LC Paper No. CB(2)1401/01-02(02)

The Bar's Submissions on the proposed amendments to the Conveyancing and Property Ordinance relating to the execution of conveyancing documents by corporations

Introduction

1. The Law Society has submitted a case ("**the Case**") to the Government proposing certain legislative amendments to the Conveyancing and Property Ordinance, Cap. 219 ("**CPO**"). Under cover of its letter dated 14th January 2002, the Department of Justice sent a consultation paper ("**the Consultation Paper**") to the Bar Chairman inviting the Bar to make comments on the Consultation Paper.

Background

2. The Government has set out the relevant background in the Consultation Paper. It is not necessary to repeat the same again in this report. Suffice for me to point out, in relation to the advice which the Law Society obtained from the London QC in 1990 and 1991, that it was already perceived by the Law Society at that time that the problem of proving due execution of conveyancing documents by corporations was a common one. In their Instructions to Counsel (referred to in Law Society Circular 105/90 dated 29th May 1990), Messrs. Edmund Cheung & Co. acting for the Law Society described the problem as follows:

> "It is recognized that in Hong Kong there are a large number of cases where board resolutions or powers of appointments authorizing the execution of conveyancing documents by corporations are missing from the relative title deeds and some of those corporations are no longer in existence. It

> follows that in such case it is impossible for a vendor of land to obtain the necessary resolution or power of appointment….."

3. Although no statistical evidence (and it may be impossible to have such evidence) was available on how widespread was the perceived problem, it must be taken that the collective "front line" experience of those members of the Law Society who engaged in handling conveyancing transactions everyday would provide a good assessment of how common was the difficulty. This is also to some extent evidenced by the number of cases which found their way to the Court since the time when the advice of London QC was obtained. Annexed to this report is a list of cases (not meant to be exhaustive) between 1991 and now in which the Hong Kong Courts dealt with the issue of corporate executions in the context of conveyancing transactions.

4. If the problem was perceived in 1990 or 1991 by the Law Society as one that existed in "a large number of cases", it is unlikely that the problem would be any less common now. For, as pointed out by the Law Society in paragraph 7(D) of the Case, conveyancing practice has in the past been based in good faith on the advice of the London QC who advised that the protection given by Section 23 of the CPO was more extensive than the subsequent authorities have established to be the case. No doubt there must have been many transactions in the past ten years which were structured in accordance with the advice of the London QC. The problem has thus been perpetuated in the past 10 years.

5. Thus, as a preliminary observation, it might be said that the Administration have underestimated the position when it queried, in paragraph 36 of the Consultation Paper, the wisdom of relaxing the established formal requirements of corporate execution "for the purpose simply of dealing with a small number of past formally defective assignments". All indications show that the problem is not limited to a small number of past formally defective assignments. We are of the view that the concern of the Law

Society's concern is legitimate. Whether it should be addressed by legislative intervention is of course another question to be canvassed later in this report.

The Law Society's critique of Grand Trade

6. As can be noted in the list of cases set out in the Annex to this report, until the recent decision of the Court of Appeal in **Grand Trade Development Ltd. v. Bonance International Ltd.** [2001] 3 HKC 137, all the decisions, except the decision of **Hillier Development Ltd. v. Tread East Ltd.** [1993] 1 HKC 285, were all decisions of first instance. The case of **Hillier Development** is often said to be restricted to the special facts of the case (rather unusually, the assignment in that case described the signatory as "one of its directors as directed and authorized by the board of directors to sign"), and there were little discussions in the Court of Appeal's judgment on the general principles regarding corporate execution in the present context (the Court of Appeal in **Hillier Development** was more concerned with other issues raised in the appeal). Thus the **Grand Trade** decision was the first decision emanating from the Court of Appeal in which the general principles involved were discussed at some length.

7. The judgment of **Grand Trade** has been analysed and summarized by the Law Society in paragraph 1 of the Case. To that summary may be added the following:

(1) by virtue of the combined effect of s.11(2) and Article 114 of Table A, the distinction drawn by the Courts in some cases before **Grand Trade** (notably **Lo Wing Wah v. Chung Kam Wah** [2000] 1 HKLRD 227, **Chan Sai Hung v. Well Develop Ltd**. [2000] 4 HKC 50 and **HongKong and Shanghai Banking Corp Ltd v. Ho Sin Yi**, HCMP 5420/2000, unreported) between what was sometimes called a "deeming provision" and a "mandatory provision", was held by the Court of Appeal to be an inconsequential distinction. Even if the relevant provision

in the Articles of Association of the company concerned was only a "deeming provision" in the sense that it did not mandatorily require the seal of the company to be applied in a certain manner, by reason of Article 114 of Table A (which applied to every company unless excluded or modified by the company's Articles), the company could only affix its seal in accordance with the mandatory requirements provided in that Article. Article 114 of Table A expressly requires the sealing to be accompanied by the signature of a director *and* countersigned by the secretary or by a second director or by some other person appointed by the directors for the purpose;

(2) it is also important to note the approach of the Court of Appeal in its emphasis on the effect of a formally defective assignment in terms of the passing of the legal estate (see the judgment of Le Pichon JA at p.147F to 148B, 153D-G). At 148I of her judgment, her ladyship held:

> "I do not read the ***Peking Fur Store*** case as authority for the proposition that the affixing of the company's seal outside the strict requirements of the articles themselves is sufficient to constitute the document a deed of the company so that the legal estate passes…."

