COMPLETE GUIDE

Contract law and authorised signing

CYGNETISE

Contents

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What is a contract?

Contract is probably one of the best-known legal concepts as it takes such a central role in modern society's political, economic, and social life. Very often, contract is used interchangeably with words like agreement, bargain, undertaking, or deal. Whatever the term, the underlying idea of a contract is that it gives people the freedom to pursue their own lives whilst considering the rest of society. Contract is central because it allows for a free society to still live and function in order, which would otherwise turn into anarchy.

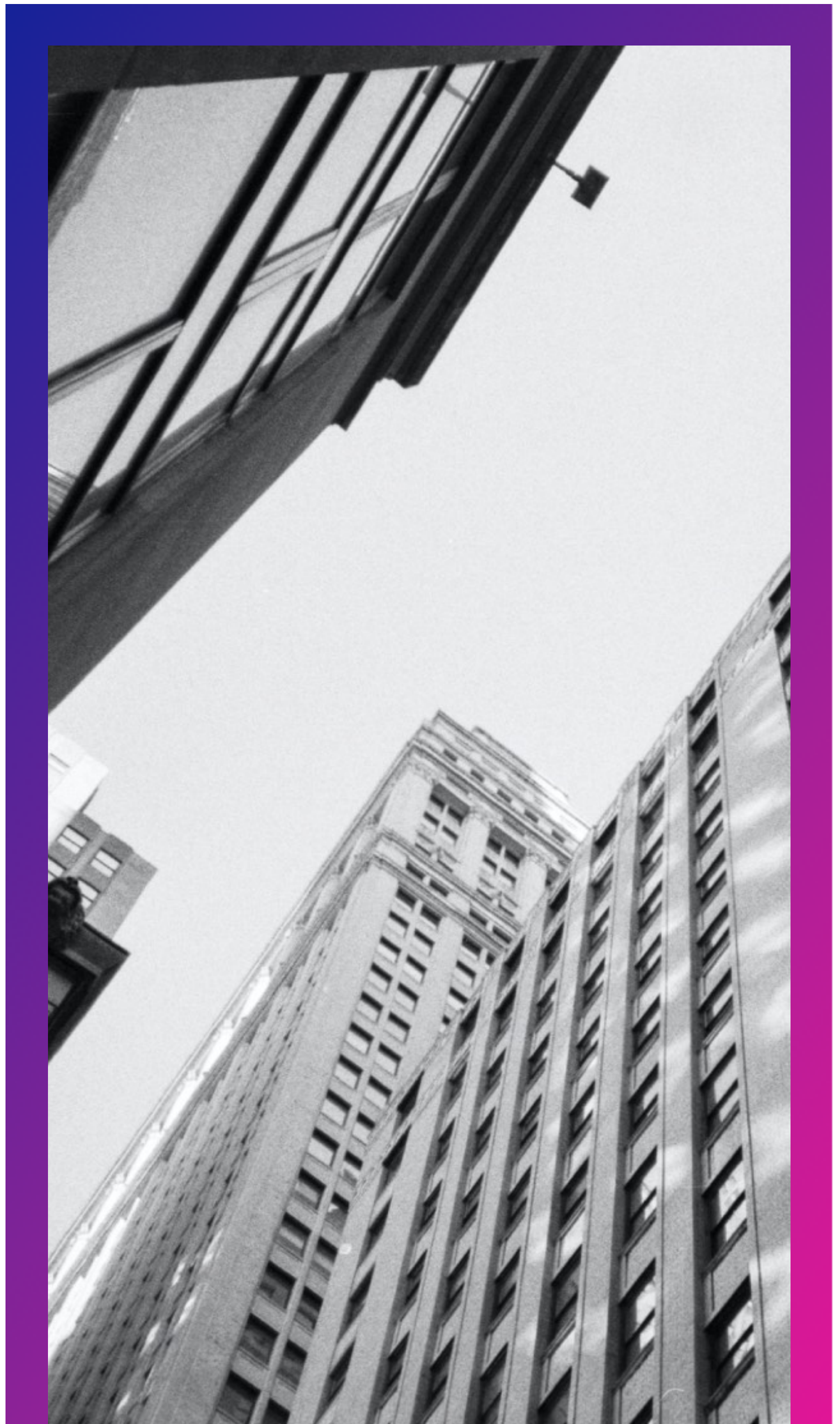
In legal terms, the simplest definition of a contract is that it is "a legally binding promise (or set of promises) or agreement between two parties or groups". "Legally binding" here means that the promise or agreement will create rights and obligations that may be enforced by law.

