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Introduction

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I The subject matter of this book: unauthorised agency

This book explores the legal problems caused by agents who act in an unauthorised manner. This general idea is broken down into three central issues in the analysis which follows: apparent authority, ratification and the liability of the *falsus procurator*. Each of these individual ideas will be expanded upon below. For the moment, the question which may arise is why this particular area has been selected as worthy of analysis. Agency law is a much under-researched area, and there are undoubtedly many other aspects equally deserving of attention. We would argue that the problems caused by unauthorised agents illustrate a central tension in agency law: the tension between the use of the concept of contract as the primary tool for the analysis of the legal relationships involved and the tri-partite nature of those relationships (involving principal, agent and the principal’s contracting party known as the ‘third party’). In other words, a legal concept formed with

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bi-partite relationships in mind is applied to more complex tri-partite legal relationships.

The major problem inherent in the use of a contractual analysis is that it brings with it a significant role for the concept of consent. Where two parties are involved in a contractual relationship, they will normally reach *consensus in idem* in a direct manner. Where three parties are involved, consent is achieved in a more indirect way. The situation has been rationalised by explaining that the principal consents in advance to all the agent's acts carried out on his behalf.¹ The principal's consent exists in the 'background' during the agent's negotiations, and can be referred to later in order to create the *consensus in idem* required for the formation of a contract between principal and third party.

It is perhaps helpful to consider the practical implications of the role of consent in agency. Consent is provided when the principal gives to the agent authority to act on his behalf. That authority is, of course, not unlimited. By granting authority to the agent, the principal identifies the specific activities which the agent is able to carry out on his behalf, and, by implication, those which lie beyond the scope of the agent's power. It seems, however, to be an unavoidable fact of commercial life that agents regularly act beyond the confines of their authority. Often, this is due to fraudulent intentions on the part of the agent, but this may not be the case. The agent may take a 'calculated risk' that the principal will view the prospective contract favourably. His prediction may not, however, turn out to be accurate. Fluctuations in market prices occurring since the date on which the agent purported to conclude a contract on his principal's behalf may have rendered the contract unattractive to the principal. Because the agent has stepped beyond the boundaries of his authority, one can no longer utilise the principal's 'lurking' consent. *Consensus in idem* is not present, and, as a general rule, no contract is formed. The third party who is unaware of the agent's lack of authority is disappointed. The anticipated contract does not exist.

It seems clear that to adhere too rigidly to this general rule would be unacceptable in principle. It seems almost unarguable that, of the three actors involved in agency situations, third parties are the most deserving of the law's protection. They may have little choice but to transact using an agent: the issue may not be one which is open for

¹ See the useful discussion of the role of consent in the context of agency relationships in G. McMeel, 'The Philosophical Foundations of the Law of Agency' (2000) 116 *LQR* 387.

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negotiation. But the major factor pointing in favour of third party protection is the 'information asymmetry' which exists: the third party is unable to access the information necessary in order for him to determine whether the agent is indeed properly authorised. That information is available only to the principal and the agent. The third party may struggle to understand the opaque hierarchy of the principal's business, and the powers of those working therein. Enquiries from the third party may go unanswered, or be answered incorrectly.² Even if it is possible for the third party to access this information, one could question whether it is efficient for him to do so. Each transaction will involve a different third party, and each of those third parties would have to carry out similar time-consuming checks on the agent's authority. It would be cheaper and simpler to require the principal to increase supervision of the agent to minimise the risk of agents acting in an unauthorised manner.

Whilst there is an undoubted need for third party protection, strict liability is not the answer. It could lead to an unmanageable amount of liability on the part of the principal, and eventually to a downturn in the use of agents generally. It might also fail to deal adequately with situations where the third party acts in bad faith. Judging from case-law, this is a common problem, particularly where third parties collude with fraudulent agents.³ The third party's conduct and knowledge are clearly significant factors which may rule out liability on the part of the principal.

