CHAPTER 1

Introductory Concepts in the Law of Agency

§1.1 THE AGENCY RELATIONSHIP DEFINED AND EXEMPLIFIED; ITS PLAYERS IDENTIFIED

§1.1.1 The Classic Definition

Agency is the label the law applies to a relationship in which:

- by mutual consent (formal or informal, express or implied)
- one person or entity (called the "agent")
- undertakes to act on behalf of another person or entity (called the "principal")
- subject to the principal's control.

§1.1.2 The Players: Principal and Agent; Their Ubiquity

Agency relationships are everywhere in the commercial world and in noncommercial realms as well. Whenever a person or organization seeks to act through the efforts of others, the legal concept of agency likely applies. For example:

- A student, seeking a place to live while attending law school, submits a rental application to the manager of an apartment building. Acting on behalf of the building owner, the manager checks the application and then accepts the student as a tenant. The manager acts as the owner's agent.
- A corporate shareholder, unable to attend the corporation's annual meeting, signs a "proxy" that authorizes another individual to cast the shareholder's votes at the meeting. By accepting the appointment, the proxy holder becomes the shareholder's agent.
- A landowner, preparing to leave for an around-the-world tour and wishing to sell Greenacre as soon as possible, gives a real estate broker a "power of attorney." This credential authorizes the broker to sell Greenacre on the owner's behalf and to sign all documents necessary to form a binding contract and to close the deal. The broker is the owner's agent.
• A supermarket chain that is about to purchase fancy new computerized cash registers retains a consultant to advise on what type of registers to buy and to arrange the purchase of the new machines on the chain's behalf. The consultant acts as the chain's agent.
• A bank, knowing that not all customers like dealing with ATMs, hires tellers to handle customer deposits, withdrawals, and similar transactions. The tellers are agents of the bank.

In each of these situations, someone (the "principal") has asked someone else (the "agent") to provide services or accomplish some task on behalf of the principal and subject to the principal's control. In each situation the agent has agreed to do so. To each situation, the label of "agency" applies.\(^1\)

Agency relationships also appear in literature, as in Longfellow's "Courtship of Miles Standish." Standish, seeking to court "the damsel Priscilla" but too shy to do so directly, entreats his friend John Alden to communicate to Priscilla the depth and direction of Standish's feelings. Alden agrees and becomes Standish's agent.\(^2\) Fictional agents can also be less beneficent. In Dumas's *The Three Musketeers*, Cardinal Richelieu uses the infamous Lady de Winter as his agent to trick the Duke of Buckingham and steal the diamonds secretly given him by the Queen of France.\(^3\)

An agent can be an individual human being or an organization, such as a limited liability company, corporation, not-for-profit corporation, general partnership, or limited partnership. The same is true for a principal. The R.2d mostly contemplates individual actors, while the R.3d gives considerable attention to organizations both as principals and agents. A machine or computer program, in contrast, cannot be an agent, even when serving an intermediary function.\(^4\)

### §1.1.3 The Role of Third Parties

The agency relationship may appear at first to involve only the principal and the agent. But principals typically use agents to deal with the rest of the world, or at least some part of it; thus the agent often functions as the principal's "interface" with others.\(^5\) As a result, third parties figure prominently in the law of agency.

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\(^1\) The law of agency also applies when a party merely appears to be authorized to act for another. Sections 2.3 and 2.5 discuss the law of "apparent authority" and "agency by estoppel."


\(^4\) Thus, the Uniform Computer Information Transactions Act, § 102(a)(27) uses a label that is oxymoronic from an agency law perspective: "‘Electronic agent’ means a computer program, or electronic or other automated means, used independently to initiate an action, or to respond to electronic messages or performances, on the person's behalf without review or action by an individual at the time of the action or response to the message or performance.” For further discussion of the law’s careless use of agency law concepts, see § TBD.

\(^5\) However, agency law also "encompasses the employment relation, even as to employees whom an employer has not designated to…interact with parties external to the employer's organization." R.3d, § 1.01,
<TEXT>The R.2d reflects this situation with a paradigmatic approach to illustrations which has influenced generations of law school examples: $P$ represents the principal; $A$ the agent; and $T$ the third party. The R.3d continues the use of $P$ and $A$, but varies the letters designating third parties.

### §1.2 CATEGORIES AND CONSEQUENCES: WHY DO THE LABELS MATTER?

Our system of law operates largely through a process of "categories and consequences"; that is, defining categories of behavior or characteristics and attaching consequences to those categories. This phenomenon is salient in agency law. People concern themselves with agency law labels because people are concerned about the consequences attached to those labels. For example, if $A$ is an agent of $P$, then (among other consequences) $A$ owes a duty of loyalty to $P$ and $P$ has certain obligations to indemnify $A$.6

This "category and consequences" architecture has two major practical implications for those dealing with agency law.

### §1.2.1 The First Practical Implication: Sharpening the Questions We Ask

In the practice of agency law, the question "Is $X$ an agent of $Y$?" is almost always an incomplete question and usually a bad one. The better question is, "For the purposes of [specified consequence], is $X$ an agent of $Y$?" The latter question is better because the context (the specified consequence) directs the analysis toward the appropriate subcategories and sub-issues.

**Example:** In *Great Expectations*, Pip receives ongoing support from an unnamed benefactor who acts through Mr. Jaggers. In the following passage, which occurs just after Mr. Jaggers hands Pip a £500 note, Pip is speaking.

> I was beginning to express my gratitude to my benefactor for the great liberality with which I was treated, when Mr. Jaggers stopped me. "I am not paid, Pip," said he, coolly, "to carry your words to any one," and then gathered up his coat-tails, as he had

Comment c. In this context, the key agency issues are the agent's duty of loyalty to the principal and the question of whether the employer is automatically (vicariously) liable for torts committed by the employee within "the scope of employment." Section 4.1.1 discusses an agent's duty of loyalty. Sections 3.2-3.2.6 discuss the notion of *respondeat superior*—vicarious liability for the torts of an employee.

6 See sections 4.1.1 (duty of loyalty) and 4.3.1 (principal's duty to indemnify).
gathered up the subject, and stood frowning at his boots as if he suspected them of designs against him.7

In this context, the question "Is Mr. Jaggers the agent of the unnamed benefactor?" would be at best overbroad. Mr. Jaggers seems to be the agent of the unnamed benefactor for the purposes of delivering money and perhaps information, but not for the purposes of receiving information.

§1.2.2 The Second Implication: Which Drives the Analysis – Categories or Consequences?

If we think of legal rules as “if/then” structures,8 then categories come before consequences. If a set of facts fits within category A, then the consequences of A result.

However, categories are labels for rules, and the rules are tools for achieving particular types of consequences. In most disputes, consequences drive the analysis. Which agency label or category applies depends on which consequence is at issue.

Example: Tort Victim claims that Y should be legally responsible for X’s tort. Most often, the key category will not be "agent" but rather "servant" (or "employee"), a quasi-subcategory of agent.9

Example: Tenant claims to have given notice to Landlord by leaving a note with Landlord's custodian. The appropriate category is agent, and the appropriate subcategories are actual authority and apparent authority.10

In contrast, in transactional lawyering, categorization typically drives the analysis, at least initially. In most transactional situations, the relevant facts are not entirely set, and good legal work involves at least the following five steps:

1. Discerning and understanding the client's business objectives and the client's plans for achieving those objectives
2. Imagining the facts that will result from using those plans to pursue those objectives
3. Identifying relevant legal categories that might apply to those facts, thereby predicting unpalatable legal consequences that might result from such categories (sometimes known as "assessing the legal risk" or “determining exposures”)

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7 Charles Dickens, Great Expectations, ch. 36.
8 See TBD [introductory materials]
9 See section 3.2.4 discussing respondeat superior, which makes a "master" (or "employer") vicariously liable for the torts of a "servant" (or "employee").
10 For a discussion of these subcategories, see sections 2.2 (actual authority) and 2.3 (apparent authority).
4. Rethinking the client's objectives and plans in light of the perceived legal risks (sometimes called "exposures")
5. Seeking to reconfigure the client's objectives and plans (and the resulting facts) so as to:
   ~ <BSL>avoid the dangerous categorizations and thereby the unpalatable legal consequences while
   ~ still achieving most (and perhaps all) of the client’s objectives.

Thus, in the transactional paradigm, while consequences remain all-important, it is mostly categories that drive the analysis.

§1.3 THE TWO ROLES OF AGENCY LAW: AUXILIARY OR CHOATE

Black's Law Dictionary defines "auxiliary" as "[a]iding or supporting," and "choate" as "[c]omplete in and of itself." These two terms reflect the two different roles of agency law.

§1.3.1 Agency Law as the "Main Event"

Sometimes, agency law "in and of itself" provides the rule or rules sufficient to analyze a situation.

Example: X, while undertaking a task on behalf of Y, learns of a business opportunity different from but related to the task. Without obtaining Y's consent or even informing Y of the opportunity, X takes the opportunity for herself. Y later claims that X must "disgorge" the profits realized from exploiting the opportunity. Agency law "in and of itself" can resolve this dispute: (1) Was X acting as Y's agent? (2) If so, the agent's "duty of loyalty" applies and X must indeed disgorge the profits.

§1.3.2 Agency Law in Its Supporting Role

Often agency law plays only an auxiliary role, and the "main event" occurs in some realm of substantive law; for example, torts or contracts.

Example: Hadley sues Baxendale, alleging breach of an oral contract for services. Hadley acknowledges that Baxendale himself never manifested assent to the alleged contract but asserts that one of

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12 For a discussion of this aspect of the duty of loyalty, see section 4.1.1.
13 The phrase substantive law is most commonly used in contradistinction to procedural law. This book uses the phrase in contradistinction to agency law's auxiliary role.
Baxendale's clerks did so. Agency law determines whether the clerk's manifestations are attributed to Baxendale. Although this auxiliary question can be dispositive, the "main event" is in the substantive arena of contract law.

Of course, the agency analysis is unnecessary unless Hadley can prove factually that:

- the clerk made manifestations,
- which, even if treated (per agency law) as the manifestations of Baxendale,
- would suffice as a matter of contract law to establish a binding contract containing the terms relevant to the contract-law claim of breach.

Note that the situation is conceptually complicated because it involves both:

- the interrelationship between contract law as the "main event" and agency law as the essential auxiliary; and
- the difference between the realm of legal rules and the realm of facts.

To make matters even more complicated:

- the legal rules determine which facts might be important, but, at the same time and interactively,
- what facts exist or might exist that help shape the legal analysis and can even determine which legal rules might be worth invoking.

Example: In the Hadley-Baxendale Example above, Hadley discovers to his chagrin that he cannot carry the burden of proving the necessary manifestations by Baxendale's clerk. This factual determination might cause Hadley to look to another area of substantive law, perhaps bailment.

§1.4 CREATION OF THE AGENCY RELATIONSHIP

§1.4.1 The Restatement's View of Creation

The first section of the R.3d describes the creation of an agency relationship as follows:

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14 For a discussion of the relevant theories of agency law, see section 2.3.
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.\footnote{R.3d, §1.01. R.2d §1 was to the same effect, but without gender-neutral language and without the embedded defined terms: "Agency is the fiduciary relation which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act."}

Several aspects of this description warrant special attention. Some relate to elements necessary to create an agency relationship. Others relate to the consequences that follow when an agency relationship exists.

**§1.4.2 Manifestation of Consent**

The creation of an agency relationship necessarily involves two steps: manifestation by the principal and consent by the agent. The manifestation by or attributable to the principal\footnote{A manifestation can be "attributable to the principal" under the doctrines of agency law. See sections 2.2.2 and 2.4.8.} must somehow reach the agent, otherwise the agent has nothing to which to consent. When the agent then manifests consent, an agency exists—even though the principal may initially be unaware of the manifestation.

**Example:** Smitten with equal amounts of love and timidity, Miles Standish manages a face-to-face conversation with his friend John Alden, in which Standish asks Alden to speak to the fair Priscilla on Standish's behalf. Alden agrees, and an agency relationship exists.

**Example:** Disappointed to learn that Yoram, her favorite guide, will be unavailable when she visits Alaska, Naomi sends him the following email: "Very disappointed. Will you locate and hire for me someone of comparable quality and price range for the dates I sent you?" Yoram hits the "reply" button and types, "Sure." He promptly receives an automated "out of the office" response, indicating that Naomi is gone for the weekend. A principal-agent relation now exists. It is irrelevant that the principal is as yet unaware of the agent's manifestation.

**Example:** Yoram contacts Dennis, explains the situation, and determines that Dennis is willing and available for the time Naomi wants. Yoram then emails to Naomi a description of Dennis's qualifications and rate. Naomi promptly replies, "Fine. Go ahead." Yoram tells Dennis, "The job is yours." Dennis replies, "Great." Naomi and Dennis are now principal and agent; the principal's manifestation of consent was communicated indirectly but nonetheless effectively.
§1.4.3 Objective Standard for Determining Consent

To determine whether a would-be principal and would-be agent have consented, the law looks to their outward manifestations rather than to their inner, subjective thoughts. The law's interpretive viewpoint is that of a reasonable person. In particular:

- Has the would-be principal done or said something that a person in the position of the would-be agent would reasonably interpret as consent by the would-be principal that the would-be agent act for the would-be principal?
- In response, has the would-be agent done or said something that a person in the position of the would-be principal would reasonably interpret as consent to act for the would-be principal?

Typically it is the parties' words that evidence their reciprocal consents. However, given the law's objective standard, a party's conduct can also evidence consent. For example, an agent can manifest consent by beginning the requested task:

Example: Rachael, the owner of Blackacre, writes to Sam: "Please act as my broker to sell Blackacre." Sam puts a "For Sale" sign on Blackacre. By beginning the requested task Sam has given the necessary manifestation of consent. An agency relationship exists.

The objective standard also means that, in the eyes of the law, two parties can be agent and principal even though one of them had no subjective desire to create the legal relationship. Thus, even a reasonable misinterpretation can create an agency relationship.

Example: Frustrated by the recalcitrance of Thomas Becket, the Archbishop of Canterbury, Henry II of England exclaims, "Will nobody rid me of this troublesome cleric?" Four of Henry's barons overhear the remark and proceed to kill Becket, believing that they are acting on behalf of and subject to the control of the king. Although Henry later protests that he never intended for anyone to kill the Archbishop, the barons nonetheless acted as his agents. In these circumstances Henry's outward manifestation, reasonably interpreted, indicated consent. Even assuming that Henry's protest is genuine, his subjective intent is irrelevant.

§1.4.4 Consent to the Business or Interpersonal Relationship, Not to the Legal Label

In this respect, agency law follows the modern approach to contract formation.
Agency is a legal concept—a label the law attaches to a category of business and interpersonal relationships. If two parties manifest consent to the type of business or interpersonal relationship the law labels "agency," then an agency relationship exists. The legal concept applies and the label attaches regardless of whether the parties had the legal concept in mind and regardless of whether the parties contemplated the consequences of having the label apply.

Sometimes when parties form a relationship, they expressly claim or disclaim the agency label. For instance, franchise agreements often include a statement to the effect that "this agreement does not create an agency relationship" or that "the franchisee is not for any purposes the agent of the franchisor." Courts do consider such statements when trying to determine just what relationship the parties actually established. However, the parties' self-selected label is never dispositive and is relevant only as a window on the underlying reality. For example, a disclaimer of agency status may help show that neither party consented to act on the other's behalf and subject to the other's control. However, if the actual relationship between two parties evidences the elements necessary to establish agency, then all the disclaimers in the world will not deflect the agency label. To paraphrase a former president of the United States, "You can hang a sign on a pig and call it a horse, but it's still a pig." 19

§1.4.5 Agency Consensual, but Not Necessarily Contractual; Gratuitous Agents

Agency is not a subcategory of contract law; not all consensual relationships belong to the law of contracts. Although agents and principals often superimpose contracts on their agency relationship, the agency relationship itself is not a contract.

Therefore, since the doctrine of consideration belongs exclusively to the law of contracts, an agency relationship can exist even though the principal provides no consideration to the agent. Agents who act without receiving any consideration are "gratuitous agents." In most respects, the rights and powers of gratuitous agents are identical to those of paid agents. The major exceptions concern the right of the parties to terminate the agency and the standard of care applicable to the agent.

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18 In a franchise agreement, one business ("the franchisor") authorizes another business ("the franchisee") to use the franchisor's name and trademark and to sell either a product produced by the franchisor or an array of services developed by the franchisor. In return, the franchisee typically pays an initial franchise fee plus an ongoing royalty, commission, or service fee. Franchise agreements typically obligate franchisees to operate their business in compliance with requirements set by the franchisor. These requirements can be quite detailed and comprehensive.

19 "Bush Assails 'Quota Bill' at West Point Graduation," N.Y. Times, June 2, 1991, at A32 (George Bush objecting to certain aspects of the 1991 Civil Rights bill) ("You can't put a sign on a pig and say it's a horse.").

20 See sections 1.3, 4.1.6, and 4.3.3.

21 See section 5.2.3.

22 See section 4.1.4.
§1.4.6 Formalities Not Ordinarily Necessary to Create an Agency

An agency relationship can exist even though the parties never express their reciprocal consents in any formal fashion. Ordinarily, the parties' consent need not be in writing. Indeed, as section 1.4.3 indicates, conduct alone can suffice; in the proper circumstances, words are not necessary.

However, in some jurisdictions the "equal dignities" rule applies. The rule: (i) is statutory; (ii) pertains to transactions that must be in writing in order to be enforceable; and (iii) provides that an agent can bind a principal to such transactions only if the agency relationship is documented in a writing signed by the principal. For example, California Civil Code section 2309 states: "An oral authorization is sufficient for any purpose, except that an authority to enter into a contract required by law to be in writing can only be given by an instrument in writing."

§1.4.7 Consent and Control

To create an agency, the reciprocal consents of principal and agent must include an understanding that the principal is in control of the relationship. "Since the whole purpose of the relation of agency is that the agent shall carry out the will of the principal," agency cannot exist unless the "acting for" party (the agent) consents to be subject to the will of the "acted for" party (the principal). The control need not be total or continuous and need not extend to the way the agent physically performs, but there must be some sense that the principal is "in charge." At minimum, the principal must have the right to control the goal of the relationship.

Often the manifestations creating a relationship do not expressly address the issue of control. If the issue is in question, courts will examine how the relationship actually operated in order to decide whether the "acting for" party consented to be controlled. The facts of the relationship may imply or negate consent.

Case in Point—Krom v. Sharp and Dohme, Inc.: A hospital patient caught hepatitis from contaminated blood and sought to sue the blood supplier for breach of warranty. To succeed, the patient had to show that he was in privity with the blood supplier, but it appeared that the hospital, not the patient, had made the purchase from the supplier. The patient claimed he was nonetheless in privity, asserting that the hospital was acting as his agent when it obtained the blood. The court rejected the patient's claim, noting that there was no indication that the hospital was in any way subject to the patient's control.

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23 R.2d, Chapter 5, topic 1, Introductory Note.
24 If the control characteristic is lacking, the relationship cannot be a true agency. See Chapter 6, and especially sections 6.1.2, 6.2, and 6.3.2.
While "consent to control" is an element necessary to establish an agency relationship, issues of control also play a major role in at least three other parts of agency law. It is important to keep all four roles distinct from each other. The other three roles are:

1. **Control as an element of "servant"/"employee" status.** Whether the principal has a right to control the physical performance of the agent's tasks determines whether the agent is a "servant" or "employee." As discussed in Chapter Three, this issue is crucial to determining the principal's vicarious liability for certain torts committed by the agent.

2. **Control as a consequence.** As a consequence of agency status (rather than as an element necessary to create that status), the principal has the power to control the agent. Even though the agent may have consented to give the principal only limited control, once the agency relationship comes into existence, the principal has the power (though not necessarily the right) to control every detail of the agent's performance.

3. **Control as a substitute method for establishing agency status.** When a creditor exercises extensive control over the operations of its debtor, that control can by itself establish an agency relationship. The law treats the debtor as the agent and the creditor as the principal. As a consequence, the creditor becomes liable for the debtor's debts to other creditors.

### §1.4.8 Consent to Serve the Principal's Interests

To create an agency relationship the agent must manifest consent to act for the principal; that is, the agent must manifest a recognition that serving the principal's interests is the primary purpose of the relationship. The facts of the relationship can and often do imply that recognition.