This approach of the Court of Appeal highlights the consequence of formal defects from the point of view of the passing of the legal estate. Such an approach contrasts starkly with the "risk approach" adopted in some cases. Some of the cases in which the "risk approach" was adopted have been referred to in paragraphs 43 and 44 of the Consultation Paper. We shall return to this point later when we address the need for legislative intervention.

8. It is the Law Society's view that the **Grand Trade** decision was

incorrect. In paragraph 2 of the Case, the Law Society gave two reasons for its view. They are:

(1) that because the Articles of the company in **Grand Trade** provided that the seal should not be used except with the board's authority, the affixing of the seal on the assignment "must on the face of it have been used with the authority of the board". The Law Society complains that the Court of Appeal has failed to consider the issue of estoppel;

(2) that the judgment has deprived section 23 of its legal effect for deeds executed by a corporation. The Law Society reasoned that if the description in the deed followed the exact wording of the articles of association, the deeming provision of the articles of association would apply and there was no need for the vendor to rely on the presumption under section 23. If the execution of the document was in accordance with section 20 there was already an irrebuttable presumption and, again section 23 would not be applicable. The Law Society therefore argued that the legislative intent could not be that postulated by the court.

9. With great respect to the Law Society, we do not think that the first reason given by it for criticizing the correctness of the judgment of the Court of Appeal is sound. If the Court be right in considering (as to that, there may be *other reasons* for saying that it is *not* right) that on the face of the instrument in question, the instrument had not been executed in accordance with the formal requirements provided under Article 114 and the deeming provision provided in the company's Articles, we do not see how any question of estoppel could arise in the absence of other extrinsic circumstances (and there were no other relevant extrinsic circumstances in that case). It begs the question to argue that the seal must have been used with the board's authority by referring to the Articles, when those Articles themselves (including Article 114 as incorporated into them by statute) required the use of the seal to comply with certain formal requirements and those requirements had not been

complied with. The mere fact that the seal was affixed to the instrument in question cannot possibly by itself raise an estoppel against the company if the requirements provided in the Articles had not been followed.

10. As to the second reason given by the Law Society, it is true, as pointed out by the Administration in paragraph 14 of the Consultation Paper, that the interpretation of section 23 has been settled by the Court of Appeal in favour of the narrower approach. But it would be an exaggeration to say that the Court of Appeal's judgment has "deprived section 23 of its legal effect for deeds executed by a corporation". In **Grand Trade**, the Court of Appeal did recognize that section 23 would have the effect of saving the need to prove that the person described in the deed as being authorized by the board to sign was in fact so authorized. This is clear from p.150A-D of the judgment where the Court of Appeal accepted that **Hillier Development** was correctly decided, impliedly accepting that no actual proof would be required for the authority of the signatory if it had been stated on the face of the document that he was so authorised. So it cannot really be said that **Grand Trade** has deprived section 23 of all legal effect, but it is true that it does give it an interpretation much narrower than what the London QC has previously advised the Law Society.

11. Is the narrow interpretation a correct one? In our view, perhaps not. We have not found the Court of Appeal's analysis on section 23 and the Turquand's rule convincing. But one must accept that unless **Grand Trade** is overruled by the Court of Final Appeal, the judgment represents the current state of the law. So it may not be particularly helpful to spend a lot of time examining the arguments for and against the correctness of the decision (indeed that is not the point of the consultation). We would therefore only set out our views very briefly in this regard:

(1) on section 23, as held by the Court of Final Appeal in **Leung Kwai Lin Cindy v. Wu Wing Kuen** [2001] 1 HKC 567, the section "is remedial, to facilitate conveyancing. It must

receive a fair, large and liberal construction" (per Litton NPJ at 577E). "The section is beneficial and facilitating. So it should receive a liberal construction" (per Sir Anthony Mason, to whose judgment Li CJ, Bokhary and Chan PJJ agreed). In approaching s.23, the Court of Appeal emphasized that the section required the appearance of due execution, namely that it must *on its face*, appear to be duly executed (see p.150A). It is however not clear what exactly did the Court of Appeal mean by saying this. If one takes the words "on its face" strictly and literally, presumably one can *only* look at the document within its four corners for the appearance of due execution, and is not permitted to look at anything else, including the Articles of Association. However, if all that one can do is to look *only* at the document in question without reference to the Articles, it is almost impossible in nearly all cases to decide whether the document "appears to be duly executed" or not. If, for example, one looks at the document and finds it to be signed by a single signatory described as "Chairman", or simply as "a director", how can one possibly say whether the purported execution "appears" to be proper or not? On the other hand, if one is permitted to look at say, the Articles for the appearance of due execution, and one finds in the Articles a provision (as in **Grand Trade**) to the effect that the seal is deemed to have been properly applied if the document is signed by "such person or persons as the Board may from time to time authorize for such purpose", then why is the appearance of due execution lacking just because the words "authorized by the board" was not stated on the document itself? On the face of the document as read together with the Articles, the board could have authorized a single signatory to accompany the use of the seal, and a single signatory did accompany the seal on the face of the document. Why is the appearance of execution lacking? The Court of Appeal in **Grand Trade** did not explain this. The Court pointed out that there are features in the execution of the document in the **Hillier Development** case which are

not found in the **Grand Trade** case, and distinguished **Hillier Development** on that ground. However the fact that **Hillier Development** has those special features does not necessarily mean that the case would have been decided differently even if those features were not present. In our view, if s.23 is to be given a liberal and large interpretation (as the Court of Final Appeal held), no convincing reason has been advanced by the Court of Appeal for favoring the narrow interpretation. We think a lot may be said in support of the wider interpretation favored by the London QC who gave the advice to the Law Society;

