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International Institute for the Unification of Private Law

WORKING GROUP FOR THE PREPARATION OF
PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS

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Chapter [...]

AUTHORITY OF AGENTS

(Revised draft prepared by Professor M.J. Bonell in the light of the discussions of the
Working Group at its 3rd session held in Cairo, 24-27 January 2000)

Rome, December 2000

INTRODUCTORY REMARKS

At its third session held in Cairo from 24 to 27 January 2000, the Working Group was seized of a revised draft Chapter on Authority of Agents (UNIDROIT 1999 Study L – Doc. 63) which took into account the decisions taken by the Group at its second session held in Bozen. The Group also considered the comments on this draft submitted by Professors D. DeMott and F. Reynolds (UNIDROIT 1999 Study L – Doc 63./Add.1). The draft provisions set out below take into account the discussions the Group had on both documents in Cairo (UNIDROIT 2000 Study L – Misc. 22, paras 845-887).

In order to highlight the changes made to the previous draft deleted text appears struck out and additions appear underlined.

Article 1
(Scope of the chapter)

(1) This chapter governs the authority of a person, the agent, to affect the legal relations of another person, the principal, by or with respect to a contract with a third party, whether the agent acts in its own name or in that of the principal.

(2) It is concerned only with the relations between the principal or the agent on the one hand, and the third party on the other.

(3) It does not govern an agent's authority conferred by law or the authority of an agent appointed by a public or judicial authority.

Note by the Rapporteur:

No changes with respect to the previous draft.

Article 2
(Establishment and scope of the authority of the agent)

(1) The principal's grant of authority to an agent may be express or implied.

(2) The agent has authority to perform all acts necessary in the circumstances to achieve the purposes for which the authority was granted.

Note by the Rapporteur:

No changes with respect to the previous draft.

Article 3
(Agent's act directly affecting legal relations between principal and third party)

(1) Where an agent acts within the scope of its authority and the third party knew or ought to have known that the agent was acting as an agent, the acts of the agent shall directly affect the legal relations between the principal and the third party and no legal relation is created between the agent and the third party.

(2) Notwithstanding paragraph 1, the acts of the agent shall affect only the relations between the agent and the third party, ~~where it follows from the circumstances of the case that the agent intended to do so.~~ [where the agent, in agreement with the principal, undertakes to become itself party to the contract].

Note by the Rapporteur:

This article corresponds in substance to Article 12 of the Geneva Convention and was adopted by the Working Group at its 2nd session in Bozen (cf. UNIDROIT 1999 Study L – Misc. 21, paras. 95-107).

Para. 2 in its previous version was criticised by DeMott and Reynolds because its wording seemed to suggest that the agent could on its own initiative decide to become the person to benefiting from the transaction instead of the principal (cf. UNIDROIT 1999 Study L – Doc 63/Add.1). Since this was clearly not intended, in Cairo the Rapporteur was asked to reword the paragraph in order to express more clearly the idea behind the provision (cf. UNIDROIT 2000 Study L – Misc. 22, paras. 882-883).

Para. 2 is intended to cover the situation where the agent, though acting openly on behalf of a principal, does not directly bind the principal, but in agreement with the latter, becomes itself party to the contract with the third party. In practice this occurs either because the agent, in agreement with the principal, stipulates with the third party that it alone and not the principal will be bound by the contract, or because the agent is acting as a so-called commission agent who under a number of domestic laws by definition binds only itself. One way of making it clear that under no circumstances will the agent's intention alone be controlling is to go back to the original wording of Article 12 of the Geneva Convention (“... unless it follows from the circumstances of the case, for example by a reference to a contract of commission, that the agent undertakes to bind himself only”) or – as is the intention of the amended version here proposed - to state expressly that the agent can validly stipulate with the third party that it itself becomes party to the contract only if this is done in agreement with the principal.

Article 4

(Agent's act not directly affecting legal relations between principal and third party)

(1) Where [an the agent acts within the scope of its authority, and] the third party neither knew nor ought to have known that the agent was acting as an agent, the acts of the agent shall affect only the relations between the agent and the third party. ~~if:~~

~~(a) it follows from the circumstances of the case that the agent intended to do so, or~~

~~(b) the third party neither knew nor ought to have known that the agent was acting as an agent.~~

~~(2) Notwithstanding paragraph 1, where an agent acts as the apparent owner of a business, the third party, upon discovery of the real owner of the business, may exercise also against the latter the rights it has against the agent.~~

~~(a) where the agent commits a fundamental non-performance or it is clear that there will be a fundamental non-performance of its obligations towards the principal, the principal may exercise against the third party the rights acquired on the principal's behalf by the agent, subject to any defences which the third party has against the agent;~~