**Example:** A law student, rushing to prepare for graduation and the fabulous buffet party to follow, gives a friend a list of last-minute additions to the menu and asks the friend to "do me a favor and make sure the caterer includes these on the buffet." The friend agrees. The friend has impliedly recognized that the endeavor's primary purpose is to meet the law student's needs, not to serve any separate agenda the friend may have.

### §1.4.9 All Elements Necessary

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26 "Servant" is R.2d terminology and found extensively in the case law. "Employee" is R.3d terminology.

27 An understanding between the principal and the agent may limit the principal's right to exercise control. If a principal violates that understanding when exercising the power of control, the agent may sue for damages and may also terminate the agency relationship. See sections 4.1.3 and 4.1.6.

28 See section 6.3 for an extensive discussion.
Each element discussed above must be present for an agency to exist. For example, although a construction company's foreman may exercise detailed control over a work crew, the crew members are not the foreman's agents. They have consented to work on behalf of the construction company, not the foreman.\footnote{R.3d, §1.01, comment g. The foreman and crew are "co-agents" of the construction company. R.3d, §1.04(1). The foreman is a superior agent and the crew members are each subordinate agents. \textit{Id.}, §1.04(9).} A physician provides her expertise for the benefit of her patient but has not consented to act on the patient's behalf or subject to the patient's control. A trustee acts on behalf of the trust beneficiary but is not subject to their control. Section 1.3.2 and Chapter 6 explain in more detail how to distinguish agency from other relationships.

\section*{§1.5 THE RELATIONSHIP BETWEEN AGENCY AND CONTRACT}

\subsection*{§1.5.1 Contract as an Overlay to an Agency Relationship}

Although agency itself is not a contractual relationship, the parties to an agency can make contracts regarding their agency relationship. To take the most common example, the parties can agree that the principal will pay the agent for the agent's services. For further example, the parties can by agreement set a definite term to the relationship or limit the principal's right to control the agent with regard to matters connected with the agency.

\textit{Example:} A manufacturing company plans to build a large plant and retains a "construction management" firm to manage the project on behalf of the manufacturing company. The contract between the manufacturing company and the construction management firm states: "Using reasonable care, FIRM will select the various contractors to build the plant, who shall then perform their work under contracts with COMPANY."

Contracts between agent and principal have limited impact. They can change the rights and duties that exist between agent and principal, but they cannot abrogate the powers that agency status confers on each party to the relationship. Thus, for example, despite any contract provisions to the contrary:

- the principal always has the power to control every detail of the agent's performance\footnote{See sections 4.1.3 and 4.1.6.}
- the agent may have certain powers to bind the principal\footnote{For example, if the principal allows the agent to run the principal's business and to appear as the owner, the agent has the power to bind the principal through "transactions usual in such businesses...although..."}
• both the principal and the agent have the power to end the agency at any time.32

When an agent or principal exercises a power in breach of the other's contract right, the injured party can bring an action for damages. But the exercise of power cannot be undone or enjoined.

§1.5.2 Distinguishing an Agency from a Mere Contractual Relationship

One of the most difficult lines for students (and sometimes lawyers) to draw is between an agent and an "independent contractor"; that is, a person who provides services simply as a party to a contract. "In any relationship created by contract, the parties contemplate a benefit to be realized through the other party's performance. Performing a duty created by contract may well benefit the other party, but the performance is that of an agent only if the elements of agency are present." 33

Example: Preparing for a daylong "callback" interview, a law student takes her "power suit" to the dry cleaner. For a fee, the dry cleaner provides a valuable service to the student, which benefits her. In ordinary parlance, the dry cleaner might be seen as cleaning the suit "on the student's behalf." ("Hey Charley. Who is this suit for?" "We're doing that one for Sarafina Student.") In agency law terms, however, the relationship is merely contractual. Reciprocal performance causes each party to benefit. However, in the language of R.3d, §1.01, neither party has consented to act "on the [other's] behalf and subject to the [other's] control."

Example: A manufacturing company enters into a contract with a distributor, under which the distributor agrees to purchase a specified quantity of goods, conduct its marketing and sales efforts within specified requirements, and limit its sales to a specified territory. The contract permits either party to terminate the arrangement on 60 days notice, but, as a practical matter, the distributor needs the manufacturer's goods far more than the manufacturer needs the distributor's efforts. Also as a practical matter, the manufacturer may be able to exercise significant control over the distributor beyond the terms of the contract. Moreover, executives of the manufacturing company often refer to the distributor (and other companies like the distributor) as "crucial links in our distribution network." The relationship is not an agency. The distributor has contrary to the directions of the principal." R.2d, §195. For further discussion, see section 2.6.2. See also section 2.3 (apparent authority).

32 See section 5.1.1.
33 R.3d, §1.01, comment g.
"manifested assent" to the contract, not to "the principal's control." R.3d, §1.01. Although practically the manufacturer may be "in the driver's seat," formally—according to the parties' manifestation to each other—there is no driver's seat. Or rather, each party is driving its own separate, self-interested car.

§§1.6 INTERACTION BETWEEN STATUTES AND THE COMMON LAW OF AGENCY

Although agency is a common law rubric, there is considerable interplay between statutory law and agency law. Statutes now govern key issues formerly left to the common law, and labels and principles from agency law inform both the drafting and interpretation of statutes.34

For example, one of the most important functions of agency law is to determine when information possessed by an agent is attributed to the principal.35 However, a statutory rule may well displace the common law if the principal is an organization and the transaction at issue is subject to the Uniform Commercial Code or a business entity statute.36

Statutes have also displaced much of the common law applicable to employment relations. The National Labor Relations Act (governing unionization) is perhaps the predominant example. In addition:

Employment legislation has modified common-law doctrine concerning the fellow-servant rule,37 under which an employer is not liable for injuries inflicted on one employee by the negligent acts of another, unless the act violates an employer's nondelegable duties. Employment legislation such as Title VII expands an employer's nondelegable duties substantially, subjecting the employer under some circumstances to liability for employee conduct, such as sexually harassing behavior, that usually falls outside the scope of the common-law doctrine of respondeat

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34 "Modern common law [agency] doctrines operate in the context of statutes," and statutes, both as drafted by legislatures and interpreted by courts, "incorporate definitions or doctrines that are drawn from the common law." R.3d, Introduction (2006).

35 See section 2.4.

36 See, e.g., Revised Uniform Partnership Act (1997), §102(e) (stating rules as to when "a person other than an individual knows, has notice, or receives a notification of a fact"), Uniform Limited Partnership Act (2001), §103(g) (same) and UCC §1-201(27) (stating rules for "[n]otice, knowledge or a notice or notification received by an organization"). But see Revised Uniform Limited Liability Company Act, §103, comment (stating that, in contrast to "previous uniform acts pertaining to business organizations...[f]or the most part, this Act relies instead on generally applicable principles of agency law).

37 Discussed briefly in section 4.3.2.
superior. Workers’ compensation legislation likewise imposes liability on the employer in circumstances under which the common law did not.\textsuperscript{38}

The interplay works in the opposite direction as well, as agency concepts make their way into statutory formulations. The "servant" construct has been especially influential,\textsuperscript{39} setting the scope for a wide range of statutes designed to regulate or tax the modern employment relationship. For example, the U.S. Supreme Court has held that:

Where Congress uses terms that have accumulated settled meaning under the common law, a court must infer, unless the statute otherwise dictates, that Congress means to incorporate the established meaning of these terms….In the past, when Congress has used the term 'employee' without defining it, we have concluded that Congress intended to describe the conventional master-servant relationship as understood by common-law agency doctrine.\textsuperscript{40}

For purposes of federal employment law, this approach "means in essence that the term 'employee' is to be looked up in the dictionary of the common law."\textsuperscript{41}

The interplay between common law and statute can produce confusing results, particularly when a statute uses a label taken from agency law but attaches consequences that are at odds with basic agency law principles. For example, under the common law of agency, an agent always has the power, if not necessarily the right, to terminate the agency.\textsuperscript{42} To exercise this power, an agent must communicate with the principal.\textsuperscript{43} Yet several modern business law statutes refer to "an agent for service of process" while stating that the agent's resignation is effective only 31 days after the agent communicates with a specified public official.\textsuperscript{44}

\textbf{§§1.7 MAJOR ISSUES IN THE LAW OF AGENCY}

By way of an overview, the major issues in the law of agency can be organized according to the relationship among agency's three players: principals, agents, and third parties.

\textbf{§1.7.1 Between the Principal and the Agent}

\begin{itemize}
\item \textsuperscript{38} R.3d, Introduction.
\item \textsuperscript{39} Discussed in detail in section 3.2.2.
\item \textsuperscript{40} Nationwide Mut. Ins. Co. v. Darden, 503 U.S. 318, 322-323 (1992).
\item \textsuperscript{42} See section 5.1.1.
\item \textsuperscript{43} See section 5.1.1.
\item \textsuperscript{44} ULLCA §110 (1996); ULPA (2001) §116; Re-ULLCA §115 (2006).
\end{itemize}
Under What Circumstances Does an Agency Relationship Exist?

As the R.2d explains, "Agency is a legal concept which depends upon the existence of required factual elements." Agency law is therefore fundamentally concerned with whether particular kinds of relationships qualify as agency relationships. For example, must both parties subjectively consent to the relationship? Must they intend to create the legal relationship? Must they even be aware that they are creating the legal relationship? Must the agent be promised contract-like consideration by the principal?

What Duties Does the Agent Owe the Principal?

The principal relies on the agent to accomplish tasks. How perfect must the agent's performance be? In dealing with the principal, may the agent follow the rules for "arm's-length" transactions, such as might apply to the parties to an ordinary contract? In carrying out the tasks of the agency, must the agent think only of the principal's interests, or may the agent consider its own interests as well?

What Duties Does the Principal Owe the Agent?

Must the principal compensate the agent for the agent's efforts? Must the principal alert the agent to risks involved in the agent's task? If the agent somehow gets into trouble, must the principal help out (or even bail out) the agent?

§1.7.2 Between the Principal and Third Parties

If a Third Party Has Made a Commitment or Received a Promise in Dealing with an Agent, Under What Circumstances Can the Principal or Third Party Enforce the Commitment or Promise?

People and organizations use agents to get things done, and often the agent's task involves making arrangements with third parties on the principal's behalf. For example, you might use a friend to make last-minute arrangements with the caterer you have hired for your graduation party. A bank might use its tellers to accept deposits from customers and give in return a paper evidencing the bank's resulting indebtedness (i.e., a deposit slip).

When an agency relationship involves this "arrangement making" function, it is essential that the principal be able to enforce commitments that are made by third parties to the agent. Otherwise, the agent could not accomplish much for the principal. The ability to bind third parties to the principal is thus an essential aspect of the agent's role, and questions about that aspect are therefore very important in the law of agency.

Likewise, when an agency relationship involves the "arrangement making" function, it is essential that third parties be able to enforce against the principal.

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[FN] R.2d, §1, comment b.
[46] See section 1.2.
[48] See section 4.3.
[49] Chapter 2 deals with such questions.
commitments made by the agent. Otherwise agents could not accomplish much for principals; third parties would generally insist on "dealing direct." The ability to bind the principal to third parties is thus an essential aspect of the agent's role, and questions about that aspect are therefore very important in the law of agency.\(^{50}\)

**If the Agent Possesses Certain Information, Under What Circumstances Will the Law Treat the Principal as if the Principal Possessed that Information?**

In many situations the law cares whether and when a party has particular kinds of information. Since principals often act through agents, the law of agency must decide when to hold the principal responsible for information possessed by the agent.

For example, Sam sells Blackacre to Rachael, innocently assuring her that Blackacre contains no toxic waste. Sam uses an agent to consummate the sale, and Sam's agent knows that a former owner of Blackacre buried loads of noxious chemicals on the land. The agent does not disclose this information to either Sam or Rachael. In Rachael's subsequent fraud suit against Sam, will the law attribute to Sam the knowledge possessed by his agent?\(^{51}\)

**If the Agent Conveys Certain Information, Under What Circumstances Will the Law Treat the Principal as if the Principal Had Conveyed that Information?**

In many situations the law cares whether and when a party communicates particular kinds of information. As with information possessed by an agent, the law of agency must decide when to hold the principal responsible for information conveyed by the agent.

For example, Sam uses an agent to sell Blackacre to Rachael. Without Sam's knowledge or consent the agent tells Rachael that Blackacre contains a lake "full of delicious trout." In fact, the lake contains nothing larger than minnows and the agent knows it. Will the law attribute the agent's statement to Sam?\(^{52}\)

**If an Agent's Acts or Omissions Cause Tort Injuries to a Third Party, Under What Circumstances Can the Third Party Proceed Directly Against the Principal?**

When an agent commits a tort, the injured party can of course proceed against the agent. The third party may, however, wish to pursue the principal. (For instance, the principal may have a deeper pocket or may make a less sympathetic defendant.) The law of agency must therefore determine under what circumstances a principal is liable for the tortious acts of its agent. For example, suppose the law student's friend, rushing to make last-minute arrangements with the caterer, drives negligently and runs over a dog. May the dog's owner recover damages from the law student? Or suppose a newscaster defames an innocent person. May the person sue the broadcast company?\(^{53}\)

**§1.7.3 Between the Agent and Third Parties**

\(^{50}\) Chapter 2 also deals with such questions.

\(^{51}\) See section 2.4.4.

\(^{52}\) See section 2.4.6. See also section 3.4.2 (misrepresentation by an agent).

\(^{53}\) For a discussion of these questions, see Chapter 3.
When an Agent Arranges a Commitment Between the Principal and a Third Party, Under What Circumstances May the Third Party Hold the Agent Responsible for the Commitment?

This question is of great importance to both the agent and the third party. From the agent's perspective, the risks differ greatly as between merely arranging a contract for the principal and being personally liable for that contract's performance. From the perspective of the third party, it may well have been the reputation of the agent, not the principal, that induced the third party to make the commitment in the first place.\(^5^\)

\(^5^\) See section 4.2.
CHAPTER 2

Binding Principals to Third Parties
(and Vice Versa)
in Contract and Through Information

§2.1 "BINDING THE PRINCIPAL"

§2.1.1 The Importance and Meaning of "Binding the Principal"

Perhaps the most important consequence of the agency label is the agent's power to bind the principal to third parties and to bind third parties to the principal. R.2d defines "power" as "the ability . . . to produce a change in a given legal relation (between the principal and third parties) by doing or not doing a given act."1 and, as explained previously, an agent's power to bind is central to an agent's ability to accomplish tasks on the principal's behalf.2

The concept of agency power is essentially a concept of attribution (sometimes called "imputation"). To the extent an agent has the power to bind (according to the several specific attribution rules discussed below), the agent's conduct is attributed to the principal. In the words of a venerable agency law maxim, qui facit per alium facit per se3 Thus, when a third party asserts that an agent's act or omission has "bound the principal," the third party wants the principal treated legally as if the principal itself had acted or failed to act.

Although the attribution rules differ depending on whether the underlying matter sounds in contract, sounds in tort, or concerns the possession or communication of information, the concept of attribution is ubiquitous.

Example: An applicant to a law school is delighted to receive a letter, signed by the director of admissions, stating, "We are pleased to offer you a place in the incoming class." The statement making the offer is legally attributable to the law school, even though the law school (a juridic

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1R.2d, §6. R.3d does not include this general definition, but does use similar language in defining "power given as security." R.3d, §1.04(6).
2 See section 1.5.2.
3 This maxim translates as "who acts through another acts himself." Black's Law Dictionary 1249 (1990).
person distinct from its director of admissions) never made the statement nor signed the letter.

<EXT>Example: A company's delivery van crashes into a parked car. The accident results from the van driver's negligence, but the car owner seeks damages from the company. The car owner's legal theory attempts to impute to the company the negligence of the company's driver.

<EXT>Example: A discount warehouse in Iowa contracts with a railroad to transport 150 tractors from Newark, New Jersey, to the railroad's terminal in Iowa City. The contract between the warehouse and the railroad specifies that the warehouse must pick up the tractors "within three days after receiving notice of their arrival at the Iowa City terminal, and WAREHOUSE shall pay storage fees at a rate of $500 per day for any delay in pick up." The railroad gives notice of arrival by telephoning the loading dock at the warehouse after normal business hours and speaking to a janitor. The janitor fails to inform the warehouse, the warehouse fails to make a timely pick up, and the railroad claims storage fees. In assessing the storage fees, the railroad wants the warehouse treated as if the warehouse itself had received the notice.

<EXT>Example: Sam sells Blackacre to Rachael, innocently assuring her that Blackacre contains no toxic waste. Sam uses an agent to consummate the sale (sign the closing documents, etc.), and that person knows that a former owner of Blackacre buried loads of noxious chemicals on the land. Sam's agent does not disclose this information either to Sam or to Rachael. In Rachael's subsequent suit to rescind the purchase, Rachael wants Sam treated as if he directly possessed and suppressed the information about the noxious chemicals.

<EXT>Case in Point—State v. Dalseg: “In this consolidated appeal, Jeff Dalseg and Timothy Cestnik challenge the trial court's decision to deny them credit for time served in the Nisqually Tribal Jail 'work release' program. After the men had served more than 11 months of a 12-month work release sentence in the Nisqually program, the State learned that the program did not comply with the statutory requirements for work release and asked the court to order Dalseg and Cestnik to begin serving their sentences in one that did. The trial court agreed, denying the men credit for any time served. We reverse and remand, holding that Dalseg and Cestnik are entitled to day-for-day credit for time served in the Nisqually 'work release' program under the equitable doctrine of credit for time served at liberty. . . . The trial court erred when it denied equitable relief on the ground that 'the Nisquallies' were at fault ‘for running them into the
wrong program.' Dalseg's and Cestnik's judgment and sentences specifically authorize them to serve their sentences in the Nisqually Tribal Jail work release program. This specific authorization cloaked the Nisqually Tribal Jail officials with apparent authority to execute the sentences. Thus, the Nisqually corrections officers acted on behalf of the State when they enrolled Dalseg and Cestnik in a day reporting program rather than a statutorily-compliant work release program. The error made by Nisqually corrections officers in interpreting and executing the judgment and sentences is attributable to the State.

Attribution can also work in favor of the principal, as when a person seeks to hold a third party to a contract entered into by an agent or to information received or communicated by an agent.

Example: An art dealer's employee attends an auction on the dealer's behalf and makes the winning bid on a painting. Later, the dealer tenders payment and seeks to compel the auction house to deliver the painting. The dealer seeks to be treated as if it itself had made the winning bid.

Example: A residential lease allows either party to terminate on 60 days' notice. The landlord's resident manager gives the proper 60-day notice to a tenant, but the tenant fails to vacate the apartment. In the subsequent eviction action, the landlord wishes to be treated as if it itself had given the requisite notice.

§2.1.2 "Binding the Principal" and Questions of Agency Power

Agency law uses its concept of power to analyze "binding the principal" questions. The question of "Under the law of agency, did X's act or omission bind Y?" thus becomes "Under the law of agency, did X have the power to bind Y through that act or omission?" Agency law approaches questions of power through five attribution rules. An agent can have the power to bind a principal through:

1. actual authority (including express and implied actual authority),
2. apparent authority,
3. estoppel,
4. inherent power, and
5. ratification.

5 Inherent power is actually a collection of attribution rules, or a rule with several different facets. See section 2.6. R.3d excludes from its "black letter" the concept of inherent power, relying instead on concepts of apparent authority, estoppel, and restitution. R.3d, Chapter 2, Introductory Note.

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More than one subcategory of agency power may apply in any particular situation. Indeed, in practice parties often argue attribution rules in the alternative. For example:

- **When** X made this contract on behalf of Y, X had actual authority to do so. Y is therefore bound.
- And, even if X lacked actual authority, X had apparent authority and so Y is bound.
- **And, even if X lacked both actual and apparent authority, X had the inherent power to bind Y, and so Y is bound.**
- And, even if X lacked both the authority and power to bind Y, estoppel applies and so Y is bound.
- And, even if X lacked both the authority and power to bind Y and estoppel does not apply, Y subsequently ratified X's act and so Y is bound.

This chapter discusses how each of the five attribution rules pertains to binding a principal in contract and also considers how, in contractual and similar matters, a principal can be bound by information that an agent or apparent agent receives, knows, ought to know, or communicates.⁶

**§2.1.3 Attribution (Imputation): Transaction Specific and Time Sensitive**

Attribution (also called "imputation") is always transaction specific. For instance, the attribution question is not whether "A had apparent authority to bind P," but rather whether "A had apparent authority to bind P when A did X."

Because attribution is transaction specific, attribution is also time sensitive. With the exception of ratification,⁷ all attribution rules are applied exclusively as of the time that relevant transaction occurred.