(2) Similar criticisms may be leveled against the judgment of the Court of Appeal in the way it disposed of the arguments based on the Turquand's rule. For the reasons set out in the judgment, the case of **Registrar General v. Northside Developments Pty Ltd** (1988-1989) 14 ACLR 543 is distinguishable. However, the mere fact that the case is distinguishable on its facts does not necessarily establish that the Turquand rule is not applicable to a case such as the one in **Grand Trade**. Having distinguished the **Northside** case, the Court of Appeal did not adequately explain why the Turquand's rule was not applicable. It appears that the Court of Appeal simply jumped to the conclusion that the Turquand rule was of no assistance once it was shown that the **Northside** case could be distinguished on its facts. This does not appear to me to be a convincing approach. If the board could have authorized the person signing the document to sign it, what is there to prevent the indoor management rule to apply in favour of a third party acting in good faith to assume that the board had in fact authorized the signing? In paragraph 3 of the Case, the Law Society refers to the case of **British Thomson-Houston Company Limited v. Federated European Bank, Ltd.** [1932] 2 KB 176. That is a case involving the signing of a guarantee and it appears from the report in that case that no question of sealing is involved. So again the facts of the case are

different. However the principles applied by the Court, relying on the Turquand's rule, are in our view equally applicable to **Grand Trade**. As Sir Wood, Vice-Chancellor observed in the case of **In re the Athenaeum Life Assurance Society, ex parte Eagle Insurance Co.** [1858] 4 K&J 549 at 561:

> "Thus, where the deed requires certain instruments to be under the common seal of the company, every person contracting with the company can see at once whether that requisition is complied with, and he is bound to do so; but where, as in the case I have last referred to, the conditions required by the deed consist of certain internal arrangements of the company–**for instance, resolutions at meetings, and the like**–if the party contracting with the directors find the acts which they undertake to do to be within the scope of their powers under the deed, he has a right to assume that all such conditions have been complied with. In the case last supposed he is not bound to inquire whether the resolutions have been duly passed, or the like, otherwise he would be bound to go further back, and to inquire whether the meetings have been duly summoned, and to ascertain a variety of other matters, into which, if it were necessary to make such inquiry, it would be impossible for the company to carry on the business for which it is formed."

The principles stated by Sir Wood are in our view applicable to the facts of **Grand Trade**. These principles are also supported by cases such as **Biggerstaff v. Rowatt's Wharf Ltd.** [1896] 2 Ch 93, **Morris v. Kanseen**

[1946] AC 459 etc.

The need for legislative intervention

12. Whatever views one may have over the correctness of the **Grand Trade** decision, the decision represents the current state of the law. The more important question is, has a case been made out for legislative intervention?

13. Even assuming that the **Grand Trade** decision has been decided incorrectly, as contended by the Law Society, there is no certainty at all as to when the Court of Final Appeal might have the opportunity of correcting the decision. It is to be noted that despite a plethora of cases which found their way to the courts since the Law Society obtained the advice of the London QC, it was only in mid-2001 that the Court of Appeal was presented with the opportunity of considering this area of the law in the case of **Grand Trade (**discounting the case of **Hillier Development**, in which the issue presently being considered was not directly raised in the appeal). The time when the Court of Final Appeal will have the occasion of considering the point again is anybody's guess.

14. What must be recognised is the gravity of the problem as perceived by the Law Society, whose members are obviously in the front line, as pointed out above, in the handling of conveyancing transactions in Hong Kong. Back in 1990 or 1991, the Law Society had clearly drawn on the collective experience of its members before sounding the warning that the problem was widespread and existed in a large number of cases. There is no reason to think that the Law Society was sounding a false alarm when it took the trouble of going to a London QC for advice. In the past 10 years most solicitors have acted upon the advice of London QC when putting through transactions involving corporate executions. If they are to change their practice now, only to find that the **Grand Trade** decision is ultimately found (say, by the Court of Final Appeal in a few years time) to be incorrectly decided, much harm and confusion would be done to the conveyancing practice in Hong Kong.

15. What weighs heavily in favor of legislative intervention is the consideration of the grave injustice that may be caused to many property owners in Hong Kong as a result of the **Grand Trade** decision. The decision would render the title of many properties in Hong Kong defective. Particularly in a weak property market, many of these properties would become unsaleable in practice. The injustice is compounded by the fact that in many cases, when these owners purchased the properties concerned, solicitors acting for them had probably accepted title on the basis of the correctness of the London QC advice. To many, the sudden change of the law would have the effect of rendering their properties unsaleable, through no fault of their own.

