

Electronic signatures on guarantees = High Risk for Fraud and Dishonesty

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As electronic communications and electronic signatures become more prevalent in modern electronic commerce, there is an increased risk of fraud and dishonesty.

Trade credit businesses place considerable reliance upon signatures which appear on terms and conditions of trade and, perhaps more importantly, personal guarantees.

This is risky because the signature may have been forged and/or placed on the document by an unauthorised person. Conversely, it is open for an unscrupulous person to later claim that the signature was not applied by them or by someone else without their authority.

If it cannot be established that the signature was applied by the intended guarantor, or with their authority, the guarantee is likely to be unenforceable.

We are noticing a recent spate of personal guarantors who have claimed that their signature which appears on a personal guarantee was not placed upon the document by them or with their knowledge.

In a number of instances, directors of failed companies have denied liability under personal guarantees and have claimed that their signatures were scanned and saved on company servers, and that an employee applied their signature to the personal guarantee without their knowledge.

When this occurs, the trade creditor is unlikely to succeed unless it can establish that it was more likely than not that either:

5 TIPS

to avoid forged guarantees

- 1 Obtain the original documents.
- 2 Verify the identity of the guarantor.
- 3 Send a letter to guarantors confirming that a credit application has been approved based upon their guarantee.
- 4 Ensure that each guarantee is witnessed, that you have the witnesses' contact details, and confirm that the witness saw the guarantor sign.
- 5 Document dealings with guarantors and witnesses.

1. the guarantor applied the electronic signature;
2. the electronic signature was applied with the guarantor's authority; or
3. the guarantor became aware that the signature had been applied and continued to trade upon the account and receive a benefit under the credit agreement after this time.

The above presents considerable difficulties for creditors seeking to rely on personal guarantees.

In most cases, the creditor does not physically witness the guarantor sign the document. This means that the creditor is reliant upon witnesses from the customer's business to establish that the guarantor in fact signed the document. To do this, the creditor needs sufficient information to locate the witness. Even if the witness can be found, the witness may not be willing to assist, may not recall the signing of the document, or may assert that the guarantor did not sign the document.

If the guarantor did not sign the document, then the creditor may still be able to enforce the guarantee if they can establish that the person who signed the guarantee did so with the authority of the guarantor. This requires the creditor to establish the identity of the person who applied the signature to the document, and the scope of that person's authorisation.

We have recently provided advice in respect of a situation similar to the following.

1. The alleged guarantor was one of three directors of the customer, and claimed to have limited involvement in the day to day affairs of the company.
2. The supplier received a credit application and guarantee which:
 - a. appeared to have been signed by the three directors of the company, each offering a personal guarantee;
 - b. contained drivers' licence numbers and contact details of each director; and
 - c. appeared to have been witnessed by an employee of the company.
3. The supplier received the trade credit application, opened an account, and extended credit to the company successfully for many months.
4. The company subsequently failed to pay its debt to the supplier on time of at least \$500,000.
5. The supplier issued a letter of demand upon the guarantor which was not answered.
6. In response, the guarantor denied liability under the guarantee and supplied material (including computer records) to the effect that:
 - a. he was aware of a credit account between the company and the supplier;
 - b. he had an account with an online signature website which stored an image of his signature and could apply that image to documents using his username and password;
 - c. he did not sign, nor authorise his signature being applied to, the guarantee;
 - d. he did not know that the guarantee had been forwarded to the supplier; and
 - e. his fellow director (another guarantor) had applied his signature to the guarantee.

To be able to successfully rely on the guarantee, it will be necessary for the trade creditor to establish that:

1. the fellow director was armed by the alleged guarantor with a means to apply his signature to the guarantee without sufficient safeguards against improper use; or
2. the alleged guarantor nonetheless adopted the guarantee because he became aware of the forgery and continued to trade on the the account after becoming aware of the document.

There are a number of practical steps which can be incorporated into the credit management process to limit the risks associated with applying electronic signatures.

These include the following:

1. Obtain original documents

Given that the risks associated with electronic signatures can be higher than traditional signatures, it is important to know what kind of signature was applied to the guarantee. The best way to do this is often to obtain an original copy of the guarantee.

2. Verify the guarantor's identity

The more action that can be undertaken to verify the identity of the guarantors (and that the signature has, in fact, been applied by the guarantor), the better. In an ideal situation, the creditor should be conscious to verify the information contained in an application for credit and personal guarantee. Depending upon the amount of credit to be advanced, the creditor may wish to insist upon meeting the guarantor, requiring copies of the guarantor's identification, and/or calling the witness and guarantor to confirm the existence of the guarantee.

3. Sent letter to verify guarantee

It is also recommended that, when an application for credit approved, the creditor sends a letter to each of the guarantors which confirms that a credit account is being opened in reliance upon their personal guarantee and to immediately contact the supplier if they did not intend to give a guarantee. If the guarantor later denies applying his or her signature to the guarantee, a letter of this nature can be relied upon to establish that the guarantor knew of the guarantee and has ratified the guarantee by the guarantor's conduct. Ratification has the effect of holding a guarantor liable under a personal guarantee, even if it cannot be proved that the signature was applied by the guarantor or with their authority.

4. Obtain witness details

The purpose of having a guarantee witnessed is to later be able to establish that the signature was applied by the intended person. The witness must be able to be located to be of assistance. Trade creditors should require, as part of their credit application, contact details of the person witnessing personal guarantees.

5. Document dealings with guarantors

In seeking to enforce a disputed guarantee, the court can have regard to conduct after the alleged signing of the guarantee in construing whether the parties considered there to be a guarantee. For this reason, a supplier should retain documents which confirm that the guarantor was aware of the guarantee.

Enforcement of written documents can also be impacted by verbal representations made at the time the guarantee was signed. For example, if an employee of the supplier stated to the creditor at the time the guarantee was signed to the effect that the personal guarantee was only for the credit limit appearing on the account application form, and the credit limit was subsequently increased, then the amount of the guarantee may be limited, despite what the guarantee states.

There is significant risk of fraud and dishonesty in accepting written trade credit applications and personal guarantees without further enquiry. Trade creditors should be forever conscious of fraud and dishonesty, otherwise they bear significant risk of being unable to pursue personal guarantees. These risks can be overcome with carefully considered practices and procedures.



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