**Example:** T claims that P is bound to a contract formed last Friday at 3 P.M., when T and A made certain reciprocal manifestations. The attribution analysis focuses on whether last Friday at 3 P.M. A had the power to bind P to the contract through those manifestations.

**Example:** T rents an apartment from P on a month-to-month lease. T claims to have given notice of termination to A on the last day of last

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⁶Chapter 3 considers the attribution rules relevant to tort claims. In that context, the most important attribution rule is *respondeat superior*, an aspect of inherent power. Apparent authority can be relevant for some types of torts, either instead of or in addition to *respondeat superior*.

⁷Ratification occurs when a principal affirms a previously unauthorized act, and, consequently, ratification analysis has a dual temporal focus: the moment at which the unauthorized act occurs and the moment at which the principal affirms. Section 2.7 discusses ratification in detail.
month and further claims that the notice is effective against P. The attribution analysis focuses on whether on the last day of last month A had the power to bind P by receiving notices related to the lease.

§2.1.4 Distinguishing the Power to Bind from the Right to Bind

As will be discussed throughout this chapter and the next, various circumstances can empower an agent to bind the principal. An agent has the right to bind the principal only to the extent that the principal has authorized the agent to do so. A principal gives this authorization in the same way (and often at the same time) that the principal initiates the agency relationship—namely, by making a manifestation that reaches the agent.8

To the extent an agent has the right to bind a principal, the agent automatically has the power to do so. It is possible, however, for an agent to have the power to bind while lacking the right. In such circumstances, if the agent exercises the power and binds the principal, the agent wrongs the principal. Then, consistent with the right/power distinction:

- the agent is liable to the principal for the wrongful conduct, but
- the principal is nonetheless bound to the third party.

Example: Rachael, the owner of Rachael's Service Station, promotes Sam to the position of general manager and puts him in charge of the station's day-to-day operations. Although service station managers ordinarily place orders for batteries, tires, and other accessories, Rachael instructs Sam to leave that ordering to her. Nonetheless, Sam orders batteries. Under the doctrines of apparent authority and inherent agency power,9 Rachael is bound, even though Sam had no right (vis-à-vis Rachael, his principal) to place the order.

For a graphic illustration of the relationship between the right to bind and the power to bind, see Figure 2-1.

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8 R.2d, R.3d and the case law call this authorized power "actual authority." For a detailed discussion of actual authority, see section 2.2.

9 See sections 2.3 and 2.6.2. R.3d would treat this situation as involving only apparent authority.
§2.2 ACTUAL AUTHORITY

§2.2.1 The Interface Function and the Agent's Authorized Power to Bind (Actual Authority)

For an agency relationship to come into existence, the principal must manifest consent to have the agent act on the principal's behalf with respect to some goal, task, or set of responsibilities. In many instances, the authorized zone of endeavor involves some "interface" function; that is, some tasks or responsibilities through which the agent connects the principal with third parties.

Example: Rachael hires Sam, an attorney, to represent her as vendee in a real estate closing. Part of Sam's function is to serve as Rachael's interface with the title insurance company, Rachael's lender, the vendor (through the vendor's attorney, if the vendor has an attorney), the vendor's real estate agent, the "closer," etc.

Example: Ofek is hired as a cashier at UpscaleandPricey Jeans, Inc. Her core function is to be the company's interface with its customer at the crucial moment of sale.

This interface function is ubiquitous in, but not essential to, agency relationships.
Example: A Christmas tree farm hires Al to tend and eventually harvest acres of pine trees. Al's ordinary, authorized responsibilities do not include any contact with customers, vendors, or the public.

Where agency involves an interface function, the principal's manifestation to the agent necessarily creates "actual authority" in the agent. Actual authority means an agent's authorized (rightful) power to act on behalf of the principal vis à vis third parties. Authorized acts can include the negotiation and making of agreements, and also the receipt, possession, and communication of information.

This section considers the power-to-bind ramifications of actual authority. Chapter 4 considers the ramifications for the obligations between principal and agent.

§2.2.2 Creation of Actual Authority

Essential Mechanics (Elements) Paralleling the creation of the agency relationship itself, creation of actual authority involves:

- an objective manifestation by the principal
- followed by the agent's reasonable interpretation of that manifestation,
- which leads the agent to believe that it is authorized to act for the principal.

"This standard requires that the agent's belief be reasonable, an objective standard, and that the agent actually hold the belief, a subjective standard." 11

Example: Two traveling salespeople, Bernice and Joe, are in the hotel bar. As Joe gets up to get another bowl of pretzels, Bernice says, "It's Happy Hour. While you're up, order another round of drinks for us and charge them to me." Joe orders the round and charges the price to Bernice's room. In doing so, Joe has acted within his actual authority. Bernice's statement constituted the necessary manifestation and Joe's action reflects his interpretation of that manifestation. In the circumstances, Joe's interpretation is certainly reasonable.

Example: Same situation as above, except that when Joe gets to the bar he discovers that Happy Hour has ended and that prices have returned to the regular, undiscounted rate. From the bar he conveys that information back to Bernice, who responds by waving her hand in a forward motion. When Joe charges the drinks to Bernice's room, he is

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10As explained by the R.3d., §1.01, comment c, "An agent who has actual authority holds power as a result of a voluntary conferral by the principal and is privileged, in relation to the principal, to exercise that power." Some cases refer to actual authority as "true authority."

11R.3d, §2.02, comment e. See also R.2d, § 33 (“An agent is authorized to do, and to do only, what it is reasonable for him to infer that the principal desires him to do in the light of the principal's manifestations and the facts as he [i.e., the agent] knows or should know them at the time he acts”).
acting within his actual authority. Given Bernice's specific reference to Happy Hour, it would initially have been unreasonable for Joe to charge the drinks at the regular rate. However, after checking with Bernice, he received a fresh and different manifestation.

<EXT>Restatement on Point—R.3d, §2.02, Ill. 4: “P, a photographer, employs A as a business manager. P authorizes A to endorse and deposit checks P receives from publishers of photographs taken by P. Based on P's statements to A, A believes A's authority is limited to endorsing and depositing checks and does not include entering into agreements that bind P in other respects. A endorses and deposits a check from T, a magazine publisher, made payable to P. Printed on the back of the check is a legend: ‘Endorsement constitutes a release of all claims.’ It is beyond the scope of A's actual authority to release claims that P has against T.” The result would be the same even if A could reasonably have believed that he or she was authorized to endorse the check. Actual authority requires A’s actual as well as reasonable belief.

<H5>Scope of Authority

Agency law uses the term "scope of authority" to refer to and delineate the extent of an agent's actual authority.

<H5>Modes of Communicating the Principal's Manifestation

The principal's manifestation can reach the agent directly or indirectly, and a manifestation that reaches the agent through intermediaries can certainly give rise to actual authority. Indeed, when the principal is an organization (e.g., a corporation, a limited liability company), an agent normally receives communication "from" the principal via the conduct of co-agents.

<EXT>Example: The board of directors of Scrooge, Inc. ("Scrooge") adopts a resolution allowing a 10 percent Christmas discount for any tenant who pays the January rent before December 25. The secretary to the board writes and distributes throughout the organization a memo based on the resolution. In due course, Robert Cratchit, chief rent clerk for Scrooge in the London area, receives a copy of the memo. He then has actual authority to accept 10 percent discounted rent as full payment for January obligations.

<H5>Manifestation through Inaction

In some circumstances, the principal's manifestation can consist of inaction. When silence, reasonably interpreted, indicates consent, a principal's silence can "speak [or manifest] volumes." For example, when an agent takes particular action, the action comes to attention of the principal, and the principal makes no objection, the agent may well have actual authority to repeat the action in similar circumstances.
Example: For years, the mechanics at Rachael's Service Station have, on an ad hoc basis, offered a 10 percent discount to regular customers on major service jobs. Rachael, the owner, never explicitly authorized the practice, but she has been aware of it and has not previously objected to it. As a result of Rachael's silent acquiescence, the mechanics have actual authority to offer the discount. The acquiescence satisfies the "manifestation" requirement.

Assessing the Reasonableness of the Agent's Belief

Agency law determines the reasonableness of the agent's interpretation by considering the same types of information that figure into determinations of reasonableness in other areas of law. In the words of the R.2d: "All other matters throwing light upon what a reasonable person in the position of the agent at the time of acting would consider are to be given due weight." \(^{12}\) In the words of the R.3d: "An agent's understanding of the principal's objectives is reasonable if it accords with the principal's manifestations and the inferences that a reasonable person in the agent's position would draw from the circumstances creating the agency." \(^{13}\)

The Restatements' references to "reasonable person" reflect an objective standard. In determining the scope of an agent's actual authority, what matters is the principal's objective manifestation and the agent's reasonable interpretation of that manifestation. Any unexpressed, subjective intent of the principal is irrelevant. \(^{14}\)

Fiduciary Duty and the Reasonableness of the Agent's Interpretation

The R.3d makes an interesting connection between the agent's fiduciary duty and the reasonableness of the agent's interpretation. To be reasonable, an agent's interpretation must be made "in light of the context," which includes "the agent's

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\(^{12}\) R.2d, §34, comment a. The text of §34 provides the following nonexhaustive list of factors that figure into determining the reasonableness of the agent's interpretation:

(a) the situation of the parties, their relations to one another, and the business in which they are engaged;
(b) the general usages of business, the usages of trades or employments of the kind to which the authorization [i.e., the principal's manifestation] relates, and the business methods of the principal;
(c) facts of which the agent has notice respecting the objects which the principal desires to accomplish;
(d) the nature of the subject matter, the circumstances under which the act is to be performed and the legality or illegality of the act; and
(e) the formality or informality, and the care, or lack of it, with which an instrument evidencing the authority is drawn.

\(^{13}\) R.3d, §2.02(3).

\(^{14}\) See section 1.4.3.
An agent's fiduciary position requires the agent to interpret the principal's statement of authority, as well as any interim instructions received from the principal, in a reasonable manner to further purposes of the principal that the agent knows or should know, in light of facts that the agent knows or should know at the time of acting. An agent thus is not free to exploit gaps or arguable ambiguities in the principal's instructions to further the agent's self-interest, or the interest of another, when the agent's interpretation does not serve the principal's purposes or interests known to the agent. This rule for interpretation by agents facilitates and simplifies principals' exercise of the right of control because a principal, in granting authority or issuing instructions to an agent, does not bear the risk that the agent will exploit gaps or ambiguities in the principal's instructions. In the absence of the fiduciary benchmark, the principal would be at greater risk in granting authority and stating instructions in a form that gives an agent discretion in determining how to fulfill the principal's direction.

**Principal's Control of Agent's Interpretation**

A principal can protect against ambiguity by being careful to give clear and specific instructions. Moreover, a principal can always cut back or countermand previously granted authority simply by making an appropriate manifestation and seeing that it reaches the agent. Except in extraordinary circumstances, the later manifestation "trumps" the earlier one. Once the agent knows that the principal wants to remove some or all of the agent's authority, the agent can no longer reasonably believe that it has the authority the principal wants to remove.

**Example:** Rachael, the owner of Rachael's Service Station, decides that she can no longer afford the 10 percent discount. She calls the mechanics together and says, "Effective right now, no more 10 percent discounts." The next day, one of the mechanics, momentarily forgetting Rachael's instruction, offers the discount to a customer. In doing so, the mechanic has acted without actual authority. After Rachael's instruction, the mechanic cannot reasonably believe himself authorized to give 10 percent discounts.

In some circumstances, the principal's countermanding manifestation can change the agent’s actual authority even before the agent learns of the manifestation. If the agent has reason to know of the new instructions, then almost by definition the agent's interpretation of the principal's prior manifestation are no longer reasonable.

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15 R.3d, §2.02(2).
16 R.3d, §1.01, comment e.
Example: Bligh dispatches Ahab to buy a load of whale blubber and ship it to New York City "ex Peerless." After Ahab has bought the blubber but before he has made the shipping contract, Bligh sends the following text message to Ahab: "doubts re Peerless in water use another ship." Text messages are a common means of communication between Bligh and Ahab. Unfortunately, Ahab has let his cell phone battery run down and does not retrieve Bligh's message until after the blubber is loaded on the Peerless. Even though Ahab did not actually know of the new instructions when he made the shipping contract for Bligh, Ahab had reason to know—that is, if had he acted reasonably and kept his cell phone in working condition he would have received Bligh's message. Therefore, Ahab's interpretation of his original instructions was no longer reasonable.

In cutting back or countermanding previously granted authority, the principal may be breaching a contract between the principal and agent.\textsuperscript{17} The principal may also be leaving intact the agent's inherent power to bind the principal or an enforceable appearance of authority, or both.\textsuperscript{18}

§2.2.3 Irrelevance of Third-Party Knowledge (Unidentified and Undisclosed Principals)

Typically, a third person dealing with an agent knows or has reason to know that the agent is acting as such and also knows or has reason to know who (or what) the principal is. In this situation, agency law characterizes the principal as "disclosed."\textsuperscript{19} However, the elements for creating actual authority involve the principal and the agent and have nothing to do with what third parties may or may not know.\textsuperscript{20} In determining the existence and extent of an agent's actual authority, the law focuses on the relationship between the principal and the agent (the \textit{inter se} relationship). An agent can thus have actual authority (and therefore power to bind the principal to third parties) even though at the time of the "binding" act or omission the principal is:

- \textit{unidentified} (i.e., the third party knows or has reason to know that the agent is acting for another, but not who that other is);\textsuperscript{21} or even
- totally \textit{undisclosed} (i.e., the third party neither knows nor has reason to know that the agent is acting as an agent and perforce cannot know the principal's identity).

\textsuperscript{17} See sections 1.3, 4.1.3, and 4.1.6.
\textsuperscript{18} See sections 2.6.2 (inherent power) and 2.3 (apparent authority).
\textsuperscript{19} R.3d, §1.04(2)(a) and R.2d, §4(1).
\textsuperscript{20} In contrast, the third party's view is pivotal to the existence of apparent authority. See section 2.3.5.
\textsuperscript{21} R.3d §1.04(2)(c). In the R.2d, the corresponding term is "partially disclosed," R.2d, §4(2), which, according to R.3d, §1.04, comment b, "misleadingly suggests that a portion of the principal's identity is known to the third party."
By definition, when the principal is undisclosed or unidentified, the third party can learn of the agent's actual authority only after the agent's exercise of that authority. Nonetheless, if the authority existed at the time of the transaction, the principal is bound.

Example: A power company authorizes a coal broker to buy coal for it. The broker contracts to buy the coal in its own name. When the seller later prepares to deliver the coal to the broker, the seller discovers that the broker has gone out of business. Then the seller discovers that the broker was making the purchase on the power company's behalf and had actual authority to do so. By asserting actual authority, the seller can hold the undisclosed principal (the power company) to the contract. Because actual authority is at issue, it is irrelevant that at the time of contracting the seller was ignorant of the agency relationship.

Example: An attorney contacts an art dealer and contracts to buy a famous Picasso print. The attorney explains that she is acting for a client, but declines to identify the client. (The client dislikes notoriety.) If the art dealer later learns the identity of the unidentified principal (the client) and can prove that the attorney acted with actual authority, then the art dealer can enforce the contract against the client.

§2.2.4 Actual Authority: Express and Implied

In addition to the authority expressly indicated by the principal's words and other conduct, an agent may also have implied actual authority. The concept is "black letter" in R.2d, but relegated to the comments in R.3d.

That change does not affect the way the concept operates in practice. R.2d, §35 states: "Unless otherwise agreed, authority to conduct a transaction includes authority to do acts which are incidental to it, usually accompany it, or are reasonably necessary to accomplish it." Sometimes the implication is based on custom or past dealings. Other times, "the principal's objectives and other facts known to the agent" cause an agent to infer that a particular act is authorized.

Comment b to R.2d, §35 states the very simple rationale for the concept of implied authority. "In most cases the principal does not think of, far less specifically direct, the series of acts necessary to accomplish his objects." Implied actual authority fills in the gaps.

Whether a principal is disclosed, partially disclosed, or undisclosed matters substantially as to the agent's liability on a contract. See section 4.2.1.

R.2d, §35; R.3d, Ch. 2, Introductory Note, and §2.01, comment b.

Comment b.

R.3d, §2.01, comment b.

R.3d, §2.02, Reporter's Notes to comment d ("Implied actual authority may also serve as a device to address gaps in the principal's explicit statement of authority.").
<EXT>**Example:** An insurance broker acted as local agent for an insurance company, with express authority to conduct business for the company in the locality. Although the insurance company had given no express instructions to the broker on how to handle cancellation notices received from policyholders, the broker had implied authority to receive such notices. Accordingly, notice to the broker was notice to the insurance company.

**Case in Point—Dweck v. Nasser:** “A minority stockholder, and former president, chief executive officer, and director of a closely held corporation seeks to enforce a settlement agreement terminating the litigation between herself and the defendant [Nasser], the majority stockholder. On November 19, 2007, [Shiboleth] a long-time attorney, business associate, and close personal friend of the defendant agreed to a settlement after protracted negotiations. . . . [Nasser subsequently refused to sign the settlement agreement, asserting that he had never authorized Shiboleth to settle the dispute without Nasser’s review of the settlement document. The court disagreed on several grounds, one of which was implied actual authority.] . . . Nasser directed Shiboleth to settle the action and permitted him to speak “in his name.” Moreover, he told Shiboleth that he would execute any agreement that Shiboleth and Heyman presented to him. Given this behavior and Shiboleth's long-standing close personal and business relationship with Nasser, it was reasonable for Shiboleth to assume he was authorized to settle the litigation. At his deposition, Shiboleth testified that he had settled many cases for Nasser in the past and that in those circumstances Nasser would instruct him to: ‘[D]o what you want. That means settle it in our implied terms. That's the way we communicate for twenty years. When he tells me to do what you understand or what you want, in terms of settling a case ... you are ... authorized to settle the case.’”

*The express manifestations of the principal can always negate implied authority.*

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Example: Sartre authorizes Camus to negotiate the sale of a plot of land owned by Sartre.\(^{27}\) In that locality, land sales are almost always done by warranty deed, a custom that would ordinarily give Camus implied actual authority to sign a warranty deed on Sartre’s behalf. However, Sartre tells Camus, “Existence is uncertain. Use a quit claim deed only.” Camus lacks actual authority to adhere to the local custom.

§2.2.5 Binding the Principal and Third Party in Contract via Actual Authority

If an agent acting with actual authority makes a contract on behalf of a principal, then the principal is bound to the contract as if the principal had directly entered into the contract. In almost all circumstances, the third party is likewise bound on the contract to the principal.

Example: Sam, a research scientist, instructs Irv, his lab manager, "Get me a maintenance contract on the electron microscope. Make sure that we have service 24/7/365. I don't care what it costs." Irv enters into a contract with Selma's Service Company, signing the contract, "Irv, as manager for Sam." Sam, the disclosed principal, is bound to the contract.

Example: Same situation, except that Irv signs the contract in his own name, without having made any reference to Sam. Sam, the undisclosed principal, is bound to the contract.

Example: Same situation, except that Irv enters into the contract through a phone conversation with Selma, explaining, "I'm making this agreement for the lab's owner." Sam, the unidentified/partially disclosed principal, is bound to the contract.

§2.2.6 Binding the Principal via Actual Authority: Special Rules for Contracts Involving Undisclosed Principals

When the principal is undisclosed, the third party is sometimes entitled to (i) insist on rendering performance to the agent, or (ii) escape the contract entirely.

Rendering Performance to the Agent

The third party may insist upon rendering performance to the agent if the contract requires the third party to perform

\(^{27}\) In some states, the “equal dignities rule” would require Sartre to put the authorization in a signed writing. See section 1.TBA.
personal services, or if in some other way rendering performance to the undisclosed principal would significantly change the third party's burden. This rule fits the expectations of the third party, who entered into the contract expecting to render performance to the agent, not the principal. Deviating from that expectation is fair only if the deviation does not significantly alter the third party's burdens.28

<H5>Escaping the Contract Entirely  <TEXT>In a narrow range of circumstances, a third party may escape entirely a contract made with an agent for an undisclosed principal. Escape is possible if either:

- <BL> the contract so provides; that is, the contract states that it is inoperative if the agent is representing someone; or
- a special (very difficult to establish) kind of fraud exists:
  - <BSL> the agent fraudulently represented that the agent was not acting for the principal;
  - the third party would not have entered into the contract knowing the principal was a party; and
  - the agent or undisclosed principal knew or should have known that the third party would not have made the contract with the principal.

