

## **BEST PRACTICE STATEMENT:**

### **RE: EVIDENCE OF CORPORATE AUTHORISATIONS FOR FINANCIAL MARKETS AGREEMENTS (THE “AUTHORISATIONS”)**

#### **1. Purpose of this Best Practice Statement**

The purpose of this Best Practice Statement is to highlight the essential elements to be included in authorisations (hereafter, ‘Authorisations’) provided by financial institutions, and to propose a preferred format for such Authorisations.

#### **2. Purpose of Authorisations**

Authorisations ought to provide clear evidence of a financial institution’s corporate authority for:-

- the range of financial markets agreements that may be executed in its name, including for example master agreements for derivatives, foreign exchange, repo, securities lending and other financial transactions; and
- the person or persons who will execute them on its behalf, together with specimen signatures which can be checked against executed agreements.

Authorisations should not be subject to conditions or limitations that cannot be verified by a counterparty without further enquiry. They should be certified, if necessary, by a person other than a designated signatory, as being a true and correct copy and in effect at the date of execution of the relevant financial markets agreement. A counterparty is then able to satisfy itself, without further time consuming enquiries, that the proposed financial markets agreement has been duly authorised and executed and constitutes a legally

binding contract with the financial institution. While this is fundamentally a long-standing tenet of good banking practice, it has received a new urgency as a result of the operational risk elements of Basel II.

### 3. **Current State of Authorisations**

Many Authorisations currently provided in the financial markets, including those by some major financial institutions, leave residual doubts as to the scope of the authority for the relevant financial markets agreements and the signatories executing them.

#### 3.1 ***Identification of Transactions rather than Agreements***

In many cases, Authorisations define the financial markets transactions in which a financial institution proposes to participate rather than the type of financial markets agreement that will govern them. Examples of the purported definitions of such financial markets transactions include:

- General terms used to identify certain product types –
  - “fixed income transactions/business”.
  
- The use of catch-all provisions –
  - “to enter into Derivatives or similar contracts”.
  
- The enumeration of certain transactions followed by the phrase –
  - “any other similar transactions”.
  
- Transactions described by reference to purpose-
  - “Transactions for the purpose of hedging”; or
  - “In connection with the business” of the particular institution.

all of which leave a counterparty in an uncertain position given their ambiguity.

#### 3.2 ***Format of the Authorisation***

The format of Authorisations varies: for example, Powers of Attorney, Directors’ Resolutions, Statements issued by a Chief Executive and Secretarial Certificates.

These formats may be generally acceptable per se, but uncertainties may still arise as to the source of the document in which the authority is embodied and whether or not the Authorisation itself continues in force in all respects.

### 3.3 *Signatories nominated by the Authorisation*

The manner in which signatories are nominated for the purpose of executing financial markets agreements are also often diverse and unsatisfactory. Signatories may be nominated by submission of:-

- signatory books, which do not themselves refer to the relevant financial markets agreements specifically;
  - an informal compliment slip with specimen signatures attached thereto and no further evidence of authority;
  - signatories whose authority depends on unverified conditions, e.g.
    - “The Treasurer and in the absence or disability of the Treasurer by the Assistant Treasurer”,
      - A, B, C who are for the time being employed by the Institution.
  - signatories by reference to their title or function without certification as to the signatories title or function, e.g.
    - “a Financial Markets Lawyer”,
    - “a Divisional Secretary”,
    - “a Chief Operating Officer”.
  - Limitations on the duration of authority that cannot be verified, e.g.,
    - The powers granted hereby to \_\_\_\_\_ shall be deemed automatically revoked upon that person or persons ceasing to be employed.
4. The general inadequacy of current Authorisations may increase legal risk, cause uncertainty and consequent delays, and give rise to operational inefficiency and backlogs in processing financial markets agreements and ancillary documentation. This view is shared by many practitioners in the area and is echoed in a letter of February 2004 issued by the Chairman of the Foreign Exchange Committee of the Federal Reserve Bank of New York to market participants<sup>1</sup>.

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<sup>1</sup> <http://www.newyorkfed.org/fxc/2004/fxc040223.pdf>

The European Financial Market Lawyers Group (EFMLG) shares these concerns, particularly in relation to ISDA Master Agreements, TBMA/ISMA Global Master Repurchase Agreements and ancillary agreements, including Guarantees and other credit support documentation. In consequence, a sub-group of the EFMLG (the “Sub-Group”) was formed with a view to proposing coherent Authorisation procedures which would enable financial institutions to approve financial markets agreements in an expeditious manner mutually protective of both parties to an agreement.