~~(b) where the agent commits a fundamental non-performance or it is clear that there will be a fundamental non-performance of its obligations towards the third party, the third party may exercise against the principal the rights which the third party has against the agent, subject to any defences which the agent has against the third party and which the principal has against the agent.~~

~~(3) In the cases referred to in paragraph 2, the agent shall on demand communicate the name of the principal to the third party, or the name of the third party to the principal, as the case may be.~~

~~(4) The rights under paragraph 2 may be exercised only if within reasonable time notice of intention to exercise them is given to the agent and the third party or principal, as the case may be. As soon as the third party or principal has received such notice, it may no longer free itself from its obligations by dealing with the agent.~~

Note by the Rapporteur:

This article in its previous version corresponded in substance to Article 13 of the Geneva Convention and was intended to reconcile the common law doctrine of the so-called undisclosed principal and the civil law concept of commission agent. Indeed para. 1 stated the general rule that both the agent acting on behalf of an undisclosed principal and the commission agent, though acting within the scope of their authority, do not directly affect the relations between the principal and the third party, but are themselves parties to the contract. Para. 2 provided for an exception to this rule by admitting in case of default by the agent a direct action by the principal against the third party and vice versa.

The article, in particular para. 2, met with considerable criticism at the Working Group's second session (cf. UNIDROIT 1999 Study L – Misc. 21, paras. 267-273). Also DeMott and Reynolds were in principle against the provision and stressed that

even in Common Law systems the doctrine of the undisclosed principal was no longer considered essential.

However DeMott suggested keeping para. 2 (b). In her view the third party's right to sue the principal is particularly important in a situation in which a third party had dealt with an actor over some time when, without informing the third party, the actor transferred its business assets to a newly formed limited liability vehicle and continued to deal with the third party as an undisclosed agent of the new company.

Leaving aside whether *Grinder v. Bryans Road Bldg. and Supply Co.*, 432 A.2d 453 (Md. App. 1981), cited as the leading case, is really all that pertinent (what seems to have been at stake in this case was rather the third party's right to sue the agent after having unsuccessfully sued the company, with the Court, overruling previous decisions to the contrary, stating that indeed the third party may proceed to judgment against both, but is limited to one satisfaction), the problem highlighted by DeMott clearly exists and was as such widely acknowledged by the Working Group at its last session in Cairo (cf. UNIDROIT 2000 Study L – Misc. 22, paras. 869-880).

Assuming that the Group still prefers not to keep Article 4 in its entirety, three possible solutions may be envisaged:

- to keep the provision contained in Article 4 (2)(b);
- to have a provision addressing more specifically the type of cases discussed in Cairo; or
- to let such cases be settled on the basis of principles and rules to be found elsewhere in the Principles or in the otherwise applicable law (prohibition of *venire contra factum proprium*, doctrine of undisclosed principal, unjust enrichment, tort law, etc.).

With respect to the first solution, it may be argued that the language of Article 4 (2)(b) is too generic and would therefore cover too wide a range of cases.

On the other hand, not to address at all the type of cases discussed in Cairo in the present chapter would hardly appear justifiable, not only in view of the frequency with which they occur in practice but also because they would risk being decided differently in different jurisdictions.

That leaves the adoption of a provision specifically addressing the type of cases in question. As to its content, it may be recalled that also civil law systems tend to admit that in commercial transactions a third party dealing with a person it believes to be the owner of the enterprise but who in fact merely acts as that enterprise's agent may, after discovering the truth, sue both that person and the real owner of the enterprise provided that the former had actual or apparent authority to act on behalf of the latter. In this sense see e.g. Article 2208 of the Italian Civil Code ("A managing director of an enterprise is personally liable if he fails to inform the third party that he is dealing on behalf of the owner of the enterprise; however, the third party can bring an action also against the owner of the enterprise for those acts of the managing director pertaining to the enterprise"); for German law K. SCHMIDT, *Handelsrecht* (1999), p. 123 *et seq.* (referring to a case decided by the German Supreme Court (BGHZ 62, 216): a manufacturer, after having transferred his business assets to a partnership he set up with his wife, continued to contract in his own name without disclosing to third parties that he was in fact acting as the managing director of the partnership; held, that the creditors could also sue the partnership as it was the real owner of the enterprise).

In the light of the foregoing it is suggested that Article 4 be amended as follows: para. 1 corresponds to para. 1(b) of the old version of Article 4, while para. 2 is new and is intended to cope with the type of cases discussed in Cairo.

If the article were to be accepted in its amended form, the result would be that generally in cases of an undisclosed principal and a commission agent, there will no longer be a direct action between the principal and third party or viceversa, while only in the type of cases discussed in Cairo the third party will be entitled to sue both the agent and the principal.

Article 5

(Agent acting without or outside its authority)

(1) Where an agent acts without authority or outside the scope of its authority, its acts do not affect the legal relations between the principal and the third party.