<TEXT>Misrepresentation of the principal's role is insufficient without the other elements. Mere failure to disclose the principal's existence is always insufficient.

<EXT>Example: A guitar maker has a guitar for sale. A musician wishes to buy but knows that, due to a longstanding feud, the guitar maker will refuse to sell the guitar to him. The would-be buyer therefore asks a friend to make the purchase. The guitar maker says to the friend, "I care about the guitars I make. I want to be sure that they're treated with respect." The friend responds, "Don't worry. I've wanted one of your guitars for a long time. I am looking forward to playing this one for years to come. I'll take good care of it." The guitar maker agrees to a deal, but learns the truth before the friend takes possession of the guitar. The guitar maker is not obligated to go through with the sale. The agent affirmatively misrepresented the principal's role, that misrepresentation induced the seller to make the contract, and both the agent and the principal knew that the guitar maker would not have made a contract with the principal.

<FN>28 Agency law here closely parallels contract law. See Restatement (Second) Contracts, §317(2)(a) (stating that a party to a contract may not assign its rights when "the substitution of a right of the assignee for the right of the assignor would materially change the duty of the obligor, or materially increase the burden or risk imposed on him by his contract, or materially impair his chance of obtaining return performance, or materially reduce its value to him").
Example: A railroad company wishes to acquire three parcels of land for a new line. The company fears that the landowners will ask too much money if they learn that the railroad needs the land. It also fears the same result if the landowners are contacted by someone representing an unnamed principal. The company therefore uses three different "straw men." Each of these agents individually approaches one of the landowners. Each of the agents affirmatively states that he or she is acting on his or her own account. Each negotiates for and signs a land purchase contract in his or her own name. Later, before the purchases are closed, the landowners learn that the railroad is the actual purchaser and seek to avoid or renegotiate the deals.

The landowners are bound to the original deals. The agents did actively misrepresent the role of the undisclosed principal, but neither the agents nor their undisclosed principal had reason to know that the third parties would refuse to contract with the principal. To the contrary, both the agents and principal thought the third parties would be delighted to contract with the railroad—but at a substantially higher price.

§2.3 APPARENT AUTHORITY

§2.3.1 The Misnomer of "Apparent Authority"

"Apparent authority" is a misnomer. The term refers to the power to bind, not the right. The power derives from the appearance of legitimate authority; the doctrine exists to protect third parties who are misled by appearances.

§2.3.2 Creation of Apparent Authority

Mechanics

Apparent authority exists when:

- one party ("apparent principal") makes a manifestation, which somehow reaches a third party, and
- which alone or (more often) in the context of other circumstances causes the third party to reasonably believe that another party ("apparent agent") is indeed authorized to act for the apparent principal.

For a more extensive explanation of the doctrine's rationale, see section 2.3.7.
In the words of R.3d, §2.03: “Apparent authority is the power held by an agent or other actor to affect a principal's legal relations with third parties when a third party reasonably believes the actor has authority to act on behalf of the principal and that belief is traceable to the principal's manifestations.”

**Relationship to Actual Authority**

Apparent authority can coexist and be coextensive with actual authority.

*Example:* Two traveling salespeople, Bernice and Joe, are in the hotel bar. As Joe gets up to get another bowl of pretzels, Bernice says, "While you're up, order another round of drinks for us and charge them to me." Joe orders the round and charges the price to Bernice's room. If the bartender overheard Bernice's instructions, Joe had apparent as well as actual authority to charge the drinks.

Apparent authority can also extend an actual agent's power to bind the principal beyond the scope of the agent's actual authority.

*Example:* An Art Collector arranges for Broker to attend a forthcoming art auction and bid on certain items on Collector's behalf. Collector sends a letter to the Auction House, stating, "At your upcoming auction, Broker will represent me and is authorized to bid on my behalf." In the past Broker has often placed bids for Collector in excess of $50,000. This time Collector tells the Broker, "Don't bid more than $25,000 on any item." Collector does not, however, communicate this limit to the Auction House. Although the Broker's actual authority to bid is limited to $25,000 per item, the limit does not apply to the Broker's apparent authority.

Apparent authority can also exist where no actual agency exists.

*Example:* The Art Collector arranges for Broker to attend a forthcoming art auction and bid on certain items on the Collector's behalf. Collector sends a letter to the Auction House, stating, "At your upcoming auction, Broker will represent me and is authorized to bid on my behalf." Subsequently Collector changes his mind and instructs Broker not to bid for him. Collector neglects, however, to inform Auction House of this change. Although Broker has no actual authority to bind for Collector, Broker does have apparent authority.

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**FN** 30 R.2d, §27 is to the same effect: "Apparent authority to do an act is created as to a third person by written or spoken words or any other conduct of the principal which, reasonably interpreted, causes the third person to believe that the principal consents to have the act done on his behalf by the person purporting to act for him."
The Question of Reliance

When a third party seeks to bind an apparent principal by claiming apparent authority, must the claimant show detrimental reliance? The question is imprecise (as will be seen), and the answer is somewhat complex.

Under both the R.2d and R.3d, the claimant's inference of authority must be traceable to (and therefore, in some sense, rely on) the principal's manifestation. 31 (first occasion for reliance—Point 1—in the timeline shown in Figure 2-2).

Must there be further reliance? In particular, must a claimant show that the appearance of authority caused the claimant to act to the claimant's detriment? (second occasion for reliance—Point 2—in Figure 2-2). Neither Restatement has this requirement, but many jurisdictions do. Indeed, some opinions refer to apparent authority as *agency by estoppel*. 32

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**Figure 2-2. The Role of Reliance in Creating Apparent Authority**

The doctrinal difference may have little practical significance. If a false appearance of authority does not cause a third party to act or omit to act to its detriment, then a claim will rarely be worth pursuing.

**§2.3.3 The Necessary Peppercorn of Manifestation**

For apparent authority to exist, the third party must be able to point to at least some peppercorn of manifestation attributable to the apparent principal. This peppercorn must form the basis of the third party's reasonable belief that the apparent agent is actually authorized.

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31 R.3d, §2.03; R.2d §8, comment d. The word "traceable" does not appear in R.2d but is part of the black letter of R.3d.

32 The Restatements also contemplate agency by estoppel, but the Restatement concept of estoppel is subtly different from the doctrine of apparent authority. See section 2.5 (authority by estoppel).
The R.3d uses the phrase "traceable to the principal's manifestations" to express this requirement. The "traceable" requirement means that, with one rarely important exception (discussed below), the statements of the apparent agent cannot by themselves give rise to apparent authority.\(^{33}\)

**Example:** A silver-tongued salesman, nattily dressed and appearing for all the world to be precisely whom he claims to be, rings your doorbell and introduces himself as a representative of the Acme Burial Insurance Company. He shows you an impressive, glossy brochure and a printed contract form. You sign on the dotted line and give the man a $100 down payment. You later discover that the silver-tongued fellow had no connection whatsoever with Acme and that he had created the phony brochures and contract forms as props. Unfortunately, you have no recourse against Acme. Although your belief that the salesman was acting for Acme may have been reasonable, you cannot point to any manifestation by or attributable to Acme, the apparent principal. Consequently, there is no apparent authority.

An apparent agent can supply the necessary peppercorn of manifestation only if the apparent agent: (i) is actually authorized to act for the principal, and (ii) while actually authorized, accurately describes the extent of its authority. Every agent has the implied actual authority to accurately describe the agent's own actual authority,\(^{34}\) and such accurate descriptions are therefore attributable to the principal.

**Example:** You operate a horse ranch. One day a woman approaches you and informs you that she buys horses on behalf of Acme Rodeo Company and that she has the authority to pay up to $2,500 per horse. At that time, her statements are accurate. Two weeks later she returns and purports to commit Acme to purchase a quarter horse for $2,200. Unbeknownst to you, however, three days earlier Acme had expressly restricted her authority to purchases of $1,700 or less. You should be able to hold Acme to the contract through an apparent authority claim. You can certainly show a manifestation attributable to the apparent principal. When the buying agent earlier described her buying authority, she acted within her implied actual authority. That description is therefore a manifestation attributable (and therefore "traceable") to Acme.

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\(^{33}\) Conduct by the apparent agent may be relevant to the reasonableness of the third party's belief, but that belief must ultimately rest on some manifestation attributable to the apparent principal. In contrast, a manifestation by one agent of a principal can give rise to apparent authority for another agent of the principal—if the first agent's manifestation is legally attributable to the principal. For a simple illustration of this phenomenon, see the first Example in section 2.3.4. See also section 2.8.

\(^{34}\) R.2d, §27, comment c. The principal can remove this authority by directing the agent not to represent her authority. R.3d does not address this issue, making instead only the more general point that "an agent's own statements about the nature or extent of the agent's authority to act on behalf of the principal do not create apparent authority by themselves." R.3d, §6.11, comment b.
§2.3.4 Noteworthy Modes of Manifestation

Through Intermediaries

A manifestation that reaches the third party through intermediaries can still give rise to apparent authority.

Example: Acting on instructions from the Art Collector, the Art Collector's personal secretary sends a letter to the Auction House stating: "On behalf of Art Collector, I am writing to inform you that, at your upcoming auction, Broker will be representing and bidding for Art Collector." Broker has apparent authority to bid for the Art Collector, even though the Art Collector herself (the apparent principal) never personally made the relevant manifestation. The secretary's letter constitutes a manifestation attributable to the Art Collector because the secretary's communication, made within the zone of actual authority, binds (i.e., is attributable to) the secretary's principal.35

By Position

Sometimes the principal's sole manifestation to the third party may be to put an agent in a particular role. In light of local custom and standard business practices, that role may by itself cause a third party to believe reasonably that the agent has certain authority. This type of apparent authority is sometimes called authority by position.

Example: The owner of a dry cleaning store hires Ralph to work at the counter, and expressly authorizes him to accept clothes for cleaning, give receipts, return cleaned clothes to customers, and accept payment from customers. Although the owner expressly forbids Ralph to promise to have any garment cleaned in less than two working days, Ralph promises a law student to have her "interview suit" cleaned "by tomorrow." The doctrine of apparent authority may hold the dry cleaning store to Ralph's promise. Ralph's position (as counter clerk) constitutes the necessary manifestation. The question is whether, based on that bare manifestation, the customer reasonably believed that Ralph had the authority to make the promise. Since it is customary for counter clerks to tell customers when clothes will be ready, and since 24-hour service is not unusual in the dry cleaning business, the answer is probably yes.36

Example: After lengthy negotiations with a claims adjuster and without any lawsuit having been filed, an attorney purports to settle her client's insurance claim for $25,000. Unless the client has given the

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35 For a more detailed discussion of this type of attribution, see section 2.8.
36 As a "general agent," Ralph may also have bound the owner through inherent agency power. See section 2.6.2. R.3d relies exclusively on apparent authority. R.3d, ch. 2, Introductory Note, §2.01, comment b (explaining that Restatement (Third) does not use the concept of inherent agency power).
attorney actual authority to settle for that amount, the client is not bound. The mere position of an attorney does not create apparent authority to bind a client to a settlement.\textsuperscript{37}

Under the doctrine of "apparent authority by position," the word "position" refers not to physical location but rather to a person's recognized role within an organization and the functions normally performed by a person in that recognized role. In some instances—as in the above Example with Ralph and the dry cleaning—a person's physical position signals that the person has a particular function and role on behalf of the principal. Even then, however, the physical location is merely evidence of the organizational position.

\textbf{Apparent Authority by Position within Organizations} Large organizations dominate our economy, and those organizations inevitably distribute responsibilities across many positions. Moreover, even in a small organization employees can have substantially different functions, which may be reflected in job titles.

It is therefore necessary to consider what apparent authority, if any, attaches to positions and titles within an organizational hierarchy. In general:

\textbf{Example:} Rachael is employed as a "purchasing agent" by Snerdly Manufacturing, LLC. Rachael has the apparent authority to make ordinary and usual purchases on Snerdly's behalf.

The particularities of an organization's structure may influence the apparent authority analysis.

\textit{Observing a systematic hierarchy, a third party might reasonably infer that the organization is represented by a particular agent whose acts and statements are compatible with the agent's situation within the organization. Questions of apparent authority in this context often turn on

\textsuperscript{37} Some courts hold otherwise, but the Example reflects the majority view. The situation is different when a lawsuit is ongoing and a party's attorney of record agrees to a settlement. See, e.g., Navajo Tribe of Indians v. Hanosh Chevrolet–Buick, Inc., 749 P.2d 90, 92 (NM 1988) ("While an attorney's authority to settle must be expressly conferred, it is presumed that an attorney of record who settles his client's claim in open court has authority to do so unless rebutted by affirmative evidence to the contrary.") (citation omitted).

\textsuperscript{38} R.3d, §1.03, comment b.

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the interplay between general definitions or authority associated [e.g., by custom] with specific positions and observed characteristics of how the organization actually functions.39

More particularly:

- **CEO or president**—apparent authority for transactions within the organization's ordinary course of business
- **general manager**—apparent authority for transactions within the organization's ordinary course of business
- **vice president**—no apparent authority, because the title lacks any generalized meaning; however, a "vice president for/of [some specific function]" might have apparent authority to commit the organization to matters normally handled by the person in charge of that function
- **corporate secretary**—apparent authority to certify copies of corporate documents
- **branch manager**—in most jurisdictions, no per se apparent authority to bind the principal, but probably apparent authority to communicate decisions on significant matters made by the principal and, in some jurisdictions, apparent authority to make decisions ordinarily made at the branch level

Example: The CEO of Oz Balloon Tours, Inc., purports to commit the company to sell its sole balloon. The CEO has no apparent authority for this extraordinary transaction.

Example: Same facts, except that the company has 20 balloons, regularly buys new ones, and sells used ones. The CEO has apparent authority to sell one or several used balloons.

Example: Rachael is the vice president for marketing for Sammada, LLC, a company that puts on rock concert tours and is known to spend tens of thousands of dollars in advertising. Rachael has apparent authority to enter into a $15,000 radio "buy" in a local media market to advertise a concert sponsored by Sammada.

An agent's apparent authority can be augmented if the organization provides the agent with standardized form contracts.

Example: Rosencrantz is a branch manager for the First Bank of Polonius, with actual authority to approve loans in amounts less than $50,000. The Bank provides Rosencrantz with copies of a form loan

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39 R.3d, §1.03, comment c.
agreement, the first page of which carries the Bank's name and states in bold print: **NOT VALID FOR LOANS IN EXCESS OF $100,000.** Rosencrantz uses a copy of the form agreement to commit the Bank to lend Laertes $75,000. The Bank is probably bound. It is unclear whether Rosencrantz's position as branch manager suffices to create apparent authority for a $75,000 loan. However, Rosencrantz's possession of the form agreements (a manifestation traceable to the Bank), coupled with his position, probably does.

**<H5>By Acquiescence**  
<TEXT>Sometimes the principal makes the necessary manifestation by acquiescing in an agent's conduct.  

<EXT>**Example:** On several occasions, the caretaker of an apartment complex contracts with a roof repair service to fix a leaking roof. Each time, the repair service sends an invoice to the owner of the complex, and each time the owner pays. The repair service has no other contact with the owner. On the next service call, all goes as usual except that the owner refuses to pay. The owner claims that "the caretaker has no authority to order repairs." Even if the owner is correct as to the caretaker's actual authority, the repair service can still collect. By paying the previous invoices without comment, the owner of the complex has made the predicate manifestation to "clothe" the caretaker with apparent authority to order repairs from that particular repair company.

<EXT>**Example:** After the first two days of trial, attorneys for the two sides negotiate a settlement. With the parties present in open court, the two attorneys read the settlement into the record. Neither party objects. Both parties are bound to the settlement regardless of whether either attorney had actual authority to settle. The clients' acquiescence imparted apparent authority to their respective counsel.  

**<H5>By Inaction**  
<TEXT>In limited circumstances, an apparent principal's inaction may constitute a manifestation. For an apparent principal's inaction to give rise to apparent authority, the following criteria must be met:

- <BL>Someone (including the apparent agent) must assert that the apparent agent has actual authority.
- The apparent principal must be aware of those assertions and fail to do anything to contradict them.

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<FN> 40 Under the “presumption” rule stated above in note TBD, each party’s acquiescence would prevent that party from overcoming the presumption, as well as constituting a manifestation creating the appearance of authority for the party’s lawyer. In addition, the acquiescence would constitute a manifestation of actual authority from each party to that party’s lawyer. See section TBA (manifestation by principal to agent via acquiescence).
• The third-party claimant must reasonably believe that the apparent agent is authorized.
• The third-party claimant must be aware of:
  — <BSL>the assertions themselves,
  — the apparent principal's knowledge of the assertions, and
  — the apparent principal's failure to contradict the assertions.
• <BL>The third party's reasonable belief that the apparent agent is authorized must be traceable to the apparent principal's failure to contradict the assertions.  

In these circumstances, the apparent principal's silence amounts to acquiescence and is a manifestation that is known to the third party.  

<EXT><TEXT>Case in Point—Azur v. Chase Bank, USA, Nat. Ass'n.: “Francis H. Azur filed suit against Chase Bank, USA, alleging [inter alia] violations of 15 U.S.C. §§ 1643 and 1666 of the Truth in Lending Act (TILA) . . . after Azur's personal assistant, Michele Vanek, misappropriated over $1 million from Azur through the fraudulent use of a Chase credit card over the course of seven years. . . . [W]e must evaluate whether Azur's §§ 1643 and 1666 claims are precluded because Azur vested Vanek with apparent authority to use the Chase credit card. . . . Vanek's responsibilities consisted of picking up Azur's personal bills, including his credit card bills, from a Post Office Box in Coraopolis, Pennsylvania; opening the bills; preparing and presenting checks for Azur to sign; mailing the payments; and balancing Azur's checking and savings accounts at Dollar Bank. According to Azur, it was Vanek's job alone to review Azur's credit card and bank statements and contact the credit card company to discuss any odd charges. Azur also provided Vanek with access to his credit card number to enable her to make purchases at his request. . . . Azur's negligent omissions led Chase to reasonably believe that the fraudulent charges were authorized. Although Azur may not have been aware that Vanek was using the Chase credit card, or even that the Chase credit card account existed, Azur knew that he had a Dollar Bank checking account, and he did not review his Dollar Bank statements or exercise any other oversight over Vanek, his employee. Instead, Azur . . . [failed] to separate the approval and payment functions within [his] cash disbursement process. Had Azur occasionally reviewed his statements,

<FN>41 If this element is missing, the closely related doctrine of "estoppel" may help the third party. See section 2.5.
42 Contract law has a comparable rule on "acceptance [of an offer] by silence." Restatement (Second) of Contracts, §69(1)(c).
Azur would have likely noticed that checks had been written to Chase. Because Chase reasonably believed that a prudent business person would oversee his employees in such a manner, Chase reasonably relied on the continuous payment of the fraudulent charges.43

§2.3.5 The Third Party's Interpretation: The Reasonableness Requirement

For apparent authority to exist, a manifestation attributable to the apparent principal must cause the third party to believe that the apparent agent has authority. Mere belief, however, is not enough. Apparent authority will exist only to the extent that the third party's belief is reasonable.

In determining whether a third party has reasonably interpreted the apparent principal's manifestations, the law considers the same kinds of information that are relevant to determining whether an agent has reasonably interpreted the manifestation of its principal.44 Apparent authority analysis thus parallels actual authority analysis, except that apparent authority focuses on the interpretations of the third party, not the agent. We can therefore adapt R.2d, §34, comment a to read: "All matters throwing light upon what a reasonable person in the position of the [third party] at the time of acting would consider are to be given due weight."45

Case in Point—Streetman v. Benchmark Bank: The Streetmans’ business collapsed when their bank stopped honoring plaintiffs’ overdraft checks. Asserting that the bank’s loan officer had promised that the bank would honor “all overdrafts,” the Streetmans sued. The court first held that the loan officer had no actual authority to make the promise. On the issue of apparent authority, the court stated: “The undisputed evidence clearly shows that the Streetmans knew from dealing with their previous bank that banks have lending limits; consequently, they knew that [the loan officer’s] authority was limited and that he could not agree to pay ‘all overdrafts’ drawn on their account. Moreover, a reasonably prudent person would not believe that Watts was acting within the scope of his authority by promising to pay ‘all overdrafts’ drawn on the account.”46

The Third Party's Duty of Inquiry

Sometimes an apparent principal's manifestations create an appearance of authority, but it remains unreasonable for a third party to act upon that appearance without knowing more. The reasonable interpretation requirement thus imposes a duty of inquiry on the third-party claimant.47 For instance,

43 Azur v. Chase Bank, USA, Nat. Ass'n, 601 F.3d 212, 214, 221 (3d Cir. 2010) (footnotes, internal quotation, and citations omitted). The facts also support a claim of agency by estoppel. See section 2.5.
44 See section 2.2.2.
45 R.3d, §2.03, comment c.
47 In this context, the word "duty" is somewhat misleading. Typically, a duty is an obligation the nonperformance of which entitles the obligee to a remedy. In contrast, nonperformance of the duty of
the manifestation itself may be ambiguous. Or the apparent agent's conduct may be sufficiently unusual as to raise doubts. In such circumstances, the third party cannot reasonably interpret the manifestation as an indication of authority without first making some inquiry of the apparent principal.