16. The reason why properties may become unsaleable as a result of defective corporate execution requires some elaboration. As pointed out in paragraph 8(2) above, the Court of Appeal, in our view correctly, looked at the legal consequence of defective execution from the point of view of *the passing of legal estate*. If an assignment is defectively executed by a company, it will not be effectual in passing the legal estate. The result is that unless the present owner is able to find a purchaser who is prepared only to buy an equitable estate, he will not be able to prove good title: that is so even if there is little or no risk at all that the company whose execution is being questioned will turn up to challenge the effectiveness of the assignment.

17. As pointed out in paragraph 8(2) above, there are some decisions decided by the Court of First Instance which adopted the "risk approach". Much may be said of the common sense underlying these decisions and no doubt the Courts in those cases were concerned to do practical justice by seeking to find a practical solution out of the problem. If there is no real risk of the company coming forward to set aside the defective assignment (for instance, where the company concerned was already wound up a long time ago and it is fanciful that the ghost of the company would "rise from its grave" to haunt the assignment now), why should the title

be rendered defective just because the execution was formally defective?

18. Despite the common sense attraction of the "risk approach", it is difficult to justify the approach legally. It would have been correct to adopt the risk approach if the problem was one of incumbrance to title. Where the problem is merely one of incumbrance to title, there is no question of the legal estate not passing. In that sort of situation the problem is whether the legal title is subject to incumbrance and the relevant question to be asked is whether there is any real risk of a successful assertion by the incumbrancer. If there is no such risk, the incumbrance may be ignored. That follows from the famous case of **MEPC Ltd. V. Christian-Edwards** [1981] AC 205 ("**the MEPC principle**").

19. But there is no room to extend the MEPC principle to a situation where, as in the case of **Grand Trade**, the question is not whether the title is subject to incumbrance, but the more fundamental one of whether there is any legal title at all. As to this, it is important to bear in mind the basic legal requirement for the passing of legal estate. Section 4(1) of the CPO expressly provides that a legal estate in land may be created, extinguished or disposed of *only by deed*. Further, by virtue of s.44(1) of CPO, mortgage of a legal estate may be effected at law *only by a charge by deed* expressed to be a legal charge. Without a deed, a legal estate cannot be sold, mortgaged or otherwise disposed of. Thus a properly executed deed is essential for the passing of the legal estate.

20. In this connection, we beg to disagree with the view expressed by Mr. Ho Koon Ki Tommy in his article published in (2001) HKLJ 105 entitled "Due Execution: By what Criteria?", referred to in paragraph 41 of the Consultation Paper. At p.107 of his article, the learned commentator stated that "the better view is that, *although the legal title passes* by the affixing of the company seal…..[the formally defective] assignment is *voidable* at the instance of the company". No authorities have been cited for that proposition. We do not know how much Mr. Ho might have been affected by

the much-quoted statement of Willes J in **Agar v. Athenaeum Life Assurance Society** [1858] 3 CB (NS) 725 at 756 in advancing this view, but for reasons admirably set out in the judgment of **Grand Trade**, the general statement of Willies J must not be read out of the context of the facts of the case of **Agar**, and it is clear that Willes J's statement is a statement of the common law rule applicable only in the absence of any express provisions in the articles regarding the use of the company's seal (see p.149B-C of the judgment of **Grand Trade**).

21. A defectively executed deed is not a deed at all. It is not capable of passing the legal estate irrespective of the question of risk. Subject to any express agreement to the contrary (which would be rare), the passing of the legal estate is fundamental to any sale of properties. If the vendor is not able to pass the legal estate to the purchaser upon completion, the purchaser will not get what he has bargained for. The MPEC principles have no application to such a situation. Accordingly, it is submitted that the Court of Appeal in **Grand Trade** is right in highlighting the problem of defective execution from the point of view of the passing of the legal estate. Cases such as **Peking Fur Store Ltd. v. Bank of Communications** [1993] 1 HKC 625, **Hui Yuk Chun v. Tang Wai Hang Henry** [1998] HCMP No. 1 of 1998 and **Lo Wing Wah v. Tang Wai Hang Henry** [2000] 1 HKLRD 227, insofar as they may be said to be cases that support the "risk approach", should be read with caution in the light of the approach of the Court of Appeal in **Grand Trade**.

22. If the consequence of defective execution is that legal estate cannot pass, then unless the execution can be remedied, the absence of risk will not help to save the legal title. In cases where rectification of the execution is impossible (for reasons set out in paragraph 5(C) of the Case – those reasons are very real), the properties concerned would in effect be unsaleable, for it would be difficult, if not impossible, for a purchaser to be found who is willing to take an equitable title only. If attempt is to be made in the provisional agreement to limit the title sold to equitable title only, a vendor

must be prepared to give a very substantial discount on price in order to entice a purchaser to accept such an unusual term. In this connection, one would remind oneself of the incisive remarks made by Recorder Tang SC in the case of **Wu Wing Kuen v. Leung Kwai Lin Cindy** [1999] 3 HKC 310 at 315B-E regarding the practical consequences of making special provisions in provisional agreements when a vendor comes to sell his property.

23. Owners of such properties are thus in a most helpless position. There is little that they could do to save their title. If the problem is as common as the Law Society perceives it to be, the problem should be addressed as soon as possible. Cases like **Grand Trade** are bound to arise frequently. Legislative intervention appears to be the best way out. For reasons set out in paragraph 5 of the Case (which we agree), non-legislative solutions do not appear to be practical. Title insurance is presently not commonly available in Hong Kong; rectification is in many cases not possible; and it is impractical to expect a vendor to make special provisions in provisional agreements limiting the title to be sold to equitable title only.