(2) Nevertheless, where the principal causes the third party reasonably and in good faith to believe that the agent has authority to act on behalf of the principal and that the agent is acting within the scope of that authority, the principal may not invoke against the third party the lack of authority of the agent.

Note by the Rapporteur:

No changes with respect to the previous draft.

Article 6

(Liability of agent acting without or outside its authority)

(1) An agent that acts without authority or outside the scope of its authority shall, failing ratification by the principal ~~according to Article 9~~, be liable for damages so as to put the third party in the same position as it would have been in ~~had the agent not acted at all. if the agent had acted with authority and within the scope of its authority.~~

(2) The agent shall not be liable, however, if the third party knew or ought to have known that the agent had no authority or was acting outside the scope of its authority.

Note by the Rapporteur:

Article 6 in its amended version corresponds literally to Article 16 of the Geneva Convention. At its second session in Bozen the Working Group by a majority decided to limit damages to reliance interest. However at its third session in Cairo, it decided to reverse its decision and to grant expectation interest.

Article 7
(*Conflict of interests*)

(1) If a contract concluded by an agent involves the agent in a conflict of interests with the principal of which the third party knew or could not have been unaware, the principal may avoid the contract. The right to avoid is subject to Articles 3.12 and 3.14 to 3.16.

(2) However, the principal may not avoid the contract

(a) if it had consented to, or knew or could not have been unaware of, the agent's so acting; or

(b) if the agent had disclosed the conflict of interest to it and it had not objected within a reasonable time.

Note by the Rapporteur:

No changes with respect to the previous draft.

Article 8
(*Subagency*)

An agent has implied authority to appoint a subagent to perform acts which it is not reasonable to expect the agent to perform itself. The rules of this chapter apply to the subagency.

Note by the Rapporteur:

No changes with respect to the previous draft.

Article 9
(Ratification)

(1) An act by an agent that acts without authority or outside the scope of its authority may be ratified by the principal. On ratification the act produces the same effects as if it had initially been carried out with authority.

(2) The third party may by notice to the principal specify a reasonable period of time for ratification. If the principal does not ratify within that period it can no longer do so.

Note by the Rapporteur:

Para. 1 of this Article literally corresponds to para. 1 of Article 15 of the Geneva Convention. Para. 2 was added by the Working Group at its second session in Bozen (UNIDROIT 1999 Study L – Misc. 21, para. 224).

In Cairo, also in the light of DeMott's remarks, the Group asked the Rapporteur to reconsider the question as to whom a ratification must be directed and possibly to prepare a new draft provision to be included in this Article.

The question as to whom ratification must be directed has already been extensively discussed by the Group in Bozen. The version of Article 9 considered at that time contained a paragraph which corresponded to Article 15 (5) of the Geneva Convention and the first sentence of which stated that "[r]atification shall take effect when notice of it reaches the third party or the ratification otherwise comes to its attention". While there was some support for this provision the majority of the Group favoured its deletion. It was felt that the rule that ratification could only be effective if the third party knew of it was too narrow since ratification, in some legal systems at least, was primarily a matter between the principal and the agent which did not need to be brought to the attention of the third party at all. An additional reason for deleting the provision was that at the same session in Bozen the Group had decided to add a new paragraph 2 to Article 9. This paragraph, by providing that the third party who learns of the agent's lack of authority may request the principal to ratify within a reasonable period of time, and that failing to do so the principal can no longer ratify at a later date, already offers the third party a means of ascertaining the principal's real intention.

Also in view of the fact that domestic laws do not generally provide for any hard and fast rule as to what amounts to ratification and when it becomes effective vis-à-vis the third party (see e.g. for U.S. law DeMott's remarks; for English law BOWSTEAD & REYNOLDS ON AGENCY (1996) pp. 64, 80-83; for German law SCHRAMM in *Münchener Kommentar zum BGB* (1993) Anm. 21-26 zu § 177; for French law STARCK/ROLAND/BOYER, *Obligations - 2. Contrat* (1993), Nr. 234; for Italian law CIAN/TRABUCCHI, *Commentario Breve al Codice Civile* (1999), p. 1230), it is here suggested that the Group's decision taken in Bozen be maintained. In other words, the issues at stake should not be dealt with at all in the black letter rules but the Comments could explain that ratification, just as the granting of authority, is a unilateral manifestation of intent which may be either express or

implied from words or conduct and that, though normally communicated to the agent, to the third party, or to both, ratification need not be communicated to anybody provided that it is manifested in some way and can therefore be ascertained by probative material.

Article 10
(*Termination of authority*)

(1) Termination of authority shall not be effective in relation to the third party unless it knew or ought to have known of the termination.

(2) Notwithstanding the termination of its authority, an agent remains authorized to perform the acts which are necessary to prevent harm to the principal's interests.

Note by the Rapporteur:

No changes with respect to the previous draft.