The importance of contract law

Contract law is key to the existence of our modern society, and life as we know it today. In most countries in today's global economy, goods and services are created and distributed through markets. And contracts are at the heart of how markets operate. In markets and businesses, almost every transaction that takes place involves a contract – e.g., buying or selling goods, leasing premises, hiring equipment or personnel, receiving payments, banking, etc.

The reason for this is that the lack of efficient contract enforcement puts businesses and the whole economy at risk.

Overall, economic and social progress cannot be achieved without respect for the rest of the society and effective protection of human rights.



Contracts and the law

What makes a contract valid?

Contracts are usually governed and enforced by the laws in the country where the agreement was made. Every country has its own contract rules.

However, contract law commonly involves the following 3 principal elements:

1. **Offer and acceptance (agreement)** – Every contract must have a valid offer and acceptance. One party makes an offer with a set of terms and the other party accepts the terms of the offer. This usually happens by making a payment or providing a signature in writing.
2. **Consideration** – Consideration is usually a payment or value that is exchanged for an offer. Whilst in most cases consideration is monetary, it can also be in the form of interest, benefit or a right.
3. **Legality** – For a contract to be valid, it has to be for a legal purpose. Any contract that requires a person to commit an illegal activity like a crime is considered to be void and unenforceable. Besides legality of purpose, a contract is only valid between parties who have full legal capacity to enter into a contract – these are legitimate, legal entities, or individuals above certain age (adults) with sufficient mental capacity or ability to fully understand the nature and consequences of their actions.

Types of contracts

There are different types of contracts, and they can be either verbal or in writing to be legally enforceable. Generally, the law recognises the following 4 categories:

1. **Bilateral** – This is the most common or traditional type of contract that involves a mutual exchange of promises among the parties. A bilateral contract is often called a two-sided contract because of the two promises that form it. In this type of contract, each party may be considered both making a promise, and being the beneficiary of a promise.
2. **Unilateral** – This type of one-sided contract usually requires a performance rather than a promise from the party accepting the contract's offer. And the contract happens when the required act is complete. A perfect example of a unilateral contract is a "reward" promotion, offering a monetary "reward" in exchange for some sort of information or value.
3. **Express** – An express contract takes place when the parties state the terms, either verbally or in writing, at the time of formation.
4. **Implied** – A contract is implied when there's an act or fact that clearly indicates that the parties have an intent to enter into a contract, even if no obvious offer and/or acceptance were stated orally or in writing.

Breach of contract

"Contract breach" is a term used to describe the event in which the contract is broken by under or non-performance of any of the contractual terms, warranties or conditions. The most common types of contract breaches include:

- **defective performance** - where a contract is partly performed but not to the agreed standard,
- **delayed performance** - where a contract is not performed within the required time frames,
- **complete non-performance** - a party completely fails to perform a contract.

The consequences of a contract breach will depend on the type of terms that have been broken.

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Contract laws across different jurisdictions

Contracts are usually governed and enforced by the laws in the country where the agreement was made. Every country has its own contract rules.

In the following section, we take a look at the key differences in contract law between the EU, UK and US.

EU contract law

The European Union (EU) single market permits businesses within the block to trade on an equal basis. To facilitate this, the EU has introduced a set of measures to remove all obstacles to free trade, including any limiting contractual clauses. EU directives have been introduced to for critical trading areas like e-commerce and the insurance and banking sectors. Whilst these measures have impacted contract law in some member states, the EU has no right to regulate the contract law of individual countries. So, each country maintains its own legal contract provisions and legislations vary.

Another measure the EU has taken to help unify contract law in the single market is the Principles of European Contract Law framework. It represents a set of 'model' rules for business contracts, based on fairness and simplicity. They aim to provide resolutions for issues where national laws don't offer an answer.

The Principles are available in each of the EU's languages and businesses can use and agree to some - or all - of these clauses. Then, in the case of a dispute, EU clauses will take precedence over the contract law of the country where the contract is signed.