The solution to this problem lies, we would suggest, in the application of a judicial discretion. It could be tailored to the circumstances of the case, and be applied bearing in mind the policy factors discussed above. The central issue in this project has been the analysis of the extent of third party protection existing in the legal systems studied. Those protections have been compared in order to ascertain whether a common approach exists. That common approach has then been assessed, and suggestions have been made as to what, in our view, would constitute an 'ideal' approach.

² For a good illustration of this point, see *British Bank of the Middle East v. Sun Life Assurance Company of Canada (UK) Ltd* [1983] 2 Lloyd's Rep 9, discussed by J. Collier in his article, 'Actual and Ostensible Authority of an Agent: A Straightforward Question and Answer' (1984) 43 *CLJ* 26.

³ See, e.g., the conduct taking place in the leading English case of *Armagas Ltd v. Mundogas SA, The Ocean Frost* [1986] AC 717 or the Scottish case of *International Sponge Importers v. Watt and Sons* 1911 SC (HL) 57.

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II The three aspects of unauthorised agency: apparent authority, ratification and the liability of the *falsus procurator*

Having set out our general aim, we can now descend to a more particular level. As stated at the beginning of this Introduction, the general topic has been split into three particular concepts: apparent authority, ratification and the liability of the *falsus procurator*. The first of these, apparent authority (adopting, for the moment the common law term), becomes relevant where a principal, whether actively or passively, leads a third party to believe that his agent is authorised when this is not, in fact, the case. At a later stage, the principal seeks to deny the appearance of authority, and therefore the existence of any contractual tie with the third party. Although the national forms of apparent authority differ, they all share the same general effect: the principal is prevented from relying on the agent's lack of authority. The third party therefore has a claim against the principal for protection of his expectation interest. This constitutes, however, only a limited degree of protection. It exists only where it can be proved that the principal is 'at fault' in the creation of the erroneous impression. Where fault cannot be proved, for example, because the third party relied on the agent's representations of authority, the third party has no claim against the principal. The results of this rather limited approach appear to have been unsatisfactory. In many of the legal systems analysed here, one can find attempts to extend the principal's liability. One of the most interesting issues arising from this comparison is the identification of different methods used by each legal system in order to extend liability on the part of the principal.

The second of the three central concepts, ratification, poses similar, if perhaps less serious, concerns. Again, the agent purports to enter into a contract on behalf of his principal whilst possessing insufficient authority. In contrast to apparent authority cases where the principal rejects the contractual tie, ratification enables him to validate an otherwise non-binding contract. The consent of the principal is present, albeit that it is provided at a late stage. Ratification poses fewer problems also because it tends to operate in the third party's favour: it validates a contract which the third party, all along, has considered to be binding. Importantly, however, the principal cannot be forced into ratifying. This statement must be qualified given that, in some of the systems analysed, the third party has important powers which can be used to force the

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principal to confirm whether or not he intends to ratify within a reasonable time.⁴

A particularly difficult issue in this context is the case of the third party who intends to be bound, but, having discovered the agent's original lack of authority, seeks to withdraw unilaterally from the 'contract'. The problem arises in part due to the retrospective effect of ratification, an idea shared by all the legal systems studied. Effective ratification creates a valid contractual nexus between principal and third party backdated to the moment when the agent purported to act on the principal's behalf. To give to ratification its full retrospective effect is to deny the third party the right to withdraw, even if he purports to do so prior to the principal's act of ratification.

The clash of interests between the principal and third party in this situation is a difficult one to resolve. The starting position is, we would suggest, the backdrop of the third party's information asymmetry. Because the third party is initially disadvantaged, cogent arguments are required in order to prevent him withdrawing from what is not a valid contract at the time of withdrawal. Nevertheless, there are arguments against a right to withdraw. The third party could be accused of 'playing the market': rejecting a contractual relationship which has, with the passage of time, become unattractive. There is no extra factor such as undue influence which would justify his withdrawal. The right to withdraw, in general, threatens one of the major functions of contract law. Contracts allow parties to assess future risks at the moment of formation and thus to achieve certainty through their agreement. It is also necessary to consider parties situated outside the immediate tri-partite situation. Others, so-called 'fourth parties', may be equally unaware of the agent's lack of authority, yet equally reliant on the validity of the principal/third party contract. To 'unravel' that contract could send ripples out into the commercial world, upsetting contractual relationships and, potentially, transfers of ownership of property. Such consequences clearly ought to be avoided. The attitude of a particular legal system to the third party's right to withdraw is a particularly significant issue. It acts as a 'barometer,' measuring the extent of third party protection within that particular legal system.

