them was inherently risky. Kiran was not the appellants' employee and had responsibilities towards the clients of Kerford. The gold trading had gone badly wrong. QL clients, having enjoyed a period of successful forex trading, had been cast into a different kind of investment and had sustained substantial losses. Reasonableness required that the appellants took steps to withdraw all their clients' investments before Kiran proceeded to lock the trade. Unreasonably, they failed to do so.

[23] Having considered all the evidence, we hold that the conduct of the appellants fell short of the standards of a reasonable person in their respective positions, not only at various earlier


stages preceding the entry into gold trading but also, and essentially, in respect of that entry and the subsequent locking of that trade. They were therefore negligent in relation to Scott's second and third investments at those earlier stages and especially, and to a high degree, in relation to the switch into gold trading. They were therefore liable for Scott's losses.

[24] The matter of the quantum of the compensation to be paid was not in issue. The order of the Ombud must stand.

[25] The order of the Board is as follows:

The appeal is dismissed with costs, such costs to include the costs occasioned by the application to the Chair of this Board for leave to appeal.

Dated this 4<sup>th</sup> day of January 2012.



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Judge C. T. Howie, Chair



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J. D. Perna, Member



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D. L. Brookling, Member