Case in Point—Truck Crane Service Co. v. Barr-Nelson: A supplier of construction services and a general contractor dispute whether the general contractor is liable to the supplier for services furnished to a subcontractor. The president of the general contractor writes a letter denying liability. The supplier subsequently telephones the general contractor and talks with a vice president. Without consulting the president and without actual authority, the vice president acknowledges the liability and signs an agreement guaranteeing the subcontractor's payment. When the general contractor repudiates the vice president's action, the supplier claims that the vice president had apparent authority to make the acknowledgement and sign the guarantee. A court holds otherwise, stating: "The fact that the [supplier] had been notified in writing by [the general contractor's] president that [the general contractor] denied liability for these services put the [supplier] on inquiry as to the authority of any other employee to countermand such a position."48

The Role of the Apparent Agent's Conduct

With the one exception discussed in section 2.3.3 (the Example about the horse buyer), the apparent agent's conduct cannot satisfy the manifestation requirement. That conduct can, however, enter into the reasonableness determination. Plausible behavior by the apparent agent will buttress the third party's claim; implausible behavior will undercut it.

Irrelevance of Apparent Agent's Purpose

A person with apparent authority can bind the apparent principal to a contract even if the person does not intend to benefit the apparent principal and even if the person is lying about being authorized.

Example: A bank teller accepts a customer's deposit of $9,000 in cash, deciding at that moment to pocket the cash for himself. The teller prints the customer her receipt and then "goes on break" and never returns (absconding with the $9,000). When the teller accepted the deposit, he lacked the actual authority to act for the bank.49 He continued to have

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48 Truck Crane Service Co. v. Barr-Nelson, 329 N.W. 2d 824, 827 (Minn. 1983).
49 Having decided to embezzle from the bank, the teller could no longer reasonably believe himself authorized to accept funds on behalf of the bank.
apparent authority by position, however, and the bank must credit the customer's account with $9,000.

§2.3.6 The Necessity of Situation-by-Situation Analysis

Although an apparent agent may have apparent authority as to a wide range of acts and as to a wide range of third parties, each claim of apparent authority must be analyzed separately—even different claims from the same claimant. The reasons for this approach inhere in the elements necessary to create apparent authority. For any given claim of apparent authority, the third party must show that, at the relevant moment:

1. a manifestation had occurred that was attributable to the apparent principal;
2. the manifestation had reached the third party;
3. the manifestation caused the third party to believe that the apparent agent was authorized; and
4. the third party's belief was reasonable.

If the apparent principal has made more than one manifestation, element one may vary from claimant to claimant. Elements two, three, and four may vary depending on the identity of the third-party claimant and on the specific act claimed to be authorized. For example, two different third parties may draw different conclusions from the same manifestations. Or, two different third parties may draw the same conclusion, but for one—possessing knowledge or expertise lacked by the other—the conclusion may not be reasonable. Similarly, even with regard to the same third party, one act may reasonably appear authorized while another act may not.

Given the necessity of situation-by-situation analysis, efforts to counteract an impression of apparent authority will be effective only to the extent that the counteracting manifestations timely reach the relevant third party.

Example: Rachael, the owner of Rachael's Service Station, decides that she can no longer afford the 10 percent discount she has long offered to regular customers. She calls her mechanics together and says, "Effective right now, no more 10 percent discounts." The next day, one of the mechanics, momentarily forgetting Rachael's instruction, offers the discount to a customer. The customer accepts and leaves the car for servicing. When the customer returns to pick up the car, the mechanic says, "Hey, I'm sorry. I forgot. We don't give 10 percent discounts anymore." The customer is nonetheless entitled to the discount. Based on past dealings, the mechanic had apparent authority by acquiescence. Although the mechanic now lacks actual authority, the apparent authority remains intact because Rachael's counteracting manifestation has not reached the third party.
§2.3.7 "Lingering" Apparent Authority

The doctrine of "lingering" apparent authority is the agency law's analog to the concept of inertia. 50 “[I]t is reasonable for third parties to assume that an agent's actual authority is a continuing or ongoing condition.” 51 Therefore, a person's apparent authority can continue after the person's actual authority has ended.

Example: A landlord fires her resident manager, effective immediately, giving the manager 30 days notice to vacate the apartment designated as the manager's apartment. The landlord then sends a letter to each tenant in the building, explaining the situation and stating that all inquiries, notices, and payments should be made directly to the landlord. The next morning, before the letter has arrived, a tenant delivers his rent to the former resident manager, who accepts the rent as if nothing had happened. Although the former resident manager lacked actual authority to accept the rent, apparent authority still existed.

How long apparent authority can linger depends on the circumstances. The more substantial the transaction involved, the more likely it is that the third party has a duty to reconfirm the purported agent's bona fides. Likewise, it matters how distant in time the transaction is from the most recent manifestation traceable to the purported principal. The overarching question is whether the third party's belief continues to be reasonable.

§2.3.8 Rationale of the Apparent Authority Doctrine

When a person purports to bind another in an interaction with a third party but lacks the actual authority to do so, the law must decide which of two relatively blameless parties will bear any resulting loss—the apparent principal or the third party. 52 For two different (though compatible) reasons, where apparent authority existed, the law puts the loss on the apparent principal:

1. So long as the third party has not been careless or silly, any loss resulting from the misapprehension of authority should be imposed on the party who could have prevented the misapprehension in the first place.

50 Or, for those who majored in the humanities, "The song has ended/but the melody lingers on." (Irving Berlin)
51 R.3d, §3.11, comment c.
52 In a perfect world this question would perhaps be moot, because the apparent agent would "make good" any harm done. For the relevant legal theories, see sections 4.2.2 (warranty of authority) and 4.1.2 (duty to act within authority). In the real world, however, holding the apparent agent accountable costs time, effort, and money. Moreover, the apparent agent may be judgment-proof, beyond the jurisdiction of the court, or simply nowhere to be found.
2. Any loss should be imposed so as not to disrupt normal commercial operations.

The first rationale is reflected in the doctrine's requirement that the third party's belief be reasonable. The second rationale is served because the doctrine permits a commercial entity to rely on the appearance of authority so long as the appearance can be traced back to a manifestation of the apparent principal and the commercial entity acts reasonably in interpreting that manifestation.

§2.3.9 Apparent Authority and Principals
That Are Not Fully Disclosed

An agent for an undisclosed principal can never have apparent authority, because by definition the third party is unaware that the agent is acting for any principal at all. It is therefore impossible for the third party to claim that, at the relevant moment, the agent appeared to be acting for the actual principal.\(^{53}\)

As to an agent for an unidentified (partially disclosed) principal, apparent authority is possible in theory but rare in practice. The third party must be able to point to some manifestation attributable to the principal that supports an inference that the agent has actual authority to act for some principal but which does not disclose the identity of the actual principal.

Example: P, an importer, has purchased a shipment of steel from Brazil and retains A, a customhouse broker, to clear the steel through customs. That task requires posting security for any custom duties that may be due, and customhouse brokers typically obtain security bonds on behalf of their clients. Without disclosing P's identity, A arranges for T, an insurance company, to post a surety bond for the duties on P's steel. A has apparent authority to bind P to pay T for the bond. P has provided A with the information about the shipment, which A needs in order to arrange the bond, and T is aware that A has obtained that information for the owner of the steel. P has thus made a manifestation that A is authorized to act on P's behalf, even though neither the manifestation nor any other circumstances have disclosed P's identity.\(^{54}\)

§2.3.10 Binding the Principal and Third Party in Contract
via Apparent Authority

\(^{53}\) *A fortiori*, the third party cannot trace that appearance to a manifestation attributable to the principal.
\(^{54}\) This Example is taken from R.3d, §2.03, Illustration 15, which, according to the Reporter's Notes, is in turn based on Old Republic Ins. Co. v. Hansa World Cargo Serv. Inc., 51 F. Supp. 2d 457, 495 (S.D.N.Y. 1999).
With regard to binding a principal to contracts, apparent authority creates essentially the same results as actual authority. If an apparent agent, acting with apparent authority, makes a contract on behalf of an apparent principal, then the principal is bound just as if the principal had itself entered into the contract. The third party is likewise bound to the contract.

§2.4 ATTRIBUTION OF INFORMATION

§2.4.1 The Attribution Function and Its Connection with Non-Agency Law

One of the most important functions of agency law is to treat the principal as if the principal knows, receives, or communicates information actually known, received, or communicated by an agent. Other law determines the significance of the attributed information.

Example: A contract between Hunter, Inc., and Rabbit, Inc., requires Hunter to provide Rabbit "48 hours advance notice of any deliveries." The shipping clerk of Hunter telephones Rabbit to give notice of a forthcoming delivery and speaks to a night janitor. Agency law determines whether that conversation constitutes notice to Rabbit. From there, the contract and contract law take over and determine the significance of notice given or omitted.

Example: Injured by a defective widget, a tort victim claims that the manufacturer should be liable for punitive damages, and alleges that "said Defendant knew that the said widget design was defective and prone to inflict serious injuries, and said Defendant had known of this defect and danger for at least five years before the sale of the widget that injured Plaintiff in that Defendant's chief engineer knew of said defect." Whether the manufacturer "knew" what the chief engineer knew is a question of agency law. Whether knowingly selling a dangerously defective product should result in punitive damages is a question of tort law.

§2.4.2 Attribution as of When?

Attribution of information is always time specific, with one party or another asserting that at some relevant moment some person knew, received, or communicated

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55 The exception for undisclosed principals, discussed at section 2.3.3 does not apply, because apparent authority cannot apply to an undisclosed principal.
some particular piece of information. Like the consequences of attribution,\footnote{See section 2.4.1.} the relevant moment is determined by other law. To borrow a famous comment from the Watergate crisis, agency law determines "what did he know and when did he know it."\footnote{According to Senator Howard H. Baker, Jr., the pivotal question in the Watergate crisis was, "What did the President know, and when did he know it?" Fred Shapiro, ed., Oxford Dictionary of American Legal Quotations (1993) at 13 (citing Sam J. Ervin, Jr., The Whole Truth: The Watergate Conspiracy at 174).} Other law determines which "when" matters.

\textit{Example:} In the products liability Example involving the defective widget, tort law determines that the relevant moment is the moment at which the manufacturer sold the widget that injured the plaintiff. (If the jurisdiction recognizes a post-sale duty to warn, a later moment might be relevant as well.)

\section*{§2.4.3 Attribution of Notice and Notification Received by an Agent}

Some legal rules and many contracts require or authorize one person to give "notice" of certain facts to another person or to send another person a "notification." Often a person will attempt to give notice or send notification to a principal by giving the notice or sending the notification to an agent. If the agent has actual or apparent authority to receive the notice or notification, then notice or notification to the agent has the same effect as notice made directly to the principal.\footnote{Other law determines what the effect will be. See section 2.4.1.} The attribution occurs regardless of whether the agent informs the principal of the notice or notification, unless when the agent received the notice or notification: (i) the agent was acting adversely to the principal, and (ii) the third party knew or had reason to know that the agent was so acting.

\section*{§2.4.4 Attribution of Facts Known by an Agent}

\textbf{Basic Rule} \textit{Example:} Caesar wishes to buy an apartment building for investment purposes and retains Brutus as his agent to find and negotiate the purchase of a good property. Brutus comes into contact with Anthony, who offers a seemingly attractive building for sale at an attractive price. However, when Brutus researches the neighborhood, he learns that the city has just approved a permit to open a halfway house across the street.
Anthony offers Brutus $1,000 "so that what Caesar doesn't know won't hurt me." Brutus accepts, and Caesar buys the property. When Caesar subsequently claims fraud in the inducement, Anthony cannot successfully defend by claiming that Caesar knew about the halfway house. Beginning when he accepted the bribe and continuing through the closing of the deal, Brutus was acting adversely to Caesar and Anthony knew it.

**The Auditor Cases**

Agency law has recently evolved to address the so-called “imputation defense” for auditing firms.

**Case in Point—NCP Litigation Trust v. KPMG LLP:** “In the mid-1990s, two officers of a corporation intentionally misrepresented details concerning the corporation's financial status to an independent auditing firm. That firm in turn failed to detect those misrepresentations for several years. After subsequent audits revealed the officers' fraud, the corporation was forced to acknowledge previously unreported losses of tens of millions of dollars and to declare bankruptcy. A litigation trust, acting as the corporation's successor-in-interest and representing the corporation's shareholders, filed suit against the auditor for negligently conducting the audit. The trial court granted the auditor's motion to dismiss based on the imputation doctrine, which holds that knowledge of an agent generally is attributed to its principal. The trial court concluded that the fraud was imputable to the litigation trust, as the corporation's successor, and that the litigation trust cannot sue the auditor unless the auditor intentionally and ‘material[ly] participat[ed]’ in the fraud…. We hold that the imputation doctrine does not bar corporate shareholders from recovering through a litigation trust against an auditor who was negligent within the scope of its engagement by failing to uncover or report the fraud of corporate officers and directors.”

**Complexities as to Source and Permanence of Agent's Knowledge**

Suppose an agent learns a fact "off" the job—either (1) before becoming an agent, or (2) while an agent but while "off duty." Is the fact attributed the principal?

Suppose that during the agency relationship an agent knows a fact related to his or her duties, but by the time the fact is relevant to legal relations of the principal, the agent has forgotten the fact. Is the principal still "charged" with knowledge of the fact?

The answers to each of these questions is yes, and the rationale is straightforward. An agent's duties include communicating to the principal any information that the agent has reason to know might be of interest or importance to the principal. The rules for attributing information assume that the agent fulfills the duty and that the principal does not forget.

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 FN 60 NCP Litigation Trust v. KPMG LLP, 901 A.2d 871, 873 (NJ 2006).

61 See section 4.1.5.
Case in Point—Engen v. Mitch's Bar & Grill: A bartender serves a patron a couple of drinks, after which the patron assaults another patron. The victim sues the bar for negligence, contending that (i) the bartender knew from her own "off the job" experience as the assailant's girlfriend that the assailant was prone to violence after a couple of drinks, and (ii) the bartender's knowledge was attributable to the bar, since the fact concerned a matter within the bartender's actual authority (making judgments about who could be served). The bartender's knowledge is attributed to the bar, despite the "off the job" source of the information.62

§2.4.5 Information That an Agent Should Know but Does Not

According to the R.2d and most courts, the unknown information is not attributed to the principal.63

Example: P employs A, who is president of a bank, to purchase notes for him. A is a member of the discount committee of the bank and, if he attended to his duties properly, would know that B had obtained a specific negotiable note from T by fraud. Further, had he made the inquiries that his duty to P required, he would have learned this. Not having performed his duties properly, he does not know this fact and purchases the note from B for P. P does not hold the note subject to T's interest because of A's conduct, since there was no duty of care by P to ascertain the fraud in the original transaction.64

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R.2d, §277 provides:

The principal is not affected by the knowledge that an agent should have acquired in the performance of the agent's duties to the principal or to others, except where the principal or master has a duty to others that care shall be exercised in obtaining information.

This Example comes verbatim from R.2d, §277, Illustration 1.
R.3d takes a contrary position: "Notice is imputed to a principal of a fact that an agent knows or has reason to know ... if knowledge of the fact is material to the agent's duties to the principal." 65

§2.4.6 Information Communicated by an Agent to Others

If an agent acting with actual or apparent authority

- gives notice to a third party, or
- makes a statement or promise to a third party, 66 or
- makes a misrepresentation to a third party, 67

the information conveyed has the same legal effect under contract law as if the principal had conveyed the information directly. 68

§2.4.7 Direction of Attribution

Agency law attribution works in only one direction—upward, from agent to principal. "Notice of facts that a principal knows or has reason to know is not imputed downward to an agent." 69

Case in Point—Knox-Tenn Rental Co. v. Home Ins. Co.: A patient brings a malpractice case against a hospital and several doctors who work as employees of the hospital. The hospital and doctors tender defense of the case to their professional liability insurer, under a policy naming as insureds both the hospital and its employee doctors. The

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65 R.3d, §5.03. In support of this position, the Reporter's Notes cite Southport Little League v. Vaugh, 734 N.E. 2d 261, 275 (Ind. Ct. App. 2000) as holding that "a principal is charged with the knowledge of that which his agent by ordinary care could have known where the agent has received sufficient information to awaken inquiry.

66 Not all promises are enforceable, even if made directly by a principal. Agency law only attributes the agent's promise to the principal; contract law determines whether the promise is enforceable.

67 How can an agent have actual authority to make misrepresentations? Having actual authority to make accurate statements, that agent might make a misstatement innocently, reasonably believing the misstatement to be true. According to Restatement §162, comment b, that misstatement would come within the agent's actual authority. Other instances are also possible. A nefarious principal might indeed authorize fraud, and an innocent principal might authorize statements that turn out to be misrepresentations. In any event, where actual authority leaves off, inherent agency power takes over. An agent of a disclosed or partially disclosed principal has inherent power to make an inaccurate statement that, if accurate, would have been within the agent's actual authority. See section 2.6.3.

68 The impact under tort law is subtly different. See section 3.4.2.

69 R.3d, §5.01, comment g.
insurance company desires to "reserve its rights"—that is, take up the defense of the case while reserving the right to later assert that the case is not covered by the policy. Under the insurance contract, in order to reserve its rights, the insurance company must give notice to each insured. Assuming that the hospital will pass on the information to the doctors, the insurance company gives notice to the hospital but not individually to the doctors. The insurer has waived its reservation as to the doctors, because notice received by a principal (the hospital) is not attributed downward (to the employee doctors). 

<TEXT>Similarly, imputation does not work "sideways"; that is, attribution is to the principal and not to affiliates or owners of the principal.

<EXT>Case in Point—Specialized Tours, Inc. v. Hagen.: The sole shareholder of a corporation sold his stock in the corporation, warranting that, to his knowledge, the corporation was not in violation of any government regulations. In fact, the corporation was in violation, and its general manager knew of the violation. In the buyer's breach of warranty case, the court properly refused to attribute the general manager's knowledge to the shareholder, because (i) as a matter of agency law, the general manager is an agent of the corporation (not the shareholder); and (ii) as a matter of corporate law, the corporation is a "person" legally separate from its owner (the shareholder).

§2.4.8 Information Attribution Within Organizations

<TEXT>Even most small businesses have multiple agents, and large organizations can have thousands. When a principal is an organization, information attribution can produce untoward effects—especially if "the left hand doesn't know what the right hand is doing."

<TEXT>Attribution can occur even when the agent with the attributed knowledge is not the person acting for the principal in the transaction at issue.

<EXT>Restatement on Point: Sylvia, the executive vice president of Widget, Inc. ("Widget"), purchases a products liability insurance policy for Widget, and on Widget's behalf signs an application stating that Widget knows of no present facts that would give rise to a claim under the policy. Sylvia has canvassed all top-level Widget employees via email and knows of no such facts. Unfortunately, Widget's risk assessment...
coordinator does know of one potential claim but has neglected to tell Sylvia. The facts as to the claim are relevant to the risk manager's authorized tasks and are therefore attributed to Widget. Widget's application therefore contains a material, false statement, and the insurance company is entitled to an appropriate remedy.72

§2.5 ESTOPPEL

To establish apparent authority, a third party must show some manifestation of authority attributable to the principal. But what if:

- an asserted principal has made no such manifestation and has merely sat by while someone else has claimed an agency relationship;
- the claims of authority have led third parties to extend credit, incur costs, or otherwise change their position; and
- the asserted principal knew of the claims and of the danger to third parties and yet did nothing?