Thus far, the discussion has been limited to the choice of principal or third party as the most appropriate bearer of losses. It may seem unusual to omit the agent, usually the most blameworthy party, from this

⁴ See Chapter 4 (Germany), V 3 (§ 177(2) BGB); Chapter 5 (The Netherlands), V 4 (b) (Art. 3:69(4) DCC); Chapter 12 (UP), VI 4 (b) (Art. 2.2.9(2) UP).

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discussion. With the third of the three central concepts we can turn our attention to the agent. All of the systems studied recognise an action which can be raised by the disappointed third party against the agent. It is curious, however, to note its lack of importance, particularly in English and Scots law. It seems to be seldom used, and, as a result, its rationale has not been clearly worked out. It is not clear why this action should have such a low profile. It may simply be a reflection of the fact that the principal tends to be in a stronger position financially, and is therefore, in the third party's eyes, a more attractive target than the agent. Alternatively, the agent may simply have disappeared.

This action is generally discussed under the heading of 'the liability of the *falsus procurator*' in continental Europe and 'breach of warranty of authority' in the common law and mixed legal systems. With this concept we move into new territory. No actual contract exists between third party and agent. A legal system must therefore 'construct' a legal basis for the action. The legal systems studied here have tended to favour the use of either an implied unilateral undertaking or an implied contract. Both of these solutions are, in effect, legal fictions and therefore relatively unsatisfactory. As is illustrated below, some legal systems have explored the possibility of a legal basis within tort law. This third concept is the final, and perhaps the most unusual, of the three central concepts studied in this book.

Although we have now set out the ambit of our enquiry, it will be clear that it is not entirely comprehensive. We have not considered the implications of unauthorised agency for the principal/agent relationship. This omission can now be explained. Our central aim was to assess the extent of third party protection in each of the legal systems studied. This being the case, the external, and not the internal, aspect of agency forms the major focus of the book. As a result, the remedies open to the principal against the misbehaving agent are generally not analysed in the chapters that follow, although they may be touched upon in passing. To include this aspect within our enquiry would undoubtedly have proved interesting, providing a more comprehensive picture of the law in this area. We decided to exclude this angle entirely in order to constrain an already extensive subject matter within manageable bounds.

III Direct, not indirect, agency

For common law lawyers and those from mixed legal systems, the distinction between direct and indirect agency is not a familiar one. In

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continental Europe, whether an agency situation is classed as direct or indirect depends upon whether or not the agent discloses when he concludes the contract on the principal's behalf that he is acting in the name of the principal. If he does so, this is direct representation, the effect of which is the formation of a contract between principal and third party. Where the agent acts in his own name, but still on behalf of the principal in the sense that the transaction is ultimately at the risk, and for the benefit, of the principal, this is indirect representation. The effect in this latter case is the formation of a contract between agent and third party. This outcome applies in indirect representation even where the third party is aware that the agent is acting on behalf of (though not in the name of) a principal. While indirect agency is in widespread usage in continental Europe, it is virtually unknown in the UK.⁵

The concept of unauthorised agency is usually only associated with unauthorised direct agency. The same is true for apparent authority and ratification. Although it is possible to apply these concepts to (certain cases of) indirect agency,⁶ the focus of this book is direct rather than indirect agency. This decision was motivated by two main factors. Importantly, again we did not want the project to extend beyond manageable boundaries. Additionally, direct agency, as the method of dealing present in the common law, the civil law and the mixed legal systems, constitutes the obvious area for comparison.

