

Chapter 20 – Agency and Other Methods for Carrying on Business

Introduction

- *Agent* – a person who acts on behalf of someone else for some specific purpose
 - Agents must not be negligent in carrying out their responsibilities
 - Ex: your real estate agent will not have the authority to commit you for selling at a certain price
- *Principal* – a person whom an agent represents for some specific purpose
- *Agency* – the legal relationship between a principal and an agent
 - Some agency relationships are governed by special statutes
 - Legislation addresses the risk that stock brokers may not have sufficient assets to pay claims against them by their clients

Basic Rules of Agency

Creation of an Agency Relationship

- Express agreement is a common way to create an agency relationship
 - Principal and agent enter into a contract that sets out the terms on which the agent is appointed (including scope of agent's authority and remuneration)
 - In provinces where the *Statute of Frauds* is still in force, the contract must be in writing if the relationship lasts longer than a year
 - Must also be in writing if agent signs cheques on principal's behalf
 - Ex: Listing agreement signed with real estate agent
 - Ex: *Commercial Representation Agreement* – when a manufacturer of goods agrees to allow someone to enter into contract with customers on its behalf to sell its goods
 - Relationships created by express agreement have the effect of making someone your agent, even if they are not called by that name. Ex: lawyer closing a real estate deal
- Individuals acting on behalf of a corporation are agents
 - Ex: directors, officers, other employees
- *Actual Authority* – when the principal actually authorizes the agent to act on its behalf
 - Sometimes stated in an employment contract, agency agreement or through a resolution from the corporation's board of directors
 - Can also be granted through an oral delegation of authority by a principal
- An agency relationship exists when a principal represents, or holds out, someone as its agent in discussions with a third party
 - That person will be able to deal with the third party by the authority suggested by the principal, even if that person was never properly appointed
 - *Apparent Authority* – when the principal creates the reasonable impression that the agent is authorized to act on the principal's behalf
 - A contract created by an agent within its apparent authority is just as enforceable
- Agency can arise as a matter of law
 - Ex: in partnerships each partner is an agent of that partnership

Ratification

- Even if an agency relationship does not exist, an agent can still enter into an agreement that ultimately binds a principal in limited circumstances
- If someone has no authority to act for you, the contract negotiated is not binding

- *Ratification* – when someone accepts a contract that was negotiated on their behalf but without their authority
- If you do ratify the agreement, the contract is binding on you
- If a principal does not ratify a contract, the agent is **not** personally liable to the third party
 - Unless the third party and agent intended the contract to be binding on the agent personally
- For ratification to be effective, must meet requirements:
 - Must be clear - can be either express or implied from behaviours though
 - Implied if you accept a product and use it
 - Occur within a reasonable time after the creation of a contract
 - Must accept whole contract or none of it
 - Principal must have been identified by the agent
 - Agent cannot make a contract, either on its own behalf or on behalf of some person the agent has not yet identified, and then try to find someone to ratify it
 - Principal must have had the legal capacity to enter the contract both at the time the agent created the contract and at the time of ratification
 - Minors or mentally disabled do not have legal capacity

When is the Principal Liable? The Scope of an Agent's Authority

- Where it looks like the person is an agent of the principal with authority to enter into contract, the third party wants to be able to rely on the agent having such authority
- In large transactions each party will do a significant amount of investigation to satisfy that the person executing a contract on behalf of the other party has authority to do so, and that the contract is enforceable
 - Backed up by documentation demonstrating authority exists
 - Ex: corporation's resolutions, lawyer's opinion regarding authority
- A third party usually does not know the extent of an agent's actual authority
 - Common indicators - name tag with title
 - When the principal's actions create a reasonable impression that the agent is authorized, that gives the agent apparent authority. the principal is liable to the third party under any contract created by the agent within the scope of that apparent authority (aka "ostensible authority," "agency by estoppels," "agency by holding out")
- Apparent and actual authority often overlap, but one can exist without the other
- Only the principal's conduct – not the agent's – is relevant
 - If the agent had apparent authority, but not actual, you would still be liable to the third party, but you could sue the agent for exceeding the scope of authority
 - If a principal allows an agent to act as if it had authority, such behaviour may be a representation that the agent has that authority
- *Usual Authority* – allows a person appointed to a particular position to exercise the authority usually associated with that position
 - What is usual is determined by reference to the authority of agents in similar positions in similar businesses
 - A principal will be bound by contracts with the agent's apparent authority only if the third party relied on that appearance of authority
 - Reliance is seldom hard to prove
 - Third party cannot enforce contract if it knew, or should have known, that the agent did not have authority