UK vs EU law

From a comparative law perspective, contractual contingencies significantly vary across different European jurisdictions. Under English law, for example, there's no statutory provisions for "force majeure" like in other European countries – it's not a standalone concept. And the only way for contractual performance to be statutorily excused under unexpected circumstances is if they fall within the fairly limited doctrine of frustration. This doctrine usually is applied by default unless the parties have agreed a specific set of terms in their agreement.

On the contrary, most European continental countries do provide some form of mediation on the contract in unprecedented circumstances. In the Netherlands, for example, when a judge assesses if unexpected occurrences have undermined the fairness of the contract, they can decide whether to terminate or adapt it. It must be highlighted that both remedies are called upon by the law without one prevailing over the other. Since the reform of Art. 1195 of the French Civil Code in 2016, France has adopted the same model.

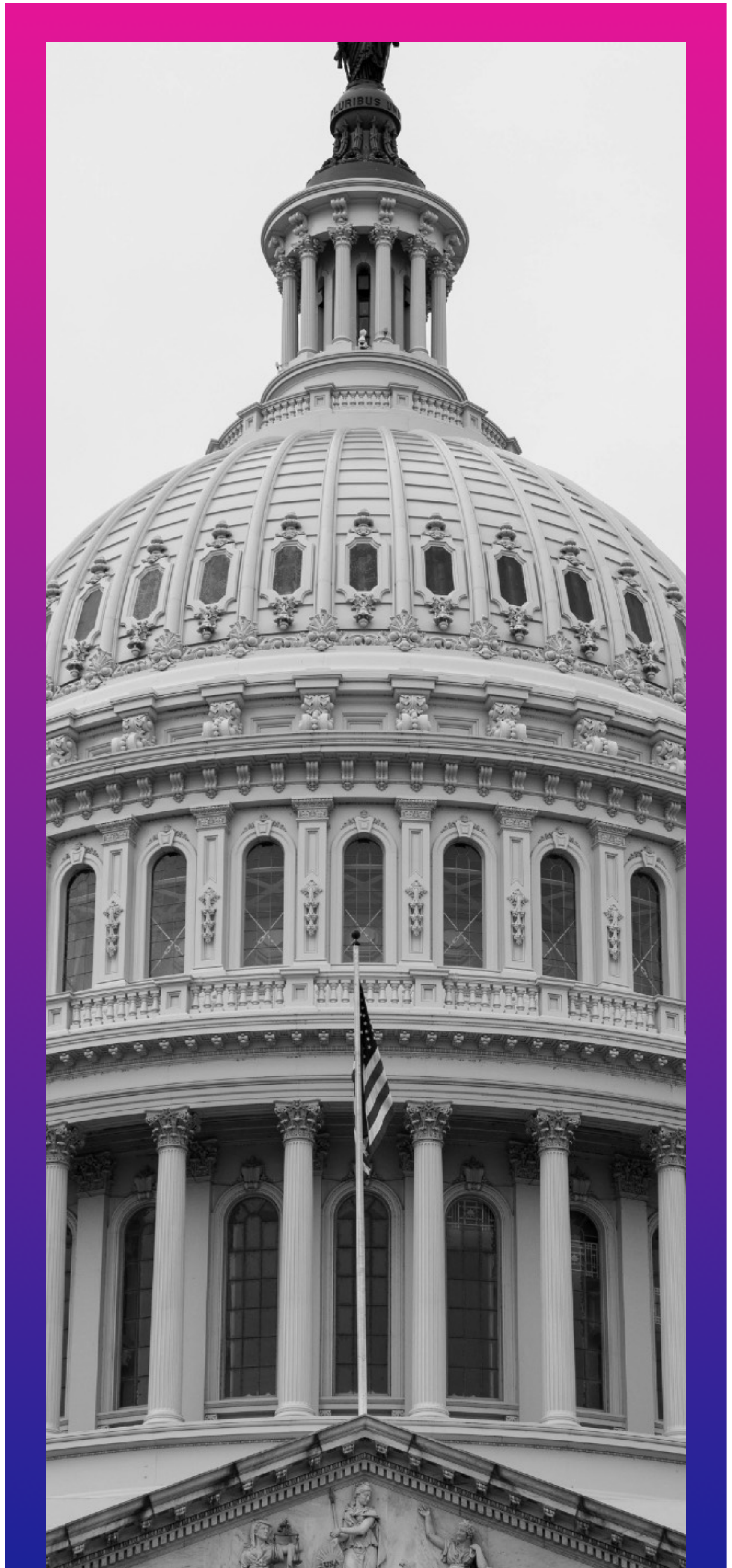
The most advanced contingency-adapted legislation in Europe was drafted in Germany in 2002, with the new wording of Art. 313 of the BGB (German Civil Code). "The provision indeed prescribes adaptation as the first and main remedy to a sudden and unexpected change of circumstances, which should push contractors to try the way of an extra-judicial renegotiation. On the contrary, termination can only be taken into consideration if adaptation turns out to be impossible or unzumutbar / unacceptable. Such an unacceptability shall be judicially proven through a balancing of interest's assessment, and can only be assessed if the survival of the contract would lead to a result which is intolerable and contrasting both with the law and fairness".

