



Hong Kong Law

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## RECENT HK CASE HIGHLIGHTS IMPORTANCE OF PROPER DOCUMENT EXECUTION

A recent Hong Kong case acts as a reminder of the importance of following the correct formalities for the execution of documents, and raises important issues in relation to the effectiveness of virtual signing and closing to constitute valid execution. “Virtual signings and closings” are now common practice given the logistical difficulties of arranging a signing meeting at which all parties can be physically present. The practice of preparing signature pages in advance to be affixed to the engrossed final form of the document for completion of a transaction has thus evolved.

**Recent Hong Kong case: Penta Investment Advisers Ltd v Allied Weli Development Ltd (formerly known as Hennabun Capital Group Ltd) [HCA 1656/2012] (the Penta Case)**

In the Penta case, the main issue for the Court of First Instance to determine was whether a guarantee (the **Guarantee**) in the form of a deed was properly executed by or on behalf of the defendant (who was the guarantor), and thus binding on it. It was held that the Guarantee was valid, but the case highlighted arguments that could potentially delay a simple contractual claim for payment.

### The Facts

Allied Weli Development Ltd (the **Guarantor**) (formerly known as Hennabun Capital Ltd), a company incorporated in the British Virgin Islands, provided a Guarantee to Penta Investment Advisers Ltd (the **Beneficiary**) to protect the Beneficiary from losses on its investment. When the Beneficiary lost on the

investment, it called on the Guarantor to honour its obligations under the Guarantee. However, the Guarantor disputed the validity of the Guarantee, alleging that the Guarantee in the form of a deed had not been duly executed.

The Guarantor gave the following reasons in support of its argument that the Guarantee had not been duly executed:

- i) When the director who signed the Guarantee was presented with the deed for signing, she was not given any details of the transaction;
- ii) The director signed underneath the words “in the presence of” and she claimed that she signed “as a witness to the existence of the ongoing negotiations” rather than in the capacity of a director; and
- iii) The director did not affix the common seal at the time of signing. The seal was affixed later by the company secretary but not in the presence of the director.

The Guarantor’s second line of defence was that even if the director had executed the deed on the Guarantor’s behalf, she did not have actual nor ostensible authority to do so. The Guarantor claimed that no board resolution had been passed authorizing the director to execute the deed and to affix the common seal to it.

The third argument made in the Guarantor’s defence was that the Guarantee did not benefit the Guarantor and thus was not binding on it.

The court rejected all the arguments and held that the Guarantor was liable under the Guarantee.

### 1. Implications for proper execution of documents

The Penta case underlines the importance of ensuring that documents are properly executed. It is worth noting that despite the judge rejecting the arguments raised by the Guarantor, it took the Beneficiary more than 2 years to obtain judgment as to the enforceability of the Guarantee. The question on the quantum due from the Guarantor to the Beneficiary is still pending.

#### 1.1 Execution of Documents

Formalities for the execution of documents are contained in the new Companies Ordinance (Cap.622) (the **CO**) which came into effect in March this year. Section 127 of the CO states that a company may execute a document by:

- i) affixing its common seal in accordance with the requirements contained in its articles of association (N.B.: the adoption and use of a common seal is optional under the new CO provided the company amends its articles of association accordingly); or
- ii) the document being signed by any two directors **or** any director and the company secretary **or** by its sole director in the case of a single-director company.

In favour only of a purchaser in good faith for valuable consideration, a document which is purported to have been signed in accordance with the above requirements is considered to have been duly executed by the company.

The above is the best practice for companies to follow in executing documents. A company which wishes to execute documents by the signature of any two of its directors (or a director and the company secretary) may amend its current articles of association to reflect this.

Alternatively, a company may adopt other methods for executing documents such as passing a directors' resolution appointing authorized signatories.

#### 1.2 Execution of Deeds

Section 128 of the CO states that a company may execute a deed by:

- i) executing a document in accordance with section 127 of the CO (see 1.1 above);
- ii) having the document expressed as a deed; and
- iii) delivering the document as a deed.

Notwithstanding the method of executing a deed set out in section 128 of the CO, a company may in its articles adopt specific procedures for the execution of deeds. A company's articles of association should therefore be reviewed in order to confirm whether a document has been properly executed.

### Procedures at virtual signings or closings

### 2. UK case: R (on the application of Mercury Tax Group Limited and another) v HMRC [2008] EWHC 2721 (the Mercury Case)

This is not a very recent case but it led to discussion as to the correct procedures at a virtual signing or closing. The facts of the Mercury case itself were not related to virtual signing and closing. The case involved a potentially legitimate tax avoidance scheme and whether the UK Revenue & Customs should have been granted a warrant to enter the Mercury Tax Group's premises to search for documents.

In an obiter comment, the judge held that the practice of Mercury Tax Group of transferring the signature pages from an incomplete draft deed (or contract) to a complete and amended final version was not legitimate. This was because the final version differed significantly from the draft, but the signatory was not informed of the changes. The final form of the deed was therefore found not to be valid. In relation to deeds, the judge said that "*the signature and the attestation must form part of the same physical document*"; while in relation to all documents (applicable to all contracts, whether deeds or not), the judge said that "*the document to be signed exists as a discrete physical entity (whether in a single version or in a series of counterparts) at the moment of signing*".