- 5.** The Sub-Group reviewed a sample of Authorisations and in order to promote the development of a more consistent approach to formulating Authorisations, issued a questionnaire to the members of the EFMLG, whose responses have been duly considered by the Sub-Group.
- 5.1** Whilst participants operating in the financial markets will not be obliged to adopt these guidelines, the EFMLG would encourage participants to follow this Best Practice Statement in order to create, as far as practicable, a standardisation of the Authorisations procedure.
- 5.2** The precise format of the Authorisation, the description of the agreements to be entered into, the manner in which the signatories are defined and the certification that the Authorisation is in effect, remain the responsibility of the parties concerned. The EFMLG assumes no responsibility for any use to which this Best Practice Statement may be utilised in any particular jurisdiction or with respect to any particular counterparty. Each participant following the recommendations contained in this Best Practice Statement should, with its own legal advisers, satisfy itself that these recommendations are appropriate to reflect the intention of the parties and are in compliance with such laws and regulations as may apply.

## COMMENTARY

6. The key authorisation issues identified by the EFMLG as causing uncertainties and delays in completion of financial markets agreements are:-

- the choice of format
- the core authority, i.e., the description of financial markets transactions or the description of financial markets agreements
- the nomination of signatories.

### 6.1 *Format of Authorisation*

Responses to the questionnaire highlighted a number of formats that were considered appropriate in relevant jurisdictions. Despite a diversity in formats, a clear preference for the Power of Attorney emerged as the most common in the majority of jurisdictions. This was followed, in descending order, by Directors' Resolutions and excerpts from the commercial register.

Accordingly, for the purposes of this commentary, the EFMLG has chosen the Power of Attorney format which, even if not necessarily appropriate and/or in compliance with all legal systems, will at least focus members' attention on those elements essential to an appropriate Authorisation. Where an alternative format is chosen, it should contain, as far as practicable, the elements of the attached sample Power of Attorney. Briefly, the sample Power of Attorney provides for:-

- the range of financial markets agreements to be entered into and the proposed signatories thereto; and
- the protection of bona fide counterparties acting in good faith without notice of its termination.

In addition to the essential elements of an Authorisation there are two further issues which require careful attention.

#### (a) *Evidence of the continued existence of the Authorisation*

This is particularly important where the Authorisation is dated considerably prior to the date of its submission. Whatever the format adopted, a provision may be included dealing with this issue, such as:

- an irrevocability clause or, in its absence, a certification that it has not been revoked
- inclusion of an expiry date, or
- a separate certificate of an appropriate corporate officer issued contemporaneously with the executed financial markets agreement.

(b) ***Source of the authority vested in the person giving the Authorisation***

A recipient will require evidence that the person providing the Authorisation is duly authorised. An original Power of Attorney, given under the common seal of a financial institution in a common law jurisdiction, may require further review of relevant board resolutions. A photocopy of such a Power of Attorney or a Statement of a Corporate Officer, a Secretarial Certificate or a Power of Attorney given by an Officer(s) of the Institution will also often require further verification.

In the case of both (a) and (b) above, the required level of certification will vary according to the actual format of the Authorisation and such other circumstances as may be deemed relevant by the recipient and its legal adviser. Any request by the recipient in this regard should be treated with respect by the provider and dealt with expeditiously.

## **6.2 *The core of the Authorisation i.e. Financial Markets Agreement***

Consideration was given to the distinction between individual transactions and the master agreement to which they are subject. The EFMLG concluded, for a number of reasons, that it is the type of financial markets agreements which should be authorised rather than a shopping list of financial transactions/products. First, it is generally the financial markets agreement that is enforced, if enforcement is required, rather than a single transaction. Secondly, most financial markets agreements, once duly executed, can be viewed as providing authority for transactions customarily entered into under them. This is particularly true with respect to a financial institution that is functionally organised and generally engages in the business of entering into financial transactions of the relevant type. Thirdly, and following on from this, the EFMLG believes that authority for the many varied transactions which a financial institution proposes to enter is a matter for its internal controls. To require a party to satisfy itself as to its counterparty's compliance with internal controls is not an appropriate conundrum to be visited upon lawyers seeking to formalise the party's financial markets agreements in a manner that is mutually protective of the interests of both parties.

The Schedule to the sample Power of Attorney specifies the various types of financial markets agreements as the subject of the Authorisation.

### 6.3 ***Nomination of the Signatories pursuant to the Authorisation***

The EFMLG recommends that the provision regarding signatories should seek to avoid conditions and limitations that cannot be verified without further inquiry. The signatory or signatories should be identified by name rather than by reference to the position he/she holds unless, perhaps, such a position is a statutory position recognised by law such as that of a Corporate Secretary in common law jurisdictions. A signatory's authority should not be made conditional upon his/her continued employment.

In some countries, commercial registers containing the names of persons authorised to sign on behalf of an institution may be relied upon without further investigation. It might be useful if such person or persons were nominated as signatories or at least one of the alternative signatories. In that case, a certified translation of the relevant extract should be made available in English to the requesting counterparty.

Reference to signature books per se is not satisfactory. They frequently are out of date and often provide for limited or ambiguous authorities: for instance, they may refer to types of transactions rather than specific financial markets agreements.

If a counterparty insists upon a 'protective provision' that an authority may be revoked if the nominated signatory is no longer employed by the institution, the EFMLG suggests that the Authorisation should be accompanied by a further certificate that the authority has not been revoked, perhaps by the legal adviser dealing with the transaction.