US contract law

In the US, contracts are usually governed and enforced by the laws in the state where they are made. Depending on the type and subject of agreement (i.e. sale of goods, property lease), a contract may be governed by one of 2 types of state law. These are:

1. **The Common Law** - most contracts (i.e. employment agreements, leases, general business agreements) are controlled by the state's common law. This is a tradition-based yet constantly evolving set of laws that is formed from court decisions over the years.

2. **The Uniform Commercial Code (UCC)** - the common law doesn't govern trade contracts that are primarily for the sale of goods. These fall under the Uniform Commercial Code (UCC), a standardised collection of guidelines that govern the law of commercial transactions. Most states have adopted the UCC accordingly, making the UCC's provisions part of the state's codified laws pertaining to the sale of goods. Similar to the UK, the UCC provides a doctrine of frustration in "force majeure" circumstances, but it also includes a principle of impracticability. The impracticable principle serves a much wider purpose than simply a non-performance protection, but it can never go so far as a complete adaptation of the contract.



Executing contracts and the role of authorised signers / signatories within organisations

A failure to properly execute a contract can result in a number of issues like an unenforceable or invalid contract, and disputes. One of the key steps in executing contracts effectively is knowing who can sign what within an organisation and maintaining a valid and up-to-date authorised signatory list.

Whilst negotiating and securing a deal are usually the hardest, the final stage of the contract management process is no less challenging. A failure to execute a contract the right way, can result in a number of issues like an unenforceable or invalid contract, arguments and shorter limitation period.

To ensure the effective execution of a contract, the parties should generally go through the following 3 key steps:

1. **Determine the type of contract and all formalities of the agreement** – e.g., if you're in the UK, are you dealing with a simple contract or a deed? Some types of contracts need to comply with certain formalities (e.g. if an agreement is to be executed as a deed, the signature must be witnessed).

2. **Identify who can sign** – Who can sign what also depends on the type of contract. For example, UK deeds can be signed by; two directors, registered as such at Companies House; one registered director plus the company secretary; or one registered director, in the presence of a witness who also signs the document (depending on the company's articles of association and what method(s) have been authorised by the company). In contrast, simple contracts can also be signed by a person (or persons) with express or implied authority to sign. Knowing who can sign what within an organisation is then particularly important. Having an effective authorised signatory management process and policy in place can help you achieve this.

3. **Choose a method of signing** – Traditionally, contracts are signed by applying wet-ink signatures on hard copy documents. Nowadays, contracts can also be implemented via electronic signatures. In some cases, e-signatures are still not permitted so the method of signing will also depend on the type of documents.

What is an authorised signer?

Simply put, an authorised signatory or signer is a person who's been given the right to sign documents on behalf of the authorising organisation. However, the term's meaning and interpretation seem to vary significantly across different jurisdictions and industries.

