

# Introduction to Agency Law

by Sophia



## WHAT'S COVERED

In this lesson, you will learn about another area of law that has implications for business organizations. Specifically, this lesson will cover:

## 1. The Importance of Agency Law

The **Restatement (Third) of Agency** states in §1.01:

“**Agency** is the fiduciary relationship that arises when one person (a **principal**) manifests **assent** to another person (an **agent**) that the agent shall act on the principal’s behalf and subject to the principal’s control, and the agent manifests assent or otherwise consents so to act.”

Most organized human activity - and virtually all commercial activity - is carried on through agency. No corporation would be possible, even in theory, without such a concept.

➔ **EXAMPLE** We might say, “General Motors is building cars in China,” but we can’t shake hands with General Motors. “The General,” as people say, exists and works through agents.

Likewise, partnerships and other business organizations rely on agents to conduct business. Indeed, it is not an exaggeration to say that agency is the cornerstone of enterprise organization. In a partnership, each partner is a general agent; under corporation law, the officers and employees are agents of the corporation.

The existence of agents does not, however, require a whole new law of torts or contracts. A tort is no less harmful when committed by an agent; a contract is no less binding when negotiated by an agent.

What does need to be taken into account, though, is the manner in which an agent acts on behalf of his principal and toward a third party, possibly creating liability for the principal.



## TERMS TO KNOW

### Restatement (Third) of Agency

A summary of the law of agency published by the American Law Institute in 2006, revising the previous Restatement (Second) of Agency. It is a secondary (not primary as statutes and case law are) source of law, but more highly respected and relied on by courts than most secondary sources. Still, not all states follow restatements of the law exactly.

**Agency**

An area of the law concerned with the relationship between principal, agent, and third parties. A relationship whereby one person acts on the authority of another.

**Principal**

In an agency relationship, the person on whose authority an agent is acting; the source of authority.

**Assent**

Agreement or compliance that is wholly voluntary.

**Agent**

A person who acts on another's authority and on behalf of the one with authority.

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## 2. Recurring Issues in Agency

Several problematic scenarios recur in agency, and law has developed in response.

**IN CONTEXT**

Consider John Alden (1599–1687), one of the most famous agents in American literature. He is said to have been the first person from the Mayflower to set foot on Plymouth Rock in 1620; he was a carpenter, a cooper (barrel maker), and a diplomat.

His agency task - of interest here - was celebrated in Henry Wadsworth Longfellow's poem, "The Courtship of Miles Standish." He was to woo Priscilla Mullins (d. 1680), "the loveliest maiden of Plymouth," on behalf of Captain Miles Standish, a valiant soldier who was too shy to propose marriage. Standish turned to John Alden, his young and eloquent protégé, and beseeched Alden to speak on his behalf, unaware that Alden himself was in love with Priscilla.

Alden accepted his captain's assignment, despite the knowledge that he would thus lose Priscilla for himself, and sought her out. But Alden was so tongue-tied that his vaunted eloquence fell short, turned Priscilla cold toward the object of Alden's mission, and eventually led her to turn the tables in one of the most famous lines in American literature and poetry: "Why don't you speak for yourself, John?" John eventually did: The two were married in 1623 in Plymouth.

Let's analyze this sequence of events in legal terms— recognizing, of course, that this example is an analogy and that the law, even today, would not impose consequences on Alden for his failure to carry out Captain Standish's wishes.

Alden was the captain's agent: He was specifically authorized to speak in his name in a manner agreed on, toward a specified end, and he accepted the assignment in consideration of the Captain's friendship. He had, however, a conflict of interest. He attempted to carry out the assignment, but he did not perform according to expectations. Eventually, he wound up with Priscilla himself.

Here are some questions to consider, the same questions that will recur throughout the discussion of agency:

1. How extensive was John's authority? Could he have made promises to Priscilla on the captain's behalf—for example, that Standish would have built her a fine house?
2. If he committed a tort, could he have imposed liability on his principal? Suppose, for example, that he had ridden at breakneck speed to reach Priscilla's side and, en route, ran into and injured a pedestrian on the road. Could the pedestrian have sued Standish?
3. Suppose Alden had injured himself on the journey. Would Standish be liable to Alden?
4. Is Alden liable to Standish for stealing the heart of Priscilla— that is, for taking the "aim" of the enterprise for himself?

As these questions suggest, agency law often involves three parties:

- The principal
- The agent
- A third party

It therefore also deals with three different relationships:

- Between principal and agent
- Between principal and third party
- Between agent and third party

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## 3. Creation of the Agency Relationship

The agency relationship can be created in two ways:

- By agreement (expressly)
- By operation of law (constructively or implicitly)

### 3a. Agency Created by Agreement

Most agencies are created by contract. Thus, the general rules of contract law covered in Unit 2 apply. But agencies can also be created without contract, by agreement.