IV The aim of this book: the search for common European rules

Our principal aim in producing this book is to identify common approaches, or the 'common core' of the rules with respect to unauthorised agency.⁷ In addition, we highlight the areas where, in our view, the solution adopted by the common core is unsatisfactory, bearing in mind our principal concern, already expressed, of third party protection. To the extent that the common core is lacking, we suggest what would be a

⁵ See H. L. E. Verhagen, 'Agency and representation', in J. M. Smits, *Elgar Encyclopaedia of Comparative Law* (Cheltenham/Northampton: Edward Elgar, 2006), pp. 47–48; D. Busch, 'Indirect Representation and the Lando Principles: An Analysis of Some Problem Areas from the Perspective of English Law' (1999) 7 *ERPL* 319.

⁶ See, on 'unauthorised indirect representation', 'apparent authority for indirect representation' and 'ratification of unauthorised indirect representation', D. Busch, *Indirect Representation in European Contract Law* (The Hague: Kluwer Law International, 2005), pp. 232–7.

⁷ To borrow the terminology from the Trento Common Core of European Private Law Project referred to in our Preface.

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welcome approach. In setting out this ‘common core’ we are pursuing different aims. The first relates to the development of a common contract law for Europe. With the much-awaited publication of a Common Frame of Reference, Europe stands at a pivotal point in the harmonisation process.⁸ It is thus timely that this book is available as a resource to those involved in the development of agency rules at European level.

Furthermore, we would certainly hope that, by studying the approach of another legal system, readers will be encouraged to develop their own legal systems in new ways, be it in their capacity as legislators, judges or legal practitioners or as academics. In making this point we recognise that those seeking to reform the law should not lose sight of the doctrinal foundations of their own systems, remembering the words of the late Professor Bill Wilson that ‘a legal system which has no doctrinal foundation must drift’.⁹ As a result, we imagine that civil lawyers will be most interested in the chapters describing other civilian systems, and *mutatis mutandis* the chapters on the common law and mixed legal systems. Nevertheless, it would not be surprising, as we emerge into a new phase of harmonisation of European contract law, to see examples of borrowing from beyond the same legal family.¹⁰

Thus we aim to identify common European rules, and create a body of work which will enable different legal systems to learn from one another. A further aim is that which relates to the inclusion of mixed legal systems within our project. This aim is best explored in the discussion below where we set out the reasons which motivated our choice of the legal systems taking part in this project.

V The legal systems studied

Within this book the reader will find chapters on unauthorised agency in France, Belgium, Germany, the Netherlands, England, the United States,

⁸ The Draft Common Frame of Reference (‘DCFR’) is intended to act as a “‘toolbox” or handbook for the EU legislator, to be used when revising existing and preparing new legislation in the area of contract law’: see European Parliament resolution of 12 December 2007 on European Contract Law, B6-0513/2007. It is not intended to be binding in nature. The DCFR was delivered to the Commission on 28 December 2007.

⁹ W. A. Wilson, ‘The Importance of Analysis’, in D. Carey Miller and D. W. Meyers, *Comparative and Historical Essays in Scots Law: A Tribute to Professor Sir Thomas Smith* (Edinburgh: Butterworths and Law Society of Scotland, 1992), p. 162 at 171.

¹⁰ See generally on the aims and functions of comparative law: K. Zweigert and H. Kötz, *Introduction to Comparative Law* (trans. T. Weir), 3rd edn (Oxford: Oxford University Press, 1998), pp. 13–31.

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Scotland, South Africa, the Principles of European Contract Law¹¹ and the UNIDROIT Principles of International Commercial Contracts 2004.¹² At first sight this may seem to be a strange and random grouping. Our principal aim was, as stated above, the search for common European rules. It was therefore important to include major European systems such as France and Germany. The Netherlands provided the opportunity to analyse a relatively modern, sometimes innovative, civil code. Belgian law often, but not always, followed the lead provided by French law. The PECL, as a highly influential contract 'code', undoubtedly merited a place in our project, given that they form the basis of development of a Common Frame of Reference for Europe. The inclusion of the major common law system within Europe, England, completed our European picture.

We have included two legal systems which are 'mixed' in the sense that, in those systems, an initial and strong civil law base has been overlaid with English influence.¹³ They are Scotland and South Africa. Their inclusion allows us to enquire whether systems which stand between Europe's two great legal traditions might have some distinctive contribution to make to the problems of unauthorised agency.