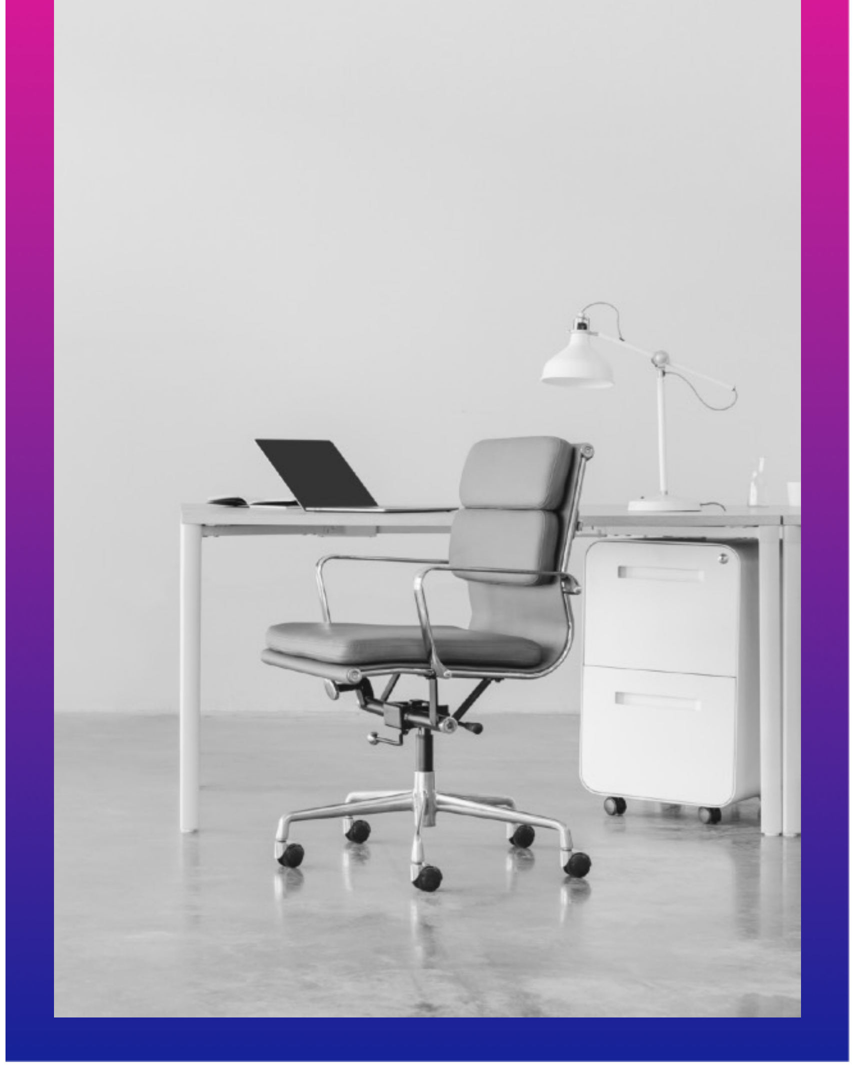
Different types of authorised signatories

Company signature authorisation

Designated officers/employees within an organisation who are authorised to process and approve official documents and third-party agreements on behalf of the organisation are often referred as "authorised signers".

The process of signature authorisation usually forms part of a broader "Delegation of Authority Policy" that establishes an internal procedure for appointing approval and signing authority, and defining the level of scope of that authority. The policy also includes a list of general responsibilities for authorised signers to follow when reviewing, approving and processing company contracts and official documentation.

For example, many organisations restrict signature



authorisation to directors or senior employees and set contract value limits applying at different seniority levels.

Typical company signatory duties include:

- Being party to resolutions
- Signing and delivering official documents and agreements with third parties and serving as a company's agent
- Signing/authorising goods/product orders
- Signing/authorising permits, passes or time-sheets
- Giving any notices
- Executing any specific undertakings and approvals

Authorised signers on bank accounts

In banking, personal and business account holders can authorise someone else to manage their account. These people are also usually called authorised signatories. Many banks require account holders to be recognised as authorised signatories, too.

In terms of level of authority, authorised signers usually have the same access to the bank account as the account holder.

In business banking, however, the rights of authorised signers tend to differ across various jurisdictions and depend on local government's specific legislations. Some of the most common types of permissions held by authorised signers on business accounts are:

- Ability to withdraw / deposit cash, and sign checks/ cheques
- Access to an account's balance
- Access to transactions history
- Ability to cancel payments on checks/cheques
- Ability to close the account

In the US, there're also specific rules for authorised signers on business accounts owned by limited liability companies (LLCs). Although an authorised signer is allowed to do business in the same way as the owner of the bank account (the LLC), he/she doesn't have the same legal responsibilities as account holders. This requires a highly trusted individual to be designated as the second authorised signer on an LLC permitted to make financial transactions from the account such as spending or approving company funds.