- When the principal is a corporation, one more requirement:
 - Agent must be someone who is permitted to make such a representation under the allocation of responsibility within the business organization
 - Third party could not rely on a representation from the agent alone if the agent did not have authority to enter contracts

When a Principal is Bound by the Acts of an Agent

- Agent acts within the scope of the actual authority given by the principal to the agent created
 - By express delegation to the agent
 - By appointing the agent to a position with that authority
 - By implication from the circumstances
- Agent acts within the scope of apparent authority created by the principal's representation to a third party, which may consist of:
 - Principal's statement or conduct
 - Principal's acquiescing (agreeing) to the agent acting with that authority
 - Principal appointing the agent to a position that would usually have that authority
- Agent enters into a contract on behalf of an identified principal's, but without the principal's authority, and the principal ratifies the contract

When is the Agent Liable?

- If the third party and the agent agree, the agent may be personally liable
 - May be agreed implicitly
- If the agent presented itself to the third party as the principal
 - Ex: agent fails to disclose that it was acting on behalf of a principal
- If the third party later discovers that the person it dealt with was only an agent, and if the agent **did** have authority to act on behalf of an *undisclosed principal*, the third party can hold either the agent or the principal liable
 - *Undisclosed Principal* – when the agent purports to contract without disclosing that is acting on behalf of a principal
 - To avoid risk, agent should explain role and disclose existence of principal
- Agent is not liable unless agent and third party agree that the agent would be
 - However, agent may be liable for any losses that the third party suffers as a result
 - Agent may be liable for fraud or deceit to the third party if makes a deal that it was not authorized to make
 - Even if there was no fraud, agent may be liable for *breach of warranty of authority*
 - *Breach of Warranty of Authority* – when an agent indicates that it is authorized to act for a principal when it is not
 - Liable even if honestly, but mistakenly, thought it had principal's authority
 - Third party does not bear the risk of loss when it is misled by the agent

The Agent's Duties to the Principal

- Agent must follow duties set out in contract
- Agent held responsible if fails to follow instructions
- Agent may have duties that are not mentioned in the contract, but that arise from circumstances related to the contract
 - Ex: insuring goods that agent was only contracted to sell
- Agent's obligation **cannot** be delegated to anyone else – they are personal obligations

- Important practical exceptions
 - Ex: hiring law firm, and law firm delegates work to partners and employees
- Agent owes *fiduciary duty* and *duty of care* to the principal

Fiduciary Duty

- *Fiduciary Duty* – requires an agent to act in good faith and in the best interests of the principal
- Agents must avoid situations in which their personal interests conflict with the best interests of their principals
 - Ex: principal wants to sell land, you cannot buy land, or sell to someone with whom you have a relationship
- Must pay any proceeds over to principal if breach fiduciary duty
- Fiduciary duty may be breached even if principal did not suffer any loss
- Fiduciary duty obligations:
 - Agent must disclose to principal any information that may be relevant to principal's interests (any bargains, sales etc.)
 - Agent cannot personally profit from any unauthorized use of information or opportunities that arose as a result of the agency relationship
 - An agent cannot compete with the principal
- Fiduciary duty may be displaced by the principal's instructions
 - If principal tells you to act in a certain way, you must, even if you think it is not in the principal's best interests

Duty of Care

- *Duty of Care* – requires an agent to take reasonable care in the performance of its responsibilities
 - Depends on what the agent agreed to do and the circumstances of the relationship
- If duty is breached, agent must compensate principal for any losses
 - Principal may be denied recovery if it knew that agent was incompetent or unqualified
- Agent must understand the scope of the obligations, ensure that it is able to fulfill these obligations and alert its principal to any deficiencies in its skills