24. Apart from the problem created by the situation considered in **Grand Trade**, there are other corporate sealing situations, not considered in **Grand Trade**, which may cause problems. For example, in **Lim Shui Chun v. Billion Light Investment Ltd**. [2000] 2 HKC 621, Deputy Judge held, in reference to Requisition No. 6 identified at p.626D-G of the report, that a board resolution was required to prove that the seal had been properly affixed despite that the relevant assignment was in fact signed by a director described as such, and the Articles of the company only required the seal to be affixed "in the presence of a director". The Deputy Judge's reason for so holding was that, although the Articles only required the seal to be affixed in the presence of a director, it also provided that the seal could only be used "by the authority of a resolution of the Board of Director". The Deputy Judge rejected the argument based on the Turquand rule by holding that the rationale in Turquand "is irrelevant and affords no answer

to the requisition" (see p.626G). Why that is so the Deputy Judge did not explain (Incidentally it is not clear how the argument based on the Turquand rule was advanced by the Defendant who, according to the report, was acting in person and was absent at the hearing). It is also noted that the case of **Hillier Development** was not cited or referred to in the judgment.

25. Thus the problem of sealing formalities may not feature only in the form of accompanying signatures (as in **Grand Trade**), but in other ways. **Lim Sui Chun** is an illustration. One commentator has taken the view that the case has been wrongly decided (see Part 2 of Professor Philip Smart's article in Hong Kong Lawyer (October 2001) at p. 46-47). Indeed one would have thought that the facts in **Lim Sui Chun**, insofar as it relates to Requisition 6, presents a classic case for the Turquand rule to apply. Be that as it may, it is not right to assume that **Grand Trade** has settled once and for all the law relating to corporate sealing. Problems can arise in a variety of forms. That however does not mean that the proposed legislation should be drafted as widely as possible to cover all eventualities. It may be better to let cases such as **Lim Sui Chun** to be sorted out in the Courts rather than by legislative intervention. We note that in the Case, the Law Society has not addressed the need for legislation to deal with situations like **Lim Sui Chun**. We can only assume that the Law Society does not see that there is any acute problem arising from that case which would require legislative intervention.

The proposed section 23A

26. The Law Society has suggested a draft section 23A to be introduced into the CPO. The draft has been set out in paragraph 6 of the Case.

27. As pointed out by the Administration in paragraph 26 of the Consultation Paper, the proposed s.23A (1) has been drafted in very wide terms. If the proposed s.23A (1) is to become part of the law, a very wide presumption would be introduced into the law

with the effect that all conveyancing documents are presumed to have been duly executed until proof to the contrary. Such a presumption goes well beyond the "mischief" complained of by the Law Society and we are unable to see that a case has been made out for the need of legislation of such breadth and width.

28. Not only is the proposed s.23A not limited to addressing the situation in **Grand Trade (**which concerns the affixing of the common seal of a company attested by a single signatory), it is not limited to corporate execution of deeds at all. As can be readily seen, the proposed presumption is intended to be applicable to all deeds *or other instruments*, whenever executed, relating to conveyancing. Presumably the word "instrument" as used in the proposed s.23A will have the same meaning as that defined in s.2 of CPO, namely "any document having legal effect except a will". Thus the proposed presumption will apply to all contracts, nominations, security agreements, equitable charges, and all other documents intended to have legal effect (except a will) relating to land. The presumption is certainly not confined in its application to the problem relating to sealing formalities.

29. In paragraph 27 of the Consultation Paper, the Administration pointed out that in cases where the articles cannot be found it is likely to be impossible for the contrary to be proved (i.e. to prove that the articles do not in fact allow the execution in a particular manner) and the proposed presumption under s.23A(1) would in effect be converted into a irrebuttable presumption. The Administration expressed the concern that a vendor with a problematic title might then be inclined to intentionally lose the articles, relying instead on the protection of the proposed presumption.

30. We agree with the Administration's view to the extent that *in cases of execution of deeds*, and the articles cannot be found, it is likely to be impossible for the contrary to be proved. However, in cases of companies incorporated in Hong Kong and overseas companies registered under Part XI of the Companies Ordinance, the concern

about a vendor with a problematic title intentionally "losing" the Articles appears to me to be more illusory than real. This is because in most cases, by virtue of the requirement under s. 15 of the Companies Ordinance, the memorandum and articles of a company have to be registered in the Company Registry. Thus a party disputing the execution can, in most cases, obtain a copy of the articles of the company concerned from the Company Registry and intentional "losing" of the articles by the vendor will not normally achieve the purpose. This applies to all Hong Kong companies as well as oversea companies with a place of business in Hong Kong, as the articles of such overseas companies are also required to be registered under s.333 of the Companies Ordinance.

31. However, the Administration's concern would be valid for foreign companies which do not have a place of business in Hong Kong and are not required to be registered here. There would be every incentive for a vendor not to produce the articles or charter or other constitutional document of a foreign company which might contain provisions regarding the mode by which deeds may be executed by the company. To do so would be foolish: the deed would be presumed to have been duly executed until the contrary is proved.