Signature authority can be given by an LLC to one or more individuals for all legal and financial documents or rights can be approved for only certain accounts or transactions. Moreover, sometimes different roles have the permission to sign off on specific paperwork. For example, a managing director or LLC president may be the authorised signer for the following documentation:

- Loan documents
- Partnership Agreements
- Contracts

Whereas, the CEO of the LLC may have the authority to sign off on other documents, such as:

- Loans
- Checks/ Cheques
- Any other finance-related paperwork

In personal banking, individual authorised signatories can usually use an account separately if the mandate says "several", "any" or "either" authorised signatory can sign (that is, operate the account).

Otherwise, if a mandate requires "joint", "both" or "all" (or in some cases "any two") authorised signatories to sign or access the account together, it means that one authorised signatory alone cannot use the account. Other authorised signatories must also authorise the transactions. A bank cannot allow transactions or other activity without the consent of the other holders.

Trading authorisation on investment accounts

In brokerage, authorised traders refer to brokers or agents who are permitted to trade on behalf of the investor/client. In other words, trading authorisation allows an investor to grant certain level of authority to a third party for the purpose of trading on a designated trading account.

This usually happens when an individual person decides to appoint a financial professional to receive financial advice. Generally, there're two types of trading authorisation levels: full trading authorisation and limited trading authorisation.

To establish the level of trading authorisation, the primary account holder is usually required to consent to the authorisation through an official formal document or contract.

In the UK, under FCA's MiFID II regulation, organisations who buy or sell financial instruments are now required to maintain a valid and up-to-date internal authorised traders list.

The importance of authorised signatory management

In today's highly-dynamic business world, effective authorised signatory management is key for the successful operations of any trading organisation who manages multiple corporate relationships. A failed authorisation can not only result in unnecessary operational costs for the organisation, but also expose it to a risk of financial loss due to fraud.

What are the risks of a failed authorised signature?

A payment gets held up

Process / deal / transaction delays

A deal fails - may adversely impact deal chain

Deliberate fraud happens. Someone signs that is not eligible

Failure to comply with internal controls and corporate governance policies

Whilst lists are exchanged and requested to be provided when authenticating signatures, there is the issue of human error/ignorance, where relevant parties simply do not check them. Commonly, this is because of time constraints and/or the aforementioned presumption that the signature must be valid and the signatory properly authorised.

Transaction delay

Usually, counterparts who access the authorised signatory data (ASLs) are reliant on the latest information/ASL version being sent to them, and have no control over the frequency with which they receive the data and/or how up-to-date it is. When there is a time-sensitive matter, having to refresh a list to match a signature can be so difficult that the deal or trade fails, or in which to reach agreement lapses.

Fraud

Organisations on both sides of any transaction that require signatures are exposed to a high risk of fraud. Each day that a signatory list is inaccurate presents a serious fraud risk. This is particularly the case where a signatory leaves the organisation or is removed but the list is not updated or provided to those parties who rely on it. These persons can sign and the organisation will not know anything about it until it is too late.

Audit and compliance

From an auditor's perspective a company that does not demonstrate effective control over its finances and assets, for example failing to maintain accurate authorised signatory lists, will be deemed at risk. Many companies, especially in the banking sector, have statutory record-keeping obligations and are required to keep a clear audit trail of account-related documentation, including signatory data.

It is important that companies can demonstrate to their auditors that there is ongoing compliance with all relevant legal and regulatory requirements, internal account mandate controls and good corporate governance in relation to delegated authorities.

Regulated businesses

Regulated organisations, especially those managing or with fiduciary responsibility for third party funds and assets, ordinarily have an obligation to maintain effective systems and controls to prevent and deter financial crime. Failure by an organisation to do so, or where these are breached, could not only result in financial loss for itself or its clients, it will likely also be subject to regulatory sanctions or fines. A significant fraud or loss through negligence will impact its market reputation, insurance premiums or, at worst, its licence to operate may be suspended or revoked.

Case study: Mandate fraud

A small company's owner had a business account with a local bank where he had two authorised signatories/mandates.