The Principal's Duty to the Agent

- Principal must fulfill any obligation set out in the agency contract
- Principal must pay reasonable remuneration for the agent's services, unless agent agreed to work for free
- Principal must indemnify agent for liabilities and expenses that are reasonably incurred in connection with the agency relationship
 - Unless agent acts illegally or in breach of the agency agreement

Termination

- Either party gives notice of termination
 - Agency agreements often require a reasonable notice period
- Event occurs that results in termination under the terms of the agency contract
- Agent is appointed for a specific project or a particular period and it is completed or expires
- Performance of the agency becomes impossible
- Principal loses the capacity to contract as a result of death, insanity or bankruptcy
 - Agent may not be aware that incapacity occurred

- Principal cannot be held liable for obligations after incapacity occurs, so third party may try to hold the agent personally liable – liable for breach of warranty of authority
- If agent is an employee, relationship can only be terminated for just cause or with either reasonable notice or compensation in lieu of notice
- Nature of parties' relationship determines rules for termination

Risk Management Issues

- Contracts
 - A principal is liable for contracts created on its behalf by an agent with either apparent or actual authority
 - Actual authority easy to manage – clear statements in agency agreement
 - Apparent authority harder to manage
 - Principal must be careful when communicating with third parties, directly and indirectly
 - Principal can sue agent for breach of agency agreement if acts on apparent authority, beyond actual authority
 - If third party deals with agent before termination of agency relationship, and third party unaware of termination, may be able to enforce any new contracts unto the principal
 - Principal should notify all customers when it terminates an agent's authority
- Torts
 - Principal vicariously liable if:
 - Agent was an employee, and
 - Tort was committed within the course of employment
 - Principal generally entitled to recover amount paid from agent
 - May be liable if agent not an employee
 - If agent acting within the scope of actual or apparent authority,, the principal is liable for the agent's fraud or negligent misrepresentations

Business Relationships in Which Agency Issues Arise

- *Joint Venture* – a legal arrangement in which 2 or more parties combine their resources for a limited purpose, a limited time, or both
- *Strategic Alliance* – any arrangement in which 2 or more parties agree to co-operate for some purpose
- *Distributorship* – when one business enters into a contract to sell another's product

Franchises

- *Franchise* – a purely contractual relationship under which the franchisor gives the franchisee the right to operate its "system" in return for a set of fees
- Contain major provisions:
 - License allowing franchise to use franchisor's trademark
 - Obligations of the franchisor to assist in the operation of the franchised business
 - Training, uniforms etc.
 - Obligations of franchisee to maintain certain standards and follow certain rules and to pay fees, in part, based on the volume of sales
- A franchisee could be set up as an agency relationship, but in practice, franchise agreements invariably provide that the franchisee is not an agent of the franchisor
 - Minimizes risk to franchisor, but may still be liable

- Typically, franchise agreements will include a commitment by the franchisee to indemnify the franchisor for any liability it incurs relating to the operation of the business by the franchisee

Agents Covered by Special Statutes

- Special statutes protect the people with whom the agents deal required for some businesses
 - Ex: lawyers, real estate agents, insurance, stockbrokers, travel agents etc.
 - Person must either be licensed to work as a real estate agent, or be employed by a licensed agent
 - Real Estate agents must tell client about any compensation they will receive
 - Specific rules relating to trading (prohibits supplying false info), handling clients' money, advertising, disclosure of personal interest etc.
- Licensing bodies ensure that agents meet standards for competence, honesty, integrity and financial responsibility
 - Have power to suspend or revoke license of standards not met
- Regulatory regimes for agents often have a complaints process
 - Usually go to licensing body first to do investigation
- Stockbrokers have regulation standards for internal financial controls, insurance, requirements that firms have sufficient capital to remain solvent
 - Canadian Investor Protection Fund covers customers; losses of securities and cash balances resulting from the insolvency of a brokerage firm