In such situations, apparent authority is rarely applicable, because only in very narrow circumstances can the asserted principal's inaction serve as a manifestation.73 To prevent injustice beyond those narrow circumstances, the Restatements and some courts use the concept of estoppel. In the words of R.3d, estoppel imposes liability on a person for:

A person who has not made a manifestation that an actor has authority as an agent and who is not otherwise liable as a party to a transaction purportedly done by the actor on that person's account is subject to liability to a third party who justifiably is induced to make a detrimental change in position because the transaction is believed to be on the person's account, if

1. the person intentionally or carelessly caused such belief, or
2. having notice of such belief and that it might induce others to change their positions, the person did not take reasonable steps to notify them of the facts.74

In concept, the distinction between apparent authority and estoppel is clear enough. Unlike apparent authority, estoppel can apply even though the claimant can show

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72 This Example is based on R.3d, §5.03, Illustration 12.
73 See section 2.3.4 (manifestation by inaction).
74 R.3d, §2.05. R.2d, §8B(1) was generally to the same effect. The R.3d makes explicit a point left implicit by R.2d—namely, that to successfully claim estoppel the third party must show that its reliance was justifiable.
no manifestation attributable to the asserted principal.\textsuperscript{75} Estoppel liability can arise from
the asserted principal's mere negligent failure to protect against a misapprehension.

Unfortunately, the case law often blurs this distinction. Many jurisdictions make
detrimental reliance an element of apparent authority and even refer to apparent authority
as "agency by estoppel." Moreover, most situations that give rise to apparent authority
also give rise to estoppel. If an asserted principal makes a manifestation sufficient to
support a reasonable inference of authority (i.e., to create apparent authority), the asserted
principal can probably be said to have "intentionally or carelessly caused such belief"
(i.e., estoppel).\textsuperscript{76} The R.3d attempts to eliminate this latter source of confusion by
defining estoppel to apply only in the absence of a manifestation by the asserted
principal.

\textbf{§2.6 INHERENT AGENCY POWER}

\textbf{§2.6.1 A Gap-Filling Doctrine Based on Fairness}

In some situations, an agent has neither actual nor apparent authority, and
estoppel does not apply. Yet the agent's position creates the potential for mischief with
third parties.

\textit{Example:} Noam purchases Eli's Dry Cleaning, does not change
the business name, and hires Eli to manage the dry cleaning store.
Although dry cleaning stores customarily order cleaning solvent in large
quantities, Noam instructs Eli never to buy more than $50 worth of solvent
at a time and has no reason to believe that Eli will disregard these
instructions.

However, Eli does disregard them and places a phone order for solvent
costing $450. The seller of the solvent believes that Eli is still the owner.
Eli has acted without actual authority; his principal's manifestations
expressly prohibit the order Eli made. Eli has also acted without apparent

\textsuperscript{75} For jurisdictions that follow the pure Restatement view of apparent authority, there is another distinction:
Apparent authority can exist without a showing of detrimental reliance. See section 2.3.2 for a discussion of
the Restatements' view of apparent authority. As noted in that section, many jurisdictions differ with the
Restatements on this point.

\textsuperscript{76} The quoted language is from R.2d, §8B(1)(a).
authority; there can be no apparent authority by position when the principal is undisclosed.77

<TEXT>To deal with such situations (and others as well),78 the R.2d and some courts use the doctrine of inherent agency power.79 The doctrine imposes enterprise liability; that is, it places the loss on the enterprise that stands to benefit from the agency relationship. As explained by the R.2d:

<EXT>It is inevitable that in doing their work, either through negligence or excess of zeal, agents will harm third persons or will deal with them in unauthorized ways. It would be unfair for an enterprise to have the benefit of the work of its agents without making it responsible to some extent for their excesses and failures to act carefully. The answer of the common law has been the creation of special agency powers or, to phrase it otherwise, the imposition of liability upon the principal because of unauthorized or negligent acts of his servants and other agents.80

<TEXT>In the dry cleaner Example above, there is no culpable conduct on Noam's part. To the contrary, Eli has caused mischief while acting counter to Noam's wishes. Yet the third party is also without blame, and the policy issue arises: As between the principal and the third party, who should bear the risk of the agent's misconduct? Who should have the burden of pressing claims against the agent or absorbing the harm the agent has caused?81

<H2>§2.6.2 A R.2d Rule of Inherent Power: Unauthorized Acts by a General Agent

<TEXT>When a principal entrusts an agent with ongoing responsibilities, the notion of an enterprise fairly applies. As a result, the agent has the inherent power to take certain actions even though the principal may have forbidden those actions. The R.2d and many cases use the category of "general agent" as the entrance criterion to this type of inherent power.

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77 <FN>For an explanation of this point, see section 2.3.8.
78 The doctrine of respondeat superior, discussed in Chapter 3, is another major example of inherent agency power.
79 Some courts call the doctrine "inherent agency authority." R.3d eschews the concept of inherent power, relying instead on concepts of apparent authority, estoppel, and restitution. R.3d, Chapter 2, Introductory Note, §2.01.
80 R.2d, §8A, comment a.
81 In a perfect world, free of transaction costs, both parties could look to the agent. The world, however, is not perfect. See supra note TBD. If the principal is at fault (e.g., has negligently hired an agent with a background of misbehavior), other doctrines will place the loss on the principal. For a discussion of a principal's liability for direct negligence, see sections 4.4.1 and 4.4.2.
General and Special Agents Defined — If a principal authorizes an agent "to conduct a series of transactions involving a continuity of service," the law labels the agent a general agent. If, in contrast, a principal authorizes the agent only to conduct a single transaction, or to conduct a series of transactions that do not involve "continuity of service," then the law labels the agent a special agent.

Perhaps the simplest example of a general agent is an employee in charge of a store, a factory, or other place of business. It is not necessary, however, to have wide-ranging or important responsibilities in order to be a general agent. A full-time photocopy clerk is a general agent with regard to photocopying duties.

In theory, the "special vs. general" distinction is an "either/or" matter. That is, with regard to any particular responsibility, an agent must be either a general agent or a special agent. In practice, however, this either/or categorization encounters many gray situations.

It is possible for an agent to be a general agent with regard to some matters and a special agent with regard to others. The key factor separating general agency status from special agent status is whether the agent has an ongoing responsibility.

Example: A bank employs Larry as a teller. One day, the bank asks Larry to deal with a caterer and arrange refreshments for a retirement party. With regard to his teller duties, Larry is a general agent. With regard to the party arrangement, Larry is a special agent.

Inherent Agency Power of General Agents — Under the R.2d doctrine of inherent agency power:

- if the agent is a general agent with actual authority to conduct certain transactions,
  - the agent is acting in the interests of the principal, and
  - the agent does an act usual or necessary with regard to the authorized transactions,
- then the act binds the principal regardless of whether the agent had actual authority and even if the principal has expressly forbidden the act.

Although this rule applies in slightly different forms to all principals, it makes the most difference for undisclosed and partially disclosed principals. With a disclosed principal, apparent authority by position will typically produce the same result as inherent power. With an undisclosed or partially disclosed principal, however, apparent authority is of no help.

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82 R.2d, §3(1).
<FN> 83 R.2d, §§161 (unauthorized acts of general agents); 194 (acts of general agents); and 195 (acts of manager appearing to be owner).
Example: Sylvia decides to enter the silk importing business. The trade is notoriously biased against women, and she fears that her company will suffer if her interest in it is known. She therefore hires Phil as her general manager, but sets up the company so that Phil appears to the outside world as the owner. It is common in this trade for silk importers to sell to large customers on credit, but Sylvia instructs Phil never to extend more than $50,000 of credit to any customer without Sylvia's approval. One day, in order to close an important deal, Phil agrees, without consulting Sylvia, to extend $150,000 of credit to one customer. Although Phil acted without actual or apparent authority, Sylvia, the company's true owner and Phil's undisclosed principal, is bound. "An undisclosed principal who entrusts an agent with the management of his business is subject to liability to third persons with whom the agent enters into transactions usual in such businesses and on the principal's account, although contrary to the directions of the principal." 84

Policy-Based Limitations to the Rule

This rule of inherent agency power has two policy-based limitations. The rule does not apply if either (i) the third party knows that the agent is acting without authority, or (ii) the agent is not acting in the principal's interest. If the third party knows of the lack of authority, then the third party is not innocent, which renders inapposite a key aspect of the rule's rationale. 85 If the agent acts on the agent's own behalf, the conduct is not part of the enterprise from which the principal stands to benefit which renders inapposite another key aspect of the rule's rationale.

R.3d's Approach

R.3d expressly declines to use the concept of inherent agency power, 86 but states a black letter rule for undisclosed principals that produces essentially the same results: "An undisclosed principal may not rely on instructions given an agent that qualify or reduce the agent's authority to less than the authority a third party would reasonably believe the agent to have under the same circumstances if the principal had been disclosed." 87

Ratification

§2.7 The Role, Meaning, and Effect of Ratification

84 R.2d, §195.
85 Recall from section 2.6.1 that inherent agency power functions to allocate the risk between two relatively blameless parties.
86 R.3d, §2.06, comment b.
87 R.3d, §2.06(2).
Ratification occurs when a principal affirms a previously unauthorized act. Ratification validates the original unauthorized act and produces the same legal consequences as if the original act had been authorized.\textsuperscript{88} If, for instance, a party ratifies a contract, the ratification binds both that party and the other party to the contract.

\textbf{Example:} Toklas is a janitor in a large residential apartment complex. She has neither actual nor apparent authority to act for the owner of the complex in renting apartments. She also lacks inherent agency power. Nonetheless, she shows apartment 101B to Alice and agrees to rent the apartment to her on a six-month lease. Later, when Alice telephones the rental office to check on her move-in date, she speaks to the actual owner. The owner says, "Well, you know Toklas had no business renting that apartment to you. She's just the janitor. But we'll go ahead." The owner has ratified Toklas's previously unauthorized actions, and Alice and the owner are both bound to the lease.

Ratification typically concerns "the making or breaking of a contract," \textsuperscript{89} although both R.2d and R.3d contemplate the ratification of torts.\textsuperscript{90}

In theory, \textit{as between the principal and the third party}, ratification matters only when no other attribution rule applies. If an actor has actual, apparent, or inherent authority, or if estoppel applies, the third party has no need to show that the principal retroactively validated the act. In practice, however, "[r]atification often serves the function of clarifying situations of ambiguous or uncertain authority," \textsuperscript{91} and in litigation, parties often argue ratification in the alternative. In addition—\textit{as between the principal and the agent}— "[r]atification…exonerates the agent against claims otherwise available to the principal on the basis that the agent's unauthorized action has caused loss to the principal," \textsuperscript{92} except where the principal has ratified to "cut his losses."

\textbf{Example:} Acting beyond his authority, Edmund sells and delivers to Lucy goods belonging to Peter. Peter decides to go through with the contract, even though he might have made a better deal elsewhere. Edmund is not liable to Peter for acting without authority, even if Peter could prove with requisite specificity the availability and value of the "better deal."

\begin{footnotes}
\item R.3d, §4.01(1) states: "Ratification is the affirmance of a prior act done by another, whereby the act is given effect as if done by an agent acting with actual authority."
\item R.3d, §4.01, comment \textit{a}.
\item There are indeed \textit{a few} cases that cite ratification as the reason for holding one party liable for another's tort. Most of those cases seem to involve the ratification of a course of conduct that happened to include a tort, rather than a purposeful embracing of the tort and its attendant liability. Some of the cases involve facts that support a "scope of employment"/\textit{respondeat superior} determination (Chapter 3) as much as a holding of ratification.
\item R.3d, §4.01, comment \textit{b}.
\item R.3d, Ch. 4, Intro. Note.
\end{footnotes}
Example: Acting beyond his authority, Edmund sells and delivers to Lucy goods belonging to Peter. Lucy then resells the goods to an innocent third party and fails to pay Peter. Peter files suit against Lucy for the contract price, in essence ratifying the sale. Edmund remains liable to Peter for any damages resulting from the unauthorized sale.

§2.7.2 Mechanics of Ratification

For ratification to occur, certain preconditions must exist and the purported principal must embrace the previously unauthorized act ("affirmance").

Preconditions

Ratification can occur only if the necessary preconditions exist:

• There must have been some transaction or event involving an unauthorized act.
  — Typically, someone ("the purported agent") will have purported —
    either expressly or impliedly — to act on behalf of another (the "purported principal") in some transaction with a third party.
  — Under the R.3d, ratification can apply as well to the unauthorized act of an agent for an undisclosed principal.  

• At the time of the unauthorized act, the purported principal must have existed and must have had capacity to originally authorize the act.

Affirmance — the Act (or Inaction) of Ratification

If the necessary preconditions exist, a purported principal ratifies by either:

• making a manifestation that, viewed objectively, indicates a choice to treat the unauthorized act as if it had been authorized; or
• engaging in conduct that is justifiable only if the purported principal had made such a choice.

Footnotes:

93 R.3d, §4.03, comment 6.
94 This precondition explains why a corporation cannot ratify a contract made on the corporation's behalf before the corporation came into existence. See section 2.7.5, which contrasts ratification with novation and assumption.
In the simplest of situations, a purported principal affirms just by stating a choice.

Example: Having read that car dealers generally make better deals for male customers than for female customers, Sally hires Ralph to purchase a used car on her behalf. She specifically instructs him, however, not to buy any foreign-made car. Purporting to act on Sally's behalf, Ralph makes a great deal on a used BMW. When Sally hears of the deal, she says, "Okay, for a deal like that I don't have to 'Buy American.' I'll take the car." Sally has ratified the deal.

Affirmance occurs when the manifestation occurs. The manifestation need not reach the third party to be effective.95

A purported principal can also affirm through inaction—that is, by failing to repudiate the act "under such circumstances that, according to the ordinary experience and habits of men, one would naturally be expected to speak if he did not consent."96 Such failure to repudiate creates a situation resembling agency by estoppel.

Example: Acting without either authority or power to bind the owner of an apartment complex, Toklas, the janitor, offers a resident manager job to Felix. The landlord learns of the offer and also hears that Felix is planning to quit his current job so he can become resident manager. The landlord says nothing to Felix, and Felix quits his current job. By this inaction, the landlord has ratified Toklas’ offer.

A purported principal can also ratify by accepting or retaining benefits while knowing that the benefits result from an unauthorized act. If the purported principal accepts benefits without the requisite knowledge, the third party may have an action in restitution or quantum meruit. Ratification is usually preferable for the third party, however, because ratification entitles the third party to the full benefit of the bargain. Restitution or quantum meruit, in contrast, entitles the third party only to the value of the benefit actually conferred.

Example: Toklas, the self-aggrandizing janitor, offers to rent an apartment to Mike for a year at $50 per month off the regular monthly rent if Mike agrees to keep the grass well-mowed. During his first month as a tenant, Mike mows the grass four times. If the landlord knew of the

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95 This rule parallels the rule governing an agent's consent to act on behalf of a principal. See sections 1.4-1.4.9. In that case also, the manifestation is viewed objectively and need not reach the other relevant party to be effective.
96 R.2d, §94, comment a. In gender-neutral and less ornate language, R.3d, comment d states that a "person may ratify the act through conduct justifiable only on the assumption that the person consents to be bound by the act's legal consequences."
Unauthorized offer, the landlord has ratified the agreement by accepting the services. Mike may therefore hold the landlord to the full bargain (i.e., to a lease and a rent reduction for a year). If, however, the landlord did not know of the offer, Mike has a right only to restitution or *quantum meruit* (i.e., only to be paid for the fair value of the mowing work he has already done).97

**The "All-or-Nothing" Rule**

Ratification occurs on an "all-or-nothing" basis. If a purported principal attempts to ratify only part of a single transaction, then either the entire transaction is ratified or there is no ratification at all.

Example: Acting without authority, Rebecca purports to sell Vladi's car to Michael for $500. Rebecca also purports to extend a 90-day warranty on the car. Vladi cannot ratify the sale without also ratifying the warranty.

If a purported principal makes a "piecemeal" affirmance, whether ratification has occurred depends essentially on whether the purported principal has manifested:

- an intent to ratify and has sought to impose some exclusions or qualifications (in which case the entire transaction has been ratified and the sought-after exclusions and qualifications are ineffective); or
- an intent to be bound only if the exclusions or qualifications are part of the transaction (in which case there is no ratification and neither the purported principal nor the third party is bound, unless the third party manifests consent to the conditions).98

**§2.7.3 Principal's Ignorance or Knowledge of Material Facts: Whose Burden of Proof?**

According to the R.2d, "If, at the time of affirmance, the purported principal is ignorant of material facts involved in the original transaction, and is unaware of his ignorance, he can thereafter avoid the effect of the affirmance." 99 However, many courts and the R.3d treat the purported principal's knowledge of material information as a

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97 If a third party has fully performed an unauthorized contract, the difference may well be immaterial. In theory, the measure of recovery will be different—benefit of the bargain versus value of services conferred—but in practice, courts often use the contract price to measure the benefit.

98 This fact determination resembles the determination made under §2-207(1) of the Uniform Commercial Code. That "battle of the forms" provision distinguishes between "a definite . . . expression of acceptance…which… states terms additional to or different from those offered" and an expression in which "acceptance is . . . made conditional on assent to the additional or different terms."

99 R.2d, §91(1).
precondition to ratification. "A person is not bound by a ratification made without knowledge of material facts involved in the original act when the person was unaware of such lack of knowledge." 100 The difference is more than semantic; it determines the burden of proof.

**Materiality Defined**

R.2d defines *material facts* as those that "so affect the existence and extent of the obligations involved in the transaction that knowledge of them is essential to an intelligent election to become a party to the transaction." 101 R.2d then confines this seemingly broad concept by specifically excluding knowledge:

- of the legal effect of ratification
- about the value of the transaction or the transaction's desirability, other than knowledge of important representations made by the agent or third party as they entered into the transaction.

R.3d uses a much briefer formulation, albeit one that is somewhat vaguer. The black letter refers to "material facts involved in the original act," 102 and a comment to the black letter explains that "[t]he point of materiality … is the relevance of the fact to the principal's consent to have legal relations affected by the agent's act." 103

The difference between the two Restatements could have substantial practical implications, depending on how a court interprets R.3d's language.

**Example:** Acting beyond her authority, A purports to bind P to a contract to sell frozen orange juice to T. Thinking the contract an excellent one for P, A immediately communicates with P, who affirms the contract. However, unbeknownst to P or A, a pest infestation in South America has eliminated a major source of frozen orange juice. The contract is therefore a very bad one for P. That information is certainly relevant to the principal's decision to embrace the deal, but it is also "about the value of the transaction or the transaction's desirability." Under the R.2d approach, the information is not material to the decision to ratify. Under the R.3d, the issue is less clear.

**Knowledge Requirement Not Purely Subjective**

At first glance, the knowledge requirement seems straightforward. Knowledge is a state of mind. What should matter, therefore, is whether the purported principal lacks subjective knowledge of material facts, not whether the purported principal has reason to know those facts.

However, both Restatements and the case law eschew this conceptually pure approach. According to the R.3d: "A factfinder may conclude that a principal has...

100 R.3d, §4.06.
101 R.2d, §91, comment d.
102 R.3d, §4.06.
103 R.3d, §4.06, comment c (stating, "[f]or definitions of materiality, see Restatement (Second), Torts, §538(2)(a); Principles of Corporate Governance: Analysis and Recommendations, §1.25").
[assumed the risk of ignorance and ratified] when the principal is shown to have had knowledge of facts that would have led a reasonable person to investigate further, but the principal ratified without further investigation.”104

Principal's Ignorance versus Third Party's Reliance

The principal's ignorance ceases to be a factor if the third party has learned of and detrimentally relied on the principal's affirmance.105

§2.7.4 The Third Party's Right of Avoidance

Ordinarily, a purported principal's affirmance binds not only the purported principal but also the third party. As explained previously, a third party can preclude ratification by giving notice of withdrawal from the transaction before the purported principal affirms.106 In two situations, the third party can also avoid an otherwise binding affirmance.

 Changed Circumstances

The third party may avoid a ratification if, before the purported principal ratifies, circumstances change so materially that holding the third party to the contract would be unfair. Obviously, at some point the third party will have to inform the purported principal of the changed circumstances. However, it is not necessary that the third party give notice before the affirmance.

Both Restatements use the same, classic example:

Purporting to act for P but without power to bind P, A contracts to sell Blackacre with a house thereon to T. The next day the house burns. P's later ratification does not bind T. T may elect to be bound by the contract.107

Conflicting Arrangements

A third party can also avoid ratification if the third party:

- learns that the purported agent acted without authority;
- relies on the apparent lack of authority; and
- makes substitute, conflicting arrangements or takes some other action that will cause prejudice to the third party if the original transaction is enforced.108

For the necessary reliance to exist, the third party must act before learning of the purported principal's affirmance.