One day, he intended to use his business credit card to withdraw money from an ATM and his card was retained. He then contacted the bank and found that his name was no longer associated with his company's account.

After further investigation, it turned out that an ex-employee of the company had sent a formal letter to the bank requesting the existing account mandates to be replaced by him. The bank then changed the mandate accordingly and the fraudster received full access to the account.

See some of our use cases >

"Authorised signatories are essential in any transaction involving companies of any size. If the signatory is not authorised the consequences can be severe not only for the company who fails to use an authorised signatory, but even those they are contracting with. The very first topic taught to aspiring corporate & commercial lawyers, is how companies can enter into legal documents and thus transactions through either a stamp or authorised signatory."

Michael Kashis,
Managing Partner of
Bishop & Sewell LLP

Legal cases of contract disputes and unauthorised signing

In this section, we've put together a list of some of the most prominent legal cases related to signature fraud and unauthorised signing.

Wrexham AFC v Crucialmove Ltd [2006]

In the Wrexham Associated Football Club Ltd v Crucialmove Ltd case, the Court of Appeal has decided that on an application for summary judgment, the court was entitled to find that a party did not act in good faith and to grant the application; issues concerning a party's integrity did not necessarily have to be left to a full trial for determination. In this case, it was clear that the buyer of a company's property was aware that a director of the company was making the sale in breach of his fiduciary duty and without the company's formal consent. The buyer was therefore not acting in good faith and so could not rely on the common law rules or statutory provisions protecting third parties in such situations. The contract was thus unenforceable causing losses to the buyer.

British Bank of the Middle East v Sun Life Assurance of Canada Ltd [1984]

In this case it was considered whether a bank manager had the authority to represent that one of the bank clerks had authority to advance a loan.

The transaction was a suspicious transaction, and in addition the court found that the branch manager clearly did not have authority due to the amounts involved.

Freeman & Lockyer v Buckhurst Park Properties (Mangal) Ltd [1967]

The popular case of Freeman and Lockyer (A Firm) v Buckhurst Park Properties (Mangal) Ltd. relates to determining the scope of the authority of a managing director, who is not properly appointed according to the articles of association to contract with a third party.

Freeman and Lockyer was a firm carrying on the business as architects and surveyors and Buckhurst Park Properties (Mangal) Ltd. formed the defendant company. Mr Shiv Kumar Kapoor and Mr Nimarjit Singh Hoon along with a nominee of each formed the defendant company. The Honourable Judge Herbert’s final decision was in the favour of plaintiffs and agreed that, despite the fact that Mr Kapoor was never been appointed as a managing director by the board, he had acted as such within the knowledge of the directors of the defendant company.

The defendant company appealed that decision in the Court of Appeal which was dismissed by Lord Diplock emphasising that it was not for the plaintiffs to inquire that the power to appoint Mr Kapoor as a managing director was contained in the articles of association and whether he was appointed as such. In the light of the decision of the Court of Appeal, the contract was considered valid despite the fact that it was signed by unauthorised company party and as a result the defendant company was liable for the payment of fees to the plaintiffs.

Campden Hill Ltd v Chakrani [2005]

In the Campden Hill Ltd v Chakrani [2005], the claimant company was entitled to recover monies paid into a solicitors' bank account under an unauthorised loan agreement secured against a client's property by a solicitor using forged documentation. As there was forgery found and the signature was not authorised by the client, the firm of solicitors was liable for the whole of the principal sum as well as the facility fee. The claimant was then entitled to trace into the majority of the funds paid out to the solicitor's client.

How to mitigate the risk of signature and signatory fraud. Read blog >

Managing authorised signers and contracts post-Covid

Authorised signatory lists were originally created to facilitate the management of authorised signatories and signature data by providing a level of confidence and accuracy. Unfortunately, the process by which signatory lists are maintained and distributed brings with it a number of weaknesses, allowing for mistakes to be made, lists to be exploited and fraud to occur.

What is the reality?

Due to the time-consuming nature of the task, lists are often not reproduced for individual departures and arrivals, but instead a periodic change is often chosen. The inconsistent approach leads to scenarios where employees are both on the list when they should no longer be or are not on the list when they need to be.

Signatory management of the future: Digital authorised signatory management

As with most operational deficiencies in business today, technology is sought to provide a solution and drive forward innovation. The nature of the authorised signatory lists process and its industry agnostic application means any technical answers to this problem must be simple, widely applicable and easy to integrate with legacy systems.