32. What is of even greater concern is the application of the proposed presumption to other documents which are not deeds. Documents which are not deeds are not required to be sealed, and the provisions commonly found in articles of association regarding sealing formalities are thus not applicable. For contracts made on behalf of a company, s.32 of the Companies Ordinance provides for the form of contracts required by law to be effectual in the cases provided therein. Subject to s.32, no particular formal requirements are applicable to corporate execution of documents which are not deeds. As to authority to make contracts on behalf of a company, the same is governed by the general law. For example, a managing director would normally have the usual authority to enter into contracts on the company's behalf, while a clerk would not normally have such authority unless he has been held out by

the company to have the necessary authority, in which case apparent or ostensible authority may be relied upon.

33. In paragraph 28 of the Consultation Paper, the Administration instanced the case of a corporate conveyance executed by someone described as a clerk and observed that there was no reason why purchasers should be required to accept such obviously defective titles. Insofar as the example relates to a corporate conveyance, perhaps the answer to the Administration's point is that unless the articles cannot be found from the Company's Registry, the purchaser would be able to prove the contrary by producing the articles which would normally provide for the type of persons who would be required to attest the company's seal. If the articles concerned do allow any person authorized by the board to attest the use of the company seal, then there is no reason why a clerk cannot do so. In the absence of proof to the contrary, there is no injustice caused by allowing a purchaser to assume, in a case where the articles allows the board to authorize *any person* to use the company's seal, that the board has in fact authorized the clerk to do so. If the articles do not allow, directly or indirectly, such a person to attest to the company's seal, then of course the contrary may be proved simply by producing the articles.

34. The same however cannot be said of documents which are not deeds. The articles are usually silent on the execution of such documents. Take an example of a clerk who purports to execute, on behalf of a company, an agreement for sale of a piece of land. He might have purported to sign the same without using the company's chop or any other indication that he has been authorized to do so. Yet if he has purported to sign on the company's behalf, the presumption under s.23A(1) will immediately bite to presume that the agreement so signed has been duly executed. Production of the articles of the company will not help to prove the contrary. The burden will lie on the party seeking to dispute the execution to prove that the document was in fact not properly executed. This is going to be a drastic change of the law, and certainly goes very much beyond s.23 which requires the

relevant instrument to have an appearance of due execution before the presumption under that section will bite. We do not see that any case has been made out for such a change and for that reason, the Bar do not support the enactment of a presumption in the form of s.23A(1).

35. The objection to the proposed s.23A(1) does not stop here. Even in the case of deeds, as pointed out above, the proposed s.23A goes well beyond the "mischief" identified in the Case. For example, the proposed presumption would make it difficult for a party to challenge the execution on the ground of say, apparent discrepancy in the signatures. This is because the presumption goes beyond sealing formalities and applies to other aspects of execution. Assuming a company purchased a property and the assignment was executed by the use of the common seal and signed by a single signatory (say, described as the Chairman) whose identity was disclosed in the assignment. 2 days later the company sold the property and the assignment was executed in the same way and purportedly signed by the same person except that the signature of the signatory was significantly different from the one in the previous assignment. Under the present law, a requisition may legitimately be raised on the discrepancy in the signatures but the proposed s.23A would make it very difficult to pursue such a requisition as the burden is casted upon the party disputing the execution to *prove* the contrary. It is to be noted that the sub-section requires proof to the contrary, and not just "in the absence of evidence to the contrary".

36. For completeness sake, it should also be pointed out that if the proposed s.23A(1) is enacted into law, the law regarding execution of deeds on behalf of a corporation would need to be examined with some care. Under the present law, by virtue of s.20(1) of CPO, where a person is empowered to execute a deed by a corporation, he may execute the deed as agent by signing the name of the corporation or his own name and by affixing his own seal. It is to be noted that s.20(1) only permits such execution by an agent where the person is empowered to execute a deed by a corporation,

and one would normally have to look at the articles to see if the person purportedly signing as agent is in fact so empowered. Such empowerment has to be express. However, if the proposed s.23A(1) is enacted into law, the presumption therein would have the effect of dispensing with such empowering requirement. Assuming that a company's articles is wholly silent and does not expressly empower any person to execute deeds as agent on its behalf. Under the present law, s.20(1) would not be applicable. However, if s.23A(1) is to become the law, a person who purportedly executes a deed on behalf of the company as agent, signing in his own name and using his own seal, would be presumed to have duly done so until the contrary is proved. This is so because the presumption in s.23A(1) would apply to any deed "purporting to be executed ….. *on behalf of* a corporation aggregate", and this clearly includes the purported execution by someone who describes himself as agent executing on the company's behalf. The presumption would apply even if the articles do not expressly empower such execution, for silence is not proof to the contrary.

37. Examples such as those mentioned above may be multiplied. It is unlikely that in proposing the new legislation the Law Society has intended to cast the net so wide. However, the width of the draft presented by the Law Society is such that there would be a lot of room for such unintended "side-effects". For these reasons, s.23A(1) should not be supported.

38. Turning to the proposed s.23A(2), the proposed sub-section is casted in narrower terms, and is in effect a statutory form of the Turquand's rule, with the additional clarification that no express description is required to be made in the deed or instrument of the authority of the signatory in question. The sub-section is therefore directed to overruling **Grand Trade** by legislation.