A body of literature exists in which the usefulness to comparative law of mixed legal systems is discussed. At times, expansive and possibly exaggerated claims have been made on this point. For example, in 1924 Henri Lévy-Ullman stated:

Scots law as it stands gives us a picture of what will be, some day ... the law of the civilised nations, namely, a combination between the Anglo-Saxon system and the continental system.¹⁴

A similar view is expressed by Zweigert and Kötz in their leading text on comparative law.¹⁵ MacQueen too, for similar reasons, has suggested that Scots law could help inform the development of the PECL.¹⁶ Whilst some continue to emphasise the contribution to comparative law made

¹¹ Referred to below as 'PECL'. ¹² Referred to below as 'UNIDROIT Principles'.

¹³ See on mixed legal systems, *inter alia*, J. du Plessis 'Comparative Law and the Study of Mixed Legal Systems', in M. Reimann and R. Zimmermann (eds.), *The Oxford Handbook of Comparative Law* (Oxford: Oxford University Press, 2006), pp. 477–512; J. du Plessis, 'The Promises and Pitfalls of Mixed Legal Systems: The South African and Scottish Experiences' (1998) *Stell LR* 338 at 339; and N. R. Whitty, 'The Civilian Tradition and Debates on Scots Law' (1996) *TSAR* 227 and 442 at 457.

¹⁴ Henri Lévy-Ullman (trans. F. P. Walton), 'The Law of Scotland' (1925) *JR* 370 at 390.

¹⁵ Zweigert and Kötz, *Introduction to Comparative Law*, p. 204.

¹⁶ H. MacQueen, 'Scots and English Law: The Case of Contract' (1998) *CLP* 204.

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by mixed legal systems such as Scotland,¹⁷ others doubt that mixed legal systems can indeed select the best from the competing solutions offered by the civil law and the common law.¹⁸ Whilst we would not seek to argue that Scots law offers ‘the best’ solution, we would indeed suggest that the experience of Scots law proves that the enterprise of mixing of this type is at least possible.

Some might challenge our inclusion of these mixed legal systems in the project on different grounds. Agency is sometimes classed as part of commercial law and sometimes part of contract law. Only contract law, and not commercial law, is truly ‘mixed’ in Scots and South African law.¹⁹ Those who classify agency law as part of commercial law would argue that there is nothing to be gained from its analysis here. The point of reference ought to be the dominant influence, English law. We do not agree. In our view such rigid distinctions cannot be made. As Niall Whitty has pointed out, ‘... no clear division exists between commercial law and large swathes of property and obligations’.²⁰ Agency law is a concept which crosses the boundaries between contract and commercial law. It is also relevant to note that solutions used in agency law problems often depend upon more general private law concepts, for example, ratification or personal bar. Those concepts have a wide ambit, much wider than the law of agency alone. They may have a civilian rather than a common law flavour. When applied in an agency context, the influence of the civil law arrives ‘through the back door’. For all these reasons, we would argue that one cannot categorise agency law as part of commercial law and thus the product of common law influences alone.

Whilst not wishing to anticipate the conclusions on mixed legal systems made in our final chapter, what we can say is that the analysis of the mixed legal systems in this project has been useful. South African law in particular has developed solutions, some of which stem from the civil law and some from the common law. Scots law, based in a small country with a limited case-law, has not progressed as far as South

¹⁷ See the work of J. M. Smits, particularly in *The Contribution of Mixed Legal Systems to European Private Law* (Antwerp: Intersentia, 2001); and *The Making of European Private Law: Towards a *Ius Commune Europaeum* as a Mixed Legal System* (trans. N Kornet) (Antwerp: Intersentia, 2002).

¹⁸ See the discussion of the competing arguments in du Plessis, ‘The Promises and Pitfalls’, p. 338.

¹⁹ K. G. C. Reid, ‘The Idea of Mixed Legal Systems’ (2003) 78 *Tul LR* 5 at 25; see also Whitty, ‘The Civilian tradition’, pp. 444 and 448–52.

²⁰ Whitty, ‘The Civilian Tradition’, p. 449.