New advanced technologies like blockchain allow organisations to efficiently manage and share signatory lists in real time and have a complete and clear audit trail of all data changes. By digitally transforming the process of managing authorised signatory lists and using a dedicated signatory management solution like Cygnetise, organisations can now save over 90% of their admin costs and time, whilst significantly mitigating the risk of fraud.

> "The beauty of using blockchain technology for contracts is that it can bring together ledgers, agreements and payments improving the flow of commercial agreements, and it can capture, and potentially manage, any disputes. The types of terms and conditions usually seen in a legal contract can be added to blockchain payments. These are known as Smart Contracts and they can synchronise the release of payments with the delivery of goods, services, or even financial instruments," — ***PWC***

Signatory authorisation and the use of e-signatures

Following the impacts of COVID-19 and the shift to remote working, many organisations have started to move from using "wet signatures" to adopting electronic signatures. While e-signing enables business continuity and promotes efficiencies, it can also expose organisations to higher risks of signatory fraud, unauthorised signing and non-compliance.

What is an electronic signature?

According to the US Electronic Communications (ESIGN) Act 2000 and the 2019 Official Report by the UK Law Commission, an electronic signature is a signature in electronic form that is used on a digital document or communication.

Some of the most common types of electronic signatures include:

- a name typed at the end of an email,
- a scanned copy or photo of a hand-written signature,
- a signature made using a dedicated e-signature platform (e.g. DocuSign),
- a signature written onto a screen using a stylus.

What are the risks of using electronic signatures?

Generally, digital signatures tend to be more secure than traditional paper-based wet ink signatures as they're easier to track, especially if generated through a specific digital signature software. Digital signature software products or platforms also use encryption and decryption technology alongside public key infrastructure (PKI) adding an extra step of authentication to the signing process that aims to prevent tampering.

Despite this, there are still a number of risks organisations should consider when implementing e-signatures:

1) **Risk of fraud & reliability** – while using a dedicated digital signatory software platform can help solve any authentication issues of the e-signing process, there's still a high risk of signatory forging and fraud for organisations as technology can be compromised or hacked.

2) **Risk of unauthorised signing** – a major problem with both wet ink and electronic signatures is the risk of unauthorised signing. How can organisations ensure that all their signatories (including e-signatories) are appropriately authorised? How can they reliably monitor and report on their authorised signatories? Similarly, how do signatories know what exactly they are authorised to sign? This is particularly relevant where signatories act as such for multiple legal entities within corporate group.

3) **Risk of non-compliance** – in addition to regional and international electronic signature laws, organisations should also comply with rules and regulations for presenting documents, disclosures, and other information at certain stages during a transaction (e.g. MiFID, FCA). If organisations fail to comply, they face a risk of getting sanctioned and fined by regulatory authorities, lose accreditation status, or damage their brand equity.

See how Cygnetise works >

e-Signature legal case: Bendigo and Adelaide, Bank Limited v Pickard [2019]

The Pickards, through a family trust, subscribed for interests in Great Southern Group investments, and borrowed through Bendigo and Adelaide Bank. The Pickards were required to guarantee the borrowings.

The loan agreement and guarantee were. signed on behalf of the Pickards and. their family trust by Great Southern Finance Pty Ltd under a power of attorney. The directors of Great Southern Finance Pty Ltd signed the loan agreement and the guarantee electronically.

The evidence was that the company's practice for document signing was that administrative staff, not the directors, physically affixed the signatures. The directors could not prove they authorised the administrative staff to physically affix the signatures on their behalf.

The Court decided that, as the directors of Great Southern Finance Pty Ltd could not prove they had authorised the signatures to be placed on the documents, they had not been properly signed, and therefore the guarantees could not be enforced against the Pickards.

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At Cygnetise, we have developed an application that helps you reduce the risk of fraud, facilitate business continuity and contribute to ESG by digitising the process of authorised signatory management. Our technology enables users to update their lists in real time and has a variety of sharing mechanisms so that the counterpart can always have access to the most up-to-date information without you having to recompile and redistribute.

To learn more about Cygnetise and request a free demo, click here or email our team at info@cygnetise.com

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