### 3. Implications for the practice of virtual signing or closing

The Mercury case caused widespread concern as many transactions are signed or closed at virtual signings and closings. Signing pages were usually separated from the whole documents and then attached to the remainder of the document to constitute a valid execution.

In February 2010, a joint working party of The Law Society Company Law Committee in the UK, The City of London Law Society Company Law and Financial Law Committees (the **JWP**) published a *Note on execution of documents at a virtual signing or closing* (the **Note**) that updated its original guidance note May 2009. The Note has been approved by Leading Counsel (Mark Haggood QC). Although the Note is not binding on courts, it has shaped the development of agreed procedures in this area.

The Note confirms that:

- 1) The Court of Appeal decision in *Koenigsblatt v Sweet* [1923] 2 Ch 314 (**Koenigsblatt**) remains the leading authority on the applicability of the principles of authority and ratification to the creation of legally binding written agreements (Note: *Koenigsblatt* established that an amendment to a pre-signed document can be binding if the amendments have been authorized prospectively or through ratification); and
- 2) The Mercury case as a first instance decision should be viewed as limited to its particular facts and, to the extent inconsistent with *Koenigsblatt* (a Court of Appeal decision), the *Koenigsblatt* decision should prevail.

Nevertheless, on a cautious assumption that the *Mercury* case may have wider application beyond its specific facts, the JWP considered that contracts can be circulated for signature by email and summarizes the appropriate procedures and options for execution requirements for virtual signing and closing under English law.

### 3.1 Option 1: Returning by e-mail the entire document and the signed signature page

#### ***Suitable for deeds, guarantees and other simple contracts***

- 1) When the documents are finalized, the final execution copies should be emailed to all the parties and/or their lawyers. For convenience, a separate document containing the relevant signing pages may be attached.
- 2) After each signatory prints and signs the signature pages, each party should return a single email to its lawyer or the lawyer co-ordinating the virtual signing or closing attaching:
  - i) the final version of the document (which can be copied from the execution email which was sent out earlier); and

- ii) a pdf copy of the signed signature pages.

In the case of deeds executed using this method, the email should make clear when delivery of the deed should take place, or alternatively, make clear that the deed should not be taken to be delivered merely because it has been signed and the above steps have been followed.

- 3) At or shortly after signing (or closing), a final version of the document, together with copies of the executed signature pages, can be circulated as evidence of execution of the final document.

An alternative to this method would be for each party to print out all the finalized documents, sign each on its signature page, and then return an email attaching the pdf version of the entire documents (including the signature pages).

JWP considered that a single email attaching both the final version of the documents and the signed signature pages satisfies the requirement in the Mercury case that the signature and attestation are part of the “*same physical document*” when the deed is signed.

It should be noted however that another original of the document with “wet ink” signatures of all the parties may be necessary if the document has to be filed or registered.

### 3.2 Option 2: Print off and sign signature page

#### ***For all contracts not executed as a deed***

- 1) When the documents are finalized, the final execution copies should be emailed to all the parties or their lawyers. For convenience, a separate document containing the relevant signing pages may be attached.
- 2) After each signatory prints and signs the signature page only, each party should email its signed signature pages only to its lawyers or the lawyers co-ordinating the signing or closing, with authority to attach them to the final versions of the documents.

The only difference between option 1 and option 2 is that for option 2, there is no need to re-attach the final version of the document in the email when returning the signature pages.

The original signed document is created when the final version of the document is printed out and the signature pages are attached to it.

### **3.3 Option 3: Pre-signed signature pages collected before documents (not executed as deed) are finalized**

- 1) Before the final version of the document is agreed by the parties, the signature pages are circulated to the parties for signing.
- 2) The signature pages are then returned to the relevant lawyer by email (as pdf attachments) or by courier, to be held to the order of the signatory until authority is given for them to be attached to the final version of the document.
- 3) Once the document is finalized, the law firm co-ordinating the signing or closing emails the final version of the document to each party and obtains confirmation from them that they have agreed the final version of the document and authorizing the relevant law firm to attach the pre-signed signature pages to the final version, and to date and release the documents.

This option is used when signatories are not available to sign a document on the date of signing, but are able to provide authorization.

The original signed document is created when the final version of the document is attached with the pre-signed signature pages with the approval of the relevant parties.

### **4. Conclusion**

The Companies Ordinance sets out the formalities for the execution of documents and deeds. However, it does not touch on the procedures for virtual signings and closings. The Law Society of Hong Kong has not published guidance on virtual signings or closings. To ensure the proper execution of documents, the requirements of the Companies Ordinance should be followed. As to the arrangements for the execution of documents at virtual signings or closings, it would be prudent to refer to the JWP's *Note on execution of documents at a virtual signing or closing* which is described above.

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