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104 R.3d, §4.06, comment d.
105 R.3d, §4.08; R.2d §91, comment b.
106 See section 2.7.2.
107 R.3d, §4.05, Ill. 2, which is taken almost verbatim from R.2d, §89, Ill. 1.
108 R.3d, §4.05(2); R.2d, §95, comment b.
§2.7.5 The Term "Ratification" in Other Contexts; Contrasted with Adoption and Novation

Generally In agency law, ratification is a term of art with a very specific and intricate meaning, but agency law has no monopoly on the use of the word. For example, "ratification" is often used to describe the final step in an approval process involving different sets of decision makers at each step.

Example: Article V of the U.S. Constitution states: "The Congress, whenever two thirds of both Houses shall deem it necessary, shall propose Amendments to this Constitution, or on the Application of the Legislatures of two thirds of the several States, shall call a Convention for proposing Amendments, which, in either Case, shall be valid to all Intents and Purposes, as Part of this Constitution, when ratified by the Legislatures of three fourths of the several States, or by Conventions in three fourths thereof, as the one or the other Mode of Ratification may be proposed by the Congress; . . ."

Ratification, Adoption, and Novation Even in the agency context, cases sometimes use "ratification" carelessly, usually by confusing and interchanging the terms ratification, adoption, and novation. Many of these cases involve contracts made by promoters on behalf of limited liability companies, corporations, or other entities not in existence when the contract is made. To the extent that the three terms have separate meanings, those meanings are as follows.

Ratification is the retroactive approval of a previously unauthorized act. Subject to the conditions and exceptions discussed in this section, ratification binds both the purported principal and the third party to the original undertaking and discharges the purported agent from any liability on that undertaking.

Adoption occurs when:

- a purported agent has purported to bind a purported principal to an agreement while lacking the power to do so;
- the purported principal cannot ratify the purported agent's unauthorized act, typically because at the time of the act the purported principal either did not exist or lacked capacity to authorize the act;
- the original agreement made by the purported agent and the third party expressly or impliedly empowers the purported principal to choose to receive the benefits and assume the obligations of the agreement; and
- the purported principal manifests—either expressly or through a course of conduct—its desire to receive the benefits and assume the obligations of the agreement.
Like ratification, adoption binds both the principal and the third party to the original agreement. Unlike ratification, adoption does not relate back in time to the unauthorized act. So, if for any reason the starting date of the relationship between the adopting principal and the third party is important, that date is the date of the adoption, not the date of the unauthorized act. Moreover, adoption does not release the purported agent from any liability it may have to the third party on account of the original agreement, unless the original agreement provides that the principal's adoption will indeed release the agent.

Novation is a new, independent agreement between the principal and the third party. Novations arise from the same circumstances that give rise to adoptions, and it is often the original, unauthorized contract that causes the purported principal and the third party to consider doing business with each other. The terms of the novation may be and often are identical to the terms of the prior, unauthorized agreement.

Nonetheless, a novation reflects an entirely separate process of contract formation. Once formed, the novation contract completely displaces the original, unauthorized contract and relieves the purported agent from any liability it may have had to the third party on account of that prior contract.

Whether the new arrangement is an adoption (which does not release the purported agent) or a novation (which does) is a question of the parties' intent.

Example: Rachael decides to go into business with a 1950s-style hamburger joint. She plans to organize the business as a limited liability company under the name Sam's Place, LLC. She signs a lease for the restaurant, however, before actually forming the limited liability company. In signing the lease she purports to act as president of Sam's Place, LLC and neglects to inform the lessor that Sam's Place, LLC, has not yet come into existence.

Since a nonexistent limited liability company cannot authorize anyone to do anything, Rachael's act in signing the lease is unauthorized and does not bind the LLC. As of that moment, Rachael, not the LLC, is liable to the lessor on the lease. When Rachael does form the LLC, the LLC may decide to take responsibility for the lease. However, the LLC cannot by itself take Rachael off the hook. Ratification would release Rachael, but ratification is not possible: At the time of the lease signing the LLC did not exist, so one of the necessary preconditions to ratification is absent. The LLC can adopt the lease, but that adoption will not release Rachael. If the LLC later defaults, she will still be liable.

If the lessor agrees, the LLC and the lessor can make a novation. A new contractual relationship between the lessor and the LLC will replace the original lease, the LLC will be bound, and Rachael will no longer be liable.

See section 4.2.2.
§2.8 CHAINS OF AUTHORITY

§2.8.1 Multilevel Relationships

For the most part, the Examples used in this chapter so far have been "flat." The principals act through a single agent, and agents draw their authority directly from manifestations made by the principal. Third parties claim apparent authority from manifestations made directly by a principal.

Real-life relationships tend to be more intricate.

Example: Marcia is the manager of an airport office of a rental car company. As part of her job, she hires, supervises, and, when necessary, fires the people who staff that office. Those people are agents of the rental car company, not of Marcia, even though (1) it was Marcia who told each of them, "You're hired," and (2) the company itself has never made any direct manifestation to any of them.

Example: Seeking to increase business, Marcia retains the services of Abitatruth, Inc., an advertising agency. Acting on behalf of the rental car company, Marcia authorizes the agency to spend $10,000 to rent advertising space around the airport on the company's behalf. The agency assigns the work of renting the advertising space to Alan, one of its employees. Alan has the power to bind the rental car company, even though (1) Marcia has never made any manifestation to Alan, and (2) Marcia does not even know that Alan exists.

Each of these Examples involves a "concatenation" of responsibility. That is, in each situation a chain of relationships or events makes the rental car company the principal and gives the person at the bottom of the chain the power to bind. Thus, a person can be an agent without ever having met or communicated directly with the principal.

For instance, in the first Example (Marcia hires the staff), the employees are agents of the rental car company because another agent of the company (Marcia), acting within her actual authority, has made manifestations (attributable to the company) that the company (as principal) desires the employees to act on the company's behalf and subject to the company's control. See Figures 2-3 and 2-4.

Agency law handles such complexity in characteristic fashion. It establishes categories, labels the categories, and attaches consequences to the categories. In matters of contract and communication, the key labels are superior agents, subordinate agents, and subagents.\textsuperscript{110}

\textsuperscript{110} Neither the R.2d nor the case law provides any names for these important links in the chain of agency authority. For the first edition of this book, the author coined the terms "intermediary" and...
Figure 2-3. Concatenating Authority—The Practical Structure

"subordinate." R.3d uses the terms "superior and subordinate co-agents"; §1.04(9) and this edition follows that usage.
§2.8.2 Superior and Subordinate Agents

As section 2.8.1 illustrates, a principal can use one of its agents to appoint, direct, and discharge other agents of the principal. Using "superior agents" to deal with "subordinate agents" is merely a specific instance of a principal acting through its agents. The principal uses one (or more) of its agents to manifest its desires to the principal's other agents.

This concatenated, hierarchical structure is commonplace. Only the smallest of organizations can operate without the "top dog" delegating some responsibility to superior and subordinate agents. Moreover, the delegation often works through several levels (in military terms, the "chain of command"), with agents being simultaneously superior agents vis-à-vis those "below" them, and subordinate agents vis-à-vis those...
"above" them. Superior agents and subordinate agents are "co-agents" of the principal. A subordinate agent is never the agent of a superior agent.

<EXT>Example: Marcia's actual authority to run the airport office might derive as follows: The car company's regional manager appointed her to the position, and generally described to her the duties and authority of the position. The regional manager obtained the actual authority to make such manifestations on behalf of the company when the Vice President for Leasing Operations appointed him to the regional manager position. The Vice President, in turn, obtained her actual authority to manifest the company's choice of regional managers (and to manifest the company's wishes as to the duties and authority of those managers) when the Chief Executive Officer appointed her as Vice President and outlined the duties and authority of that position. The company made the necessary manifestations to appoint and authorize the CEO when the company's Board of Directors elected the CEO.111

See Figure 2-5.

<TEXT>Most often, superior and subordinate agents are part of the same organization, but the concepts apply as well when the one agent is part of the organization comprising the principal and the other is not.

<EXT>Example: International Diversified Operations, Inc. ("IDO"), does not have its own sales force, but instead relies on independent agents who work on commission and have specified authority to accept purchase orders on IDO's behalf. IDO appoints Asif, one of IDO's employees, as national sales director, with authority to issue instructions to the independent agents. Asif is a superior agent, and the independent agents are subordinate agents.

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111 As to the conduct of a corporation's day-to-day affairs, the board of directors has the ultimate authority and power. See, e.g., Revised Model Business Corporation Act, §8.01(b) ("All corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors....")
Regardless of whether superior and subordinate agents are part of the same organization, and no matter how much authority and discretion a superior agent has, the superior agent acts on behalf of the principal and not on the agent's own account. So long as a superior agent acts with actual authority, apparent authority, or inherent agency power, the superior agent's manifestations—whether to the subordinate agents or to third parties—are attributable to the principal.
A subordinate agent binds its principal under the same rules applicable to "plain" agents. The key questions are therefore the same; namely, did the subordinate agent act with actual authority, apparent authority, inherent agency power, under circumstances giving rise to estoppel? Answering these questions involves looking at the conduct attributable to the principal, including any manifestations made by superior agents within the scope of their actual authority, apparent authority, or inherent agency power.

Example: Marcia, the manager of the rental car company's airport office, has engaged Abitatruth, an ad agency, to develop advertising for the rental car company. Marcia brings along Sara, one of her assistants, to a series of conferences with Abitatruth. During these conferences Marcia repeatedly seeks Sara's opinion as to choices posed by the ad agency and occasionally defers to Sara's judgment. Later, when the ad agency cannot get in touch with Marcia, it asks Sara to approve the content of several advertising posters. Although Marcia has stated privately to Sara that Marcia plans to approve all posters, Sara tells the ad agency, "Go ahead."

This approval binds the rental car company. Although Marcia's private statements to Sara preclude a claim based on actual authority, Sara did have apparent authority. Apparent authority presupposes a manifestation of the rental car company, which Marcia's conduct supplies. Consulting with and relying on subordinates—even in the presence of others—was certainly within Marcia's actual authority. That conduct is therefore, by attribution, the conduct of the rental car company. Coupled with the ad agency's resulting reasonable belief in Sara's authority, this attributed manifestation gave Sara apparent authority to approve the posters on the rental car company's behalf.

Superior Agent's Limited Responsibility for the Misconduct of Subordinate Agents

All agents owe a duty of care to their principal and superior agents must exercise care in selecting, directing, and discharging subordinate agents. If a superior agent fails to do so and that breach of duty proximately causes injury to the principal, the superior agent is liable to the principal for resulting damages.

Example: Marcia hires Henry to drive the courtesy van that takes passengers between the airport and the car rental office. Marcia carelessly fails to check Henry's references and driving record. The references are false, and the record includes several drunk-driving convictions. One day Henry drives the van while drunk and causes an accident. Under the doctrine of respondeat superior, the car rental company is liable for any damage Henry caused to others. Marcia is liable to the car rental company for its obligations to others, plus any damage to the company's

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112 See section 4.1.4.
113 See section 3.2.
courtesy van. She breached her duty of care in selecting and supervising a subordinate agent.

A superior agent is not, however, the guarantor of the subordinate agent's performance.

Example: Same situation, except Henry's references are okay, his driving record is clean, and Marcia uses reasonable care in hiring and supervising Henry. The car rental company remains liable to others for harm caused by Henry's drunken driving, but Marcia is not liable to the car rental company.

§2.8.3 Subagents

The Category

When a principal engages an agent to perform a task, the principal has in effect delegated the task to the agent. If the agent, acting with authority, in turn delegates part or all of that task to an agent of its own, then the second agent becomes a subagent of the original principal.

Restatement on Point: P retains A, a real estate broker, to sell Blackacre. P knows that A employs salespeople to show property to prospective purchasers and to state the terms on which the property is for sale. The salespeople are A's employees, not P's employees. The salespeople are also P's subagents.114

The Agent's Authority to Further Delegate

In theory, an agent has no authority to delegate its tasks to its own agents. However, a principal can authorize its agent to delegate, and, when the agent is a limited liability company, corporation, or other legal entity, some authority to delegate is inescapably implied. Legal "persons" can act only through the endeavors of natural persons.

The general rules for creating actual authority apply to determine whether an agent has authority to re-delegate to its own agents.115 Consistent with those rules, implied actual authority to delegate exists when: (i) the delegation relates merely to the mechanical aspects of the agent's tasks; (ii) the agent is a corporation, partnership, limited liability company, or other organization; or (iii) it is customary for agents in similar situations to delegate. The principal can of course override these implications with an express manifestation, but where the agent is an organization some delegation is inevitable.

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114 This Example is taken verbatim from R.3d, §1.04, Ill. 4.

115 Recall that if the delegation is to another agent of the principal (rather than to an agent of the agent), subagency is not involved. Instead, the "redelegator" is a superior agent, delegating to a subordinate agent.
Example: Sylvia, a rock singer, retains David, a well-known agent, to arrange on her behalf the facilities and amenities to be made available to Sylvia on an upcoming tour. David has several assistants, and they normally handle such "logistical details." Sylvia, however, says, "I want your personal touch on this. Don't let anyone else work on it." David has no authority to delegate the work.

Example: Sylvia, a rock singer, retains Pauline's Representation, Inc. ("Pauline's"), to arrange bookings. Pauline's is a limited liability company, with the necessary right to delegate the task. Sylvia, however, imposes a restriction, saying, "Make sure whoever works on my account has been with you for at least five years."

A Subagent's Power to Bind the Principal

The R.2d and R.3d differ in their approach to this issue. The R.2d approach is more elaborate and more precise. Assuming that an agent has the authority to delegate tasks to a subagent, under the R.2d determining the scope of a subagent's power to bind the principal in contract involves a two-stage analysis:

1. What is the scope of the agent's power to bind the principal?
2. Of that scope, what has the agent authorized the subagent to perform?\(^{116}\)

Example: The car rental company (acting via Marcia) gives Abitatruth actual authority to spend up to $10,000 in renting advertising space [stage 1]. Moe is a junior vice president of Abitatruth, with actual authority (from Abitatruth) to make leasing commitments of $1,000 or less [stage 2]. Moe has neither apparent authority nor inherent agency power to exceed the $1,000 limit while acting for Abitatruth [stage 2]. Moe purports to commit the car rental company to space Alpha for $800 and to space Beta for $1,250.

In each instance, Moe has acted as an agent for Abitatruth and subagent for the car rental company. The commitment on space Alpha binds the car rental company, because the commitment was within Abitatruth's authority vis-à-vis the company [stage 1] and within Moe's authority vis-à-vis Abitatruth [stage 2]. The commitment on space Beta does not bind the car rental company, because that commitment exceeded Moe's authority vis-à-vis Abitatruth [stage 2]. In sum, to bind the principal under the R.2d, a subagent's act must be both within the subagent's power to bind the agent and within the agent's power to bind the principal.

The R.3d approach has the virtue of simplicity:

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\(^{116}\) R.2d, §5, comment d.
As between a principal and third parties, it is immaterial that an action was taken by a subagent as opposed to an agent directly appointed by the principal. In this respect, subagency is governed by a principle of transparency that looks from the subagent to the principal and through the appointing agent. As to third parties, an action taken by a subagent carries the legal consequences for the principal that would follow were the action instead taken by the appointing agent.117

Unfortunately, this approach also has the defect of indeterminacy. Surely not every act of a subagent binds the principal, especially not acts that would not bind the agent.

Agent as the Guarantor of the Subagent's Performance

When an agent delegates all or part of its responsibilities to a subagent, the agent remains "on the hook" to the principal. Delegation does not relieve the agent of its responsibilities. If the subagent's performance satisfies the obligations the agent owes to the principal, then the agent, acting through the subagent, has performed its responsibilities as agent. If, however, the subagent's performance fails to satisfy the agent's obligations, then the agent is directly responsible to the principal.118

§2.8.4 Distinguishing Subordinate Agents from Subagents

The concepts of subordinate agent and subagent both presuppose a hierarchy with:

- <BL>the principal at the top,
- the subordinate agent or subagent at the bottom, and
- an intermediary (either a superior agent or an agent) in between.

Nonetheless, the two concepts reflect very different relationships with very different legal consequences. It is therefore important to distinguish one relationship from the other.

The crucial point of distinction is the manifestation that the principal makes to the intermediary. Ideally at least, that manifestation, reasonably interpreted, will lead the intermediary to believe either that:

- <BL>the principal wishes the intermediary to retain or supervise another agent of the principal—in which case the intermediary is to be a superior agent, the other agent is to be a subordinate agent, and both the superior and subordinate agents are to be co-agents of the principal; or

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117 R.3d, §3.15, comment d.
118 The rule stated here closely parallels a rule of contract law: When an obligor delegates its performance obligations to another, that delegation does not by itself discharge the obligor's duties to the obligee.
• the principal wishes to retain the intermediary as the principal's agent and recognizes that the agent may delegate some or all of its responsibility to another person—in which case that other person is an agent of the agent and simultaneously a subagent of the principal.

<EXT>Example: A landlord retains a management company to manage 150 separate apartment buildings owned by the landlord. The landlord wants a resident manager in each building and expects these caretakers to be employees of the management company. The managers will be agents of the management company and subagents of the landlord.

<TEXT>Superior and subordinate agents are usually part of the same company, as in the Examples in sections 2.8.1 and 2.8.2 involving Marcia and the car rental company. However, that circumstance is not an element of the superior/subordinate agent analysis.

<EXT>Example: The management company's contract with the landlord has significantly increased the company's obligations, and the company needs interim help recruiting and supervising resident managers. On an interim basis, the management company retains Carolyn, an experienced real estate attorney, to interview applicants for caretaker positions, and gives her authority to hire applicants she considers appropriate. The management company also retains Carolyn to supervise the applicants she hires. Like her, the caretakers she hires will be agents of the management company. When she supervises, she will be acting as a superior agent vis-à-vis subordinate agents.

<EN>PROBLEM 1

<TEXT>Captain Miles Standish loved the fair damsel Priscilla, but Standish's intense shyness prevented him from speaking to her. One day Standish lamented the situation to his friend John Alden, and Alden offered to speak to Priscilla and, on Standish's behalf, invite her to an upcoming community dance. Standish responded, stroking his beard reflectively, "I dunno. That might be a good idea." Alden took that comment as assent and rode off to see Priscilla. Actually, however, Standish did not intend to consent. Right after Alden rode off, Standish wrote in his diary, "Told Alden that I would think about his offer. Have done so and will reject it as soon as I next see him."

Before Standish saw Alden again, however, Alden saw Priscilla. Alden explained Standish's great love, and—purporting to act on Standish's behalf—invited Priscilla to accompany Standish to the dance. Priscilla accepted. Later, Standish saw Alden and told

<FN>119 Unlike Carolyn, the resident managers will probably also be servants of the management company. See section 3.2.2. However, that distinction is immaterial here.
him not to talk to Priscilla. Alden told Standish, "Too late, fellow; you're going to the
dance."

Assume that, as a matter of contract law, contracts to attend dances are valid and
enforceable. Is Standish bound?

**<E>Explanation**

**<TEXT>**Standish is bound only if Alden had actual authority to extend the invitation.\textsuperscript{120} The creation of actual authority requires (i) a manifestation by the principal, (ii) the
agent's reasonable interpretation of that manifestation as a request that the agent acts for
the principal, and (iii) the agent's manifestation of consent to act. The first and last
certainly occurred. Standish's comment ("That might be a good idea") suffices as a
manifestation. Alden's action reflects his consent. The question of the agent's
interpretation, however, is more difficult. Although Standish's subjective intent is
irrelevant, Standish's response was objectively ambiguous. Especially given what Alden
knew of Standish's shyness, it was probably unreasonable for Alden to consider himself
**<TEXT>**authorized without having first sought clarification. Therefore, no actual
authority existed and Standish is not bound on the contract.

**<EN>PROBLEM 2**

**<TEXT>A tenant rents her apartment on a month-to-month tenancy, with each term
beginning on the first of the month. Under local law, the tenant can terminate the tenancy
by giving a full calendar month's notice. For example, for the tenancy to end on March
31, the tenant must give notice before March 1. A resident manager, whom the landlord
has authorized to receive notices from tenants, manages the building. On December 28,
the tenant gives proper notice to the resident manager, stating that the tenant will vacate
by January 31. Unfortunately, the resident manager fails to pass the notice on to the
landlord until January 3. Will the tenancy end on January 31?**

**<E>Explanation**

**<TEXT>**Yes. When an agent has actual authority to receive a notice, receipt of that
notice is attributable to the principal. The agent's failure to communicate the information
to the principal may be a breach of the agent's duty to the principal\textsuperscript{121} but has no effect on
the attribution rule.