Therefore, three contract principles are especially important:

1. Consideration
2. Writing
3. Capacity

Agencies created by consent - agreement - are not necessarily contractual. It is not uncommon for one person to act as an agent for another without consideration.

➞ **EXAMPLE** Abe asks Byron to run an errand for him— to buy some lumber on his account at the local lumberyard. Such a gratuitous agency gives rise to no different results than the more common contractual agency.

Most oral **agency contracts** are legally binding; the law does not require that they be reduced to writing. In practice, many agency contracts are written to avoid problems of proof.

And there are situations where an agency contract must be in writing as previously covered in the lessons on

unenforceable contracts and the Statute of Frauds:

1. If the agreed-on purpose of the agency cannot be fulfilled within one year or if the agency relationship is to last more than one year
2. In many states, an agreement to pay a commission to a real estate broker
3. In many states, authority given to an agent to sell real estate
4. In several states, contracts between companies and sales representatives

Even when the agency contract is not required to be in writing, contracts that agents make with third parties often must be in writing. Thus, Section 2-201 of the Uniform Commercial Code specifically requires contracts for the sale of goods for the price of five hundred dollars or more to be in writing and “signed by the party against whom enforcement is sought or by his authorized agent.”

Lastly, a contract is void or voidable when one of the parties lacks capacity to make one, or if both the principal and agent lack capacity.

#### IN CONTEXT

If a minor appoints another minor to negotiate or sign an agreement, there can be no question of the contract’s voidability. But suppose only one or the other lacks capacity.

Generally, the law focuses on the principal. If the principal is a minor or otherwise lacks capacity, the contract can be avoided even if the agent is fully competent. There are, however, a few situations in which the capacity of the agent is important. Thus, a mentally incompetent agent cannot bind a principal.



#### TERM TO KNOW

##### Agency Contract

A contract creating a relationship between an agent and principal that creates the agency relationship.

### 3b. Agency Created by Operation of Law

Most agencies are made by contract, but agency also may arise impliedly or apparently. In areas of social need, courts have declared an agency to exist in the absence of an agreement. The agency relationship then is said to have been implied “by operation of law.”

#### IN CONTEXT

Children in most states may purchase necessary items, such as food or medical services, on the parent’s account. Long-standing social policy deems it desirable for the head of a family to support his dependents, and the courts will put the expense on the family head in order to provide for the dependents’ welfare. The courts achieve this result by supposing the dependent to be the family head’s agent, thus allowing creditors to sue the family head for the debt.

**Implied agencies** also arise where one person behaves as an agent would and the “principal,” knowing that the “agent” is behaving so, acquiesces, allowing the person to hold himself out as an agent.

However, **apparent agencies** can exist as well.

➔ **EXAMPLE** Suppose Arthur is Paul's agent, employed through October 31. On November 1, Arthur buys materials at Lumber Yard - as he has been doing since early spring - and charges them to Paul's account. Lumber Yard, not knowing that Arthur's employment terminated the day before, bills Paul. Will Paul have to pay? Yes, because the termination of the agency was not communicated to Lumber Yard. It appeared that Arthur was an authorized agent.



#### TERMS TO KNOW

##### **Implied Agency**

An agency that is created by acts of the parties.

##### **Apparent Agency**

An agency that does not actually exist, but appears to exist based on inaccurate representations by one who claims to be an agent.



#### SUMMARY

In this lesson, you learned that **agency law is important** because many transactions are conducted by agents who act on behalf of another. All corporate transactions are so conducted because corporations cannot themselves actually act; they are legal fictions. **Recurring issues in agency law** include the scope of the agent's authority and the duties and liabilities among and between the principal, agent, and third party.

**Creation of the agency relationship** may occur expressly, as in the case of **agencies created by agreement**. They are not necessarily contractual, but contract law applies to most such agencies. **Agencies created by operation of law** may arise implicitly or apparently.

Best of luck in your learning!

Source: THIS TUTORIAL HAS BEEN ADAPTED FROM (1) "BUSINESS LAW AND THE LEGAL ENVIRONMENT" VERSION 1.0 BY DON MAYER, DANIEL WARNER, GEORGE SIEDEL, AND JETHRO K. LIEBERMAN. COPYRIGHT 2011. ISBN 978-1-4533-3050-0. (2) "THE LEGAL AND ETHICAL ENVIRONMENT OF BUSINESS" VERSION 1.0 BY TERENCE LAU AND LISA JOHNSON. COPYRIGHT 2012. ISBN 978-1-4533-2750-0 (LICENSEE PRODUCT: BUSINESS LAW), BOTH SOURCES REPRINTED WITH PERMISSION FROM FLATWORLD.



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