39. We have 2 reservations regarding this sub-section. Firstly, we have reservation whether the sub-section should be made to apply to instruments other than deeds. The problem alluded to by the Law

Society in the Case relates to the sealing of deeds only, and in any event, it is unusual for the articles to contain specific provisions regarding the authority of any person to execute documents which do not require the use of the common seal. Secondly, we have reservation to the words "or entitled to" in the draft. Assuming that the articles of a company allows, directly or indirectly, the board to authorize any person or persons to attest to the use of the company's seal. Let us also assume that a special resolution has in fact been passed by the company to the effect that only certain officers (say, the managing director) of the company can be authorized to sign for the purpose of attesting the company's seal. Such a special resolution would be required to be registered with the Company Registry under s.117 (4) of the Companies Ordinance, and insofar as it is inconsistent with the articles, the better view is that the special resolution would prevail as the articles could be altered or added to by special resolution (see, s. 13). In such a case, there is no reason why a purchaser, who has found out that there is such a special resolution registered in the Company Registry, should be prevented from raising queries on the authority of the signatory attesting the seal if the signatory was one who could not have been properly authorized to attest to the use of the seal under the special resolution.

40. At common law, a person cannot rely on the indoor management rule if he has actual notice of the irregularity or has been put on inquiry. One can see the merits of the proposed s.23A(2) insofar as it provides that mere lack of description in the conveyancing document of the fact that the person has indeed been authorized shall not by itself be treated as actual or constructive notice of irregularity. However, where the party to the transaction has notice of some irregularities from other sources or other circumstances (as in the case postulated in the preceding paragraph), there is really no reason why he should be prevented from going behind the indoor management rule to contend that there are in fact irregularities in the execution of the instrument in question.

41. Similarly, at common law the Turquand's rule would only operate

in favor of outsiders to the company. Where the party to the transaction is not an outsider, should he be allowed to rely on the indoor management rule? For example, if a fellow director is a party to the transaction, should he be afforded the same protection of s.23A(2) as if he were an outsider? The present draft of s.23A(2) does not distinguish between outsiders and insiders, and consideration should be given to that matter before the proposed legislation is enacted.

42. Subject to suitable amendments to remove these reservations, the Bar give its support of the proposed s.23A(2). Obviously the sub-section would need to be redrafted if subsection (1) is to be removed and if account is to be taken of the reservations referred to above.

43. We should add that we do not see why the proposed sub-section should not be made to apply to both past and future transactions. The sub-section is designed to facilitate conveyancing, and not only to remedy previous problems. We are of the view that such a statutory provision would generally be beneficial to the handling and structuring of conveyancing transactions involving corporate executions.

The Administration's suggested alternative provision

44. An alternative provision has been suggested by the Administration in paragraph 38 of the Consultation Paper. The alternative provision would give statutory blessing to the "risk approach" examined in paragraphs 17 to 22 above.

45. As pointed out in paragraph 18 above, there is a lot of common sense underlying the risk approach, although it is difficult to justify the same under the present law. Obviously the risk approach can be "legalized" by appropriate legislation. This can be done by:

(1) enacting a statutory presumption providing that if there is no real risk that the relevant conveyance would be set aside in

future proceedings, the execution is deemed to have been properly made despite the formal defects; or

(2) enacting a provision to the effect that notwithstanding the defective execution, legal title is deemed to have been passed under the relevant conveyance if there is no real risk that the same would be set aside in future proceedings.

46. The great advantage of the Administration's proposal is that it would address, in a more direct way, the grievance and/or injustice caused to an owner who is left with an unsaleable property by reason of a formal but unrectifiable defect in the execution of a corporate conveyance somewhere in the chain of title which is otherwise "inconsequential" in terms of risk.

47. On the other hand, the great disadvantage of the Administration's proposal is that the risk can only be assessed having regard to all the circumstances of the case, and except in the clearest cases, reasonable solicitors acting reasonably and responsibly may well differ in their assessment of the risk. We must say that we have found the Administration's conclusion that "it should not be difficult for the solicitors for the vendor and the purchaser respectively to agree that the proposed presumption of good title should be relied on, particularly in respect of older assignments which have never been contested by the companies concerned" to be overly optimistic. Experience shows that such agreement is often difficult to obtain. How old must be the assignment, in the absence of other special circumstances, before it can be assumed that the risk of it being set aside is minimal? A reasonable solicitor might say 10 years, but a more cautious but equally reasonable solicitor might well say 20 years. And if 10 years is old enough, what about 9 years, or 8 years? Of course one cannot just look at the age of the assignment but to all the circumstances (some of these circumstances have been set out in paragraph 41 of the Consultation Paper). As in all cases where everything is weighed in the balance, factors may cancel out each other and it would be rare to find an overwhelming case such as would produce

agreement between the solicitors acting for the parties. This is not helped by the fact that the solicitors for the respective parties represent conflicting interests. Solicitors acting for the vendor would want to see the transaction proceed to completion and would be more inclined to castigate any risk as minimal or fanciful. On the other hand, even if the solicitors acting for the purchaser also wish to proceed to completion, they would be likely to be more cautious to ensure that the risk can truly be discounted or ignored, or else their client would be burdened with a defective title. In the case of a falling market, where the purchaser would naturally have the incentive of getting out of the contract if possible, he and his solicitors would be even more "cautious" in discounting the risk arising from the defective execution.

48. The long and short of it is that in most cases there are likely to be room for disagreement in such a weighing exercise. Except in the clearest cases, equally competent and responsible solicitors acting for the different parties are likely to have different views because of the conflicting interests of their clients, as the very nature of the exercise is necessarily one of degree.

49. It is likely that if the Administration's proposal is enacted into law, it would be frequently resorted to by owners with a defective title as a means of last resort to save their title. It would be optimistic to assume that the respective solicitors handling the transaction would be able to come to an agreement on the assessment of risk, and thus many of these cases would ultimately have to be decided by the courts. The possibility of opening a floodgate of disputes must be guarded against. It is vital to the profession that the law should be as certain as possible. Any law which requires the profession to carry out a weighing exercise is not likely to be conducive to the certainty of the law. The admirable attempt by the Administration to address the grievance of owners of unsaleable properties may turn out to be a damaging blow to the certainty of the law in this respect.

50. While the spirit behind the Administration's proposal should be

supported, it is submitted that any legislation along the lines of this proposal must not be allowed to introduce unacceptable uncertainties into the law. Otherwise the legislation will itself provide a fertile ground for litigation, which will not be beneficial to the property market in Hong Kong. Accordingly, it is suggested that definite and certain statutory guidelines and/or criteria should be built into any legislation of this sort. The Administration should not take the easy way out by leaving it to the Court to pronounce on the risk based on all the circumstances of the case. To do that would be to drive most cases to the hot seat of litigation, and the Bar should not support such a course.

51. Accordingly the Bar would only support the Administration's proposal if clear and definite statutory criteria are provided for determining the risk which would in turn trigger the application of the proposed statutory presumption. This may be done by restricting the type of circumstances that may be taken into account in determining the risk. For example, the statute may provide that only an assignment more than 15 years old would qualify as a relevant circumstance. Or if the company has been wound up or has been defunct for more than 5 years, it may qualify as a relevant circumstance to be taken into account. Leaving everything at large would be a recipe for disputes, if not disaster.

52. The Administration has not produced a draft of the alternative provision for the Bar's consideration, and it is impossible at this stage to give any specific comments other than the general comments mentioned above. We would merely add that the Administration's proposal should not be seen as an alternative to the proposed s.23A(2) suggested by the Law Society. We see no reason why one should be exclusive of another. As said, we look at the proposed s.23A(2) as being beneficial in its own right. The Administration's proposal addresses the issue of risk and its effect on title, which is different from the Law Society's proposal which addresses the issue of corporate execution by means of a statutory clarification / codification of the Turquand's rule.

Conclusion

53. To conclude, the Bar would like to respond to the issues set out in paragraph 46 of the Consultation Paper as follows:

Q1. We agree that legislation is needed.

Q2. We do not support the proposed section 23A (1).

Q3. We support the proposed section 23A (2), subject to the matters referred to in paragraphs 40-43 above.

Q4. We would only support the Administration's proposal if clear and statutory guidelines and criteria are built into the proposed legislation to avoid introducing unnecessary uncertainties into this area of the law.

Dated this 19th day of March 2002
Hong Kong Bar Association

ANNEX

1. **Qualihold Investments Ltd. v. Bylax Investments Ltd.**
   [1991] 2 HKC 589

2. **Tread East Ltd. v. Hillier Development Ltd.**
   (HCA 907/1991, Hon. Godfrey J.)

3. **Hillier Development Ltd. v. Tread East Ltd.**
   [1993] 1 HKC285

4. **Whole Year Development Ltd. v. Lung Chiu Yee Julia** (HCMP 966/1993, 21/6/1993, Mayo J.)

5. **Peking Fur Store Ltd. v. Bank of Communications**
   [1993] 1 HKC 625

6. **Perfectime Ltd. v. Ko Ming Bor & Anor**
   [1994] 3 HKC 507

7. **Woo Turhan & Anor v. Taiwan Fuji Trading (HK) Ltd.** [1995] 2 HKC 481

8. **Li Ying Ching v. Air-Aprung (Hong Kong) Ltd.**
   [1996] 4 HKC 418

9. **Lee Chat & Anor v. China Roll Industries Ltd.**
   [1998] 1 HKC 269

10. **Hui Yuk Chun v. Tang Wai Hang Henry & Anor** (HCMP 1/1998, 3/4/1998, Hartmann J.)

11. **Ho So Yung v. Lei Chon Un** [1998] 2 HKC 697

12. **Wong Yuet Wah Mandy v. Lam Tsam Yee & Anor** [1999] 3 HKC 268

13. **On Hong Trading Co. Ltd. v. Bank of Communications** (HCMP No.3099/1999, 29/2/2000, Recorder Kotewall, SC)

14. **Lo Wing Wah & Anor v. Chung Kam Wah**
[2000] 1 HKLRD 227

15. **Lim Shui Chun v. Billion Light Investment Ltd.** [2000] 2 HKC 621

16. **Chan Sai Hung v. Well Development Ltd.** [2000] 4 HKC 50

17. **Grand Trade Development Ltd. v. Bonance International Ltd.** [2000] 4 HKC 547 (Chung J.)

18. **Hong Kong and Shanghai Banking Corp. Ltd. v. Ho Sin Yi** (HCMP 5420/2000, 1/2/2001, Deputy Judge Gill)

19. **Grand Trade Development Ltd. v. Bonance International Ltd.** [2001] 3 HKC 137