**<EN>PROBLEM 3**

\textsuperscript{120} Since there is no indication of Priscilla's being aware of any manifestation by Standish, there can be no
apparent authority. Since Alden is not a general agent, there can be no inherent power. Since Priscilla has
not changed position to her detriment, there can be no estoppel. (The facts do not indicate that she has
bought a new dress or rejected other invitations.)

\textsuperscript{121} See section 4.1.5.
A gay man, well known as a gay rights advocate, seeks to buy a house for sale in a fashionable neighborhood, but fears that the owner, a well-known opponent of gay rights, will refuse to sell to him. The would-be buyer therefore secretly authorizes a friend to negotiate and consummate the purchase, ostensibly in the friend's name. It never occurs to the seller that the ostensible purchaser might be a front, and the seller asks no questions to that effect. The friend of course makes no comment on the subject. At closing the seller learns that the gay man is the undisclosed principal. Is the seller obliged to go through with the sale?

Explanation

Yes. Although both the agent and the undisclosed principal had reason to know that the third party would have refused to deal with the principal, there was no affirmative misrepresentation.\footnote{This Example assumes the transaction is not subject to a law prohibiting discrimination on account of sexual orientation.}

PROBLEM 4

Mr. and Ms. Yup, high-power corporate lawyers, mesh their schedules and arrange a week's vacation hiking in the Andes Mountains. To babysit their offspring ("Little Yup") and to housesit their house, the Yups hire a babysitter ("Babysitter"). The Yups provide the babysitter, among other information, the name, office phone number, and office address of Little Yup's pediatrician. They also leave a health insurance card that indicates a health insurance account number for Little Yup. Unfortunately, while the Yups are away, Little Yup becomes seriously ill. The babysitter takes Little Yup to the hospital, where expensive medical procedures enable Little Yup to recover. In order to have the hospital provide the services, Babysitter shows the health insurance card and signs a contract with the hospital. Queried about the child's parents, Babysitter responds, "They're backpacking in the Andes. I am babysitting for their child for this week." Babysitter signs the hospitalization contract: "I.M. Babysitter, for Mr. and Ms. Yup." Are Mr. and Ms. Yup bound on that contract?

Explanation

The Yups are bound, certainly on actual authority and perhaps on apparent authority as well. Merely by entrusting the child to Babysitter for a week and leaving the country, the Yups manifested consent to have Babysitter arrange for necessary medical care. Providing the name of the pediatrician and the health insurance card reinforced that basic manifestation. The Yups did not specifically mention hospitalization and did not specifically authorize Babysitter to sign hospital contracts on their behalf, but Babysitter certainly had implied actual authority to arrange hospitalization in an emergency and to sign all reasonably necessary documents for that purpose.
The argument for apparent authority is also strong. The hospital must be able to point to some manifestation of the Yups that, reasonably interpreted, led the hospital to believe that Babysitter was authorized to bind the Yups. The hospital can identify three manifestations: the Yups' entrusting of their child to Babysitter; the Babysitter's possession of the insurance card; the Babysitter's statement about her responsibilities. The first manifestation arguably establishes apparent authority by position, although babysitters do not customarily commit parents to large hospital bills. The possession of the insurance card made it more reasonable for the hospital to believe that the parents had given Babysitter authority to arrange for medical services. It is the third manifestation—Babysitter's statement—that is perhaps the strongest point. Had that statement been made directly by the Yups, there would have been no question of Babysitter's apparent authority. When Babysitter accurately described her authority, she was acting within her actual authority. As a consequence, her statement had the same effect as if the Yups had made it themselves.

<EN>PROBLEM 5

Pickwick owns an antique store that occupies the first three floors of a four-story brownstone. Pickwick lives on the fourth floor, has security cameras throughout the first three floors, and has a rather lackadaisical attitude toward maintaining personal surveillance over the store premises. He customarily leaves the store door unlocked even when he is upstairs having lunch or taking a nap. A large sign just inside the store entrance advises: "For assistance, pull on cord to ring bell."

One day, two newlyweds enter the store and are promptly approached by a respectable-looking lady who identifies herself as "Mrs. Pickwick." With Mrs. Pickwick's assistance, the newlyweds examine several large antiques and decide to purchase two of them. The newlyweds give Mrs. Pickwick $200 in cash as a down payment and arrange for a delivery day. Mrs. Pickwick takes from a rolltop desk a sheet of letterhead for "Pickwick & Company" and writes out a receipt. "Mrs. Pickwick" is in fact an imposter. Is Mr. Pickwick bound to the purported contract? If not, is Mr. Pickwick obliged to make good the $200?

<EXPLANATION>

Although the imposter lacked actual and apparent authority, Mr. Pickwick is probably liable via estoppel at least for the $200. The newlyweds "changed their position because of their belief that the transaction was entered into...for" Mr. Pickwick, and Mr. Pickwick "carelessly caused such belief" through his lackadaisical attitude toward

<FN> No manifestation attributable to Mr. Pickwick, the principal.
security. At minimum, the newlyweds are entitled to their reliance damages and perhaps to their expectation interest as well.

PROBLEM 6

Henry comes to town one day looking for some land to purchase. He learns that Eleanor has a parcel of lakefront property that she wishes to sell. Henry meets Eleanor, explains that he is "in town acting for a group of investors who are looking for lakefront in this area," and goes with Eleanor to inspect the property. Henry appears impressed, but says to Eleanor, "I'm just the gofer. I'll have to check with the folks in charge." The next day Henry comes back and tells Eleanor that he is authorized to pay her $70,000 for the property. Eleanor thinks the price is a fair one, and together they go to a local stationery store and buy a legal form titled "Contract for the Sale of Land." They fill in all the blanks, Eleanor signs as seller, and Henry signs as "agent for the Aquitaine Corporation, Buyer." As completed and signed, the contract indicates that, on behalf of Aquitaine Corporation, Henry has put $100 down and that the corporation will deliver the rest of the purchase price within 30 days.

Two weeks after the contract is signed, Eleanor sees Henry walking down a street in town. Walking with Henry is a man whom Henry introduces as Richard, president of the Aquitaine Corporation. (This man is indeed Richard, and Richard is indeed president of Aquitaine.) After casual remarks about the weather, Eleanor asks, "Does Henry do a lot of work for your corporation, Richard?" Richard responds, "We've used him on a number of occasions. He's quite a go-getter."

Thirty days pass after the signing of the contract, and Eleanor receives no payment. When she contacts the Aquitaine Corporation, it denies that Henry was authorized to act on its behalf. It truthfully states that: (i) it never made any manifestation to Henry regarding Eleanor's parcel, and (ii) Henry never had any ongoing responsibilities with Aquitaine but instead occasionally received specific assignments. Aquitaine denies any responsibility for the Eleanor—Henry transaction and flatly refuses to pay.

Henry being nowhere to be found, Eleanor brings suit on the contract against Aquitaine Corporation. Assume that the "equal dignities" rule does not apply in the jurisdiction. Assume also that Richard's comments to Eleanor are attributable to Aquitaine. What result in Eleanor's suit?

Explaination

Eleanor will lose. She will be unable to attribute Henry's actions to Aquitaine.

Since Aquitaine never made any manifestation to Henry regarding Eleanor's parcel, actual authority did not exist. Since Henry's role with Aquitaine never involved any "continuity of service," he was never a general agent. Consequently, he had no inherent

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124 R.2d, §8B(1)(a), discussed in section 2.5. See also R.3d, Ch. 2, Topic 4, Introduction.
agency power to enter into contracts on Aquitaine's behalf. The doctrines of apparent authority and estoppel are Eleanor's only hope, and that hope is forlorn.

The problem with apparent authority is one of timing: The apparent principal's manifestation came too late. To establish apparent authority, Eleanor must show some conduct attributable to Aquitaine that \textit{as of the moment of contract formation} caused her to reasonably believe that Henry had authority. Until just prior to the execution of the form contract, Eleanor did not even know who the supposed principal was. Even when Henry disclosed Aquitaine's identity, Eleanor's inference that Henry had authority was based solely on Henry's remarks, not on any conduct of Aquitaine.

In some circumstances, an apparent principal's silence in the face of an apparent agent's known conduct will suffice as a manifestation. However, in this case there is no indication whatsoever that at the time of contract formation Aquitaine Corporation was aware of Henry's claim of agency status.

The conversation between Eleanor and Richard cannot salvage the situation for Eleanor. Even if Eleanor reasonably interpreted Richard's comments to mean that Henry had authority, there remains the problem of timing. Even under the Restatement view, the claimant must link the manifestation to a reasonable belief that existed \textit{as of the moment of the relevant act}. A post hoc manifestation cannot justify an ante hoc belief. By the time Eleanor spoke with Richard, Eleanor had already executed the contract.

The Eleanor—Richard conversation will be likewise unavailing for a claim of estoppel. Even assuming that Richard's casual remark "intentionally or carelessly" caused Eleanor to believe that Henry had acted with authority,\textsuperscript{125} that belief did not cause any relevant harm. Eleanor had already signed the contract. Unless she can show that she suffered some additional prejudice subsequent to her conversation with Richard (e.g., turning down another potential buyer), she cannot establish estoppel.\textsuperscript{126}

\textbf{PROBLEM 7}

\textbf{TEXT} A small real estate company is planning to rent office space to an entrepreneur who needs "a place to hang my hat, pick up my mail, and get telephone calls." The real estate company's premises are small and its phone system very basic. The entrepreneur's calls will come through the main switchboard without a dedicated line, and her desk will be located in the same open space used by employees of the company. How can the real estate company minimize the chances that it will be held responsible for its tenant's dealings with third parties?

\textbf{Explanation}

\textsuperscript{125} Restatement, \S 8B(1)(a), discussed at section 2.5.

\textsuperscript{126} To assert that Richard's comments caused ratification is too much of a stretch. Ratification requires a manifestation of affirmance, and the purported principal's manifestation must relate specifically to the unauthorized act being ratified.
Perhaps the most important safeguard is to expend the time and effort necessary to check into the *bona fides* of the would-be tenant. Problems will arise only if the entrepreneur cheats her customers or suppliers.

As for the agency law analysis, apparent authority is the key concept. Under that concept, the main risks would come from (i) ambiguous manifestations by the real estate company, and (ii) reasonable misinterpretations by third parties. Due to the limitations of the phone system and the office setup, certain manifestations are inherent in the proposed arrangement. The key, therefore, is to preclude reasonable confusion. The safest approach is to make sure that an appropriate clarification accompanies each potentially confusing manifestation. For example, when the receptionist receives a call for the entrepreneur, the receptionist should use a greeting that indicates that the real estate company does not employ the entrepreneur. As for the office setup, a sign on the office entrance should indicate the entrepreneur's independent, unassociated status.

**PROBLEM 8**

For several years, a local band has played mostly for free at various local venues, seeking thereby to gain the experience and exposure and "break through" to paying opportunities. For the past two years, the band has relied on Oliver, its unpaid manager, to arrange its bookings.

Over the past several months, due to the band's increasing popularity, Oliver has been able to arrange modest fees for each performance. As is customary in the locality, payment is made immediately after each performance.

Last week, success created problems, as Oliver insisted on a percentage of future fees, the band told him no, he objected, and at 10 P.M. the band "fired" him. The next morning, at 10 A.M., Oliver went to a bar at which the band had previously played several times for free, as arranged by Oliver. On this occasion, Oliver (i) purported still to be the band's manager; (ii) persuaded the bar to pay a performance fee of $500; (iii) insisted on collecting $100 in advance; (iv) succeeded with that insistence, due to the band's increasing popularity; (v) pocketed the money; and (vi) never told the band anything. Is the band obligated to perform? If the band does not perform, is the band obligated to "return" the $100 to the bar?

**Explanation**

As a matter of agency law and lingering apparent authority, the band probably is bound to the contract made by Oliver purportedly on its behalf. If so, (i) contract law determines the bar's remedy if the band breaches its obligation; and (ii) at minimum, the bar will have a claim for restitution of the $100 advance payment. If the band is not obligated to perform, the band is not liable for the $100.

Obviously, Oliver's actual authority ended when the band fired him. However, his apparent authority lingered as to the bar, which had previously dealt with the band through Oliver. By performing in the past as arranged by Oliver, the band manifested to the bar that Oliver was authorized to act on its behalf. Because the bar neither knew nor
had reason to know of the split between Oliver and the band, that manifestation supports a claim of lingering apparent authority.

Oliver's pocketing of the money is irrelevant to the claim; apparent authority applies to a faithless or even fraudulent apparent agent. However, the band might argue that both the fee and the requirement of an advance payment triggered a duty of inquiry.

The first of those arguments is make-weight. Except in unusual circumstances, the authority to arrange for free performances certainly suggests the authority to arrange for compensated performances.

The advance payment requires a more complex assessment. Although advance payments are not customary, the bar evidently considered it reasonable in these circumstances to make an advance payment. Why, then, would it be unreasonable for the bar to believe that the band had authorized its manager to collect the advance payment?

If Oliver had lingering apparent authority, the band is obligated on the contract. At minimum, restitution is available, because, given Oliver's apparent authority to collect the money, his receipt of the money is treated as if the band itself had received it.

However, if Oliver lacked apparent authority to bind the band to the contract, the band is also free of any responsibility for the $100. No apparent authority means no imputation to the band of Oliver's receipt of the money. 127

<EN>PROBLEM 9

Jeffrey is a buyer's broker in the recycled newspaper business. On behalf of various newsprint manufacturers, he locates and purchases recycled newspapers. Each time Jeffrey makes a purchase, he is acting on behalf of a particular customer. He nonetheless makes each purchase in his own name.

For the past five years, one of Jeffrey's customers has been Amalgamated Newsprint. During that time Jeffrey has made about four purchases per year for Amalgamated. On each occasion Jeffrey and Amalgamated have followed the same procedure: Amalgamated places an order with Jeffrey, stating a quantity and a maximum price. When Jeffrey finds the necessary newspapers, he purchases them in his own name and informs Amalgamated of the delivery date and price. Amalgamated then wires funds to Jeffrey, and Jeffrey pays the vendor. A commission structure rewards Jeffrey for bringing an order below the maximum allowed price. Jeffrey understands that he is not authorized to make any purchases for Amalgamated without first having an order in hand.

Nonetheless, after five years Jeffrey has begun to anticipate Amalgamated's needs. Last week he saw a great purchase opportunity and, expecting an order from Amalgamated, he agreed to make the purchase. Although, as always, Jeffrey made the purchase in his own name, he noted the purchase on his books as "for Amalgamated." If Jeffrey is unable to pay for the purchase, can the vendor enforce the contract against Amalgamated?

127 The facts do not support a claim for agency by estoppel. There are no facts to suggest that the band had reason to suspect that Oliver would respond to his firing by acting dishonestly, and the short time between the firing and Oliver's dishonesty negates any suggestion that the band was dilatory in informing the past customers of the change in Oliver's status.
Explanation

Probably not. Since Jeffrey lacked the right to purchase for Amalgamated without first having an order and since Amalgamated was an undisclosed principal, neither actual nor apparent authority apply. Also, since there is no evidence that Amalgamated knew of Jeffrey’s conduct in this instance or was careless, there can be no estoppel.

The vendor's only hope is inherent agency power. The vendor must (i) label Jeffrey as Amalgamated's general agent, (ii) delineate Jeffrey's agency function as acquiring newspaper for Amalgamated on an ongoing basis, and (iii) characterize the purchase contract as "usual or necessary" to Jeffrey's authorized activities.128

The vendor will likely fail in all three respects, because it will fail in the first. Jeffrey is not a general agent. He is not "authorized to conduct a series of transactions involving a continuity of service."129 To the contrary, he receives and needs separate authorization for each individual transaction. As a result, Jeffrey has no "ongoing" authorized responsibilities and the unauthorized purchase was not "usual or necessary" to any authorized activity.

PROBLEM 10

Jeffrey makes the unauthorized purchase described in Problem 9, but in doing so tells the vendor that the purchase is being made on behalf of Amalgamated. Jeffrey then calls Amalgamated and reports his "great find." Amalgamated shocks Jeffrey by saying, "Nothing doing. No order with us, no deal from us."

Jeffrey immediately contacts the vendor, seeking a brief delay on delivery. "I bought this for a customer," he explains, "and I didn't exactly have their okay in advance. They're balking a bit. I've got to make nice with them." Jeffrey then calls Amalgamated again, apologizes profusely, and extols the benefits of this bargain. After a 45-minute conversation, Amalgamated relents and says, "All right. We'll take it."

Jeffrey immediately calls the vendor back and says, "No problem. We're fine." The vendor responds, "I'm fine anyhow. As soon as I learned that you were a go-between and had no authority, I went looking for another buyer. Just two minutes ago I sold the goods to somebody else."

Can Amalgamated enforce the original agreement against the vendor?

Explanation

No. Amalgamated did eventually affirm Jeffrey's unauthorized act, and ordinarily that affirmance would bind both the vendor and Amalgamated to the contract. In this instance, however, the vendor can avoid the ratification. In reliance on Jeffrey's

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128 R.2d, §194 (inherent agency power of general agent of undisclosed principal), discussed at section 2.6.2.
129 R.2d, §3(1) (general agent defined), discussed at section 2.6.2.
lack of authority, the vendor changed its position and bound itself to another buyer. The fact that Amalgamated ratified before that change in position took place is irrelevant. What matters is that the vendor changed position before learning of the ratification.

<EN>PROBLEM 11

Elvira enters into an oral contract with three entrepreneurs who are founding a community theater. The contract calls for Elvira to begin work managing the theater on March 1, 2009, and to work in that capacity for one year. All parties understand that the entrepreneurs plan to form a corporation to own the business and that the corporation will take over Elvira's contract.

March 1, 2009
Elvira begins work as manager.

May 1, 2009
The entrepreneurs form Community Theatre, Inc. ("CTI"), and elect themselves as the board of directors. Acting as the board, they appoint Roberta as chief executive officer and formally (albeit orally) agree to have CTI "take over the management contract with Elvira."

May 2, 2009
Roberta informs Elvira of CTI's formation, Roberta's appointment as CEO, and the board's action to take over Elvira's contract. Roberta says, "As of now, your management contract is with CTI."

May 31, 2009
Elvira receives her monthly salary check, this time drawn on a CTI checking account.

June 30, 2009
Elvira receives her monthly salary check, drawn on a CTI checking account.

July 10, 2009
Roberta terminates Elvira as manager.

Elvira subsequently sues CTI for breach of contract, asserting that under the contract CTI was obligated to continue her employment through February 29, 2010. CTI defends in part invoking the statute of frauds, noting that the original agreement contemplated performance that would extend more than one year beyond the making of the contract.

Elvira responds that: (a) the original agreement with the three entrepreneurs may have been within the statute, but she is not suing them; (b) when CTI "took over" the contract, the contract called for less than a year of performance; and therefore (c) the statute of frauds does not apply to CTI's obligations.

CTI rejoins that: (i) by "taking over" the contract, CTI ratified the original agreement; (ii) ratification relates back to the time of the action being ratified; and therefore (iii) CTI's ratification results in a contract that is within the statute of frauds.

Who is right?

<EXPLANATION>
Elvira. A party can ratify a prior act only if the party existed at the time of the act. A corporation can therefore never ratify an act taken on its behalf before the corporation came into existence.

**PROBLEM 12**

The board of directors of Rollerskating, Inc., adopts a resolution authorizing the CEO "to appoint such officers, managers, and employees of the corporation as the CEO deems appropriate, and to prescribe their respective duties, subject only to the numerical limits established by the board of directors from time to time." Aware of the resolution, Rollerskating's CEO appoints Rachael to be its purchasing agent. The CEO provides Rachael with a four-page memo outlining the internal approvals necessary before Rachael may place an order. For instance, orders costing less than $50,000 can be approved by the CEO; orders costing less than $25,000 may be approved by any vice president; orders costing less than $5,000 may be approved by any department manager. Rachael receives a request from a vice president to order a Model 5400 Wodget from Samuel Equipment Corporation ("Samuel Equipment") at a price of $15,000, and she places the order. Does the order bind Rollerskating?

**Explanation**

Yes. In placing the order, she is acting with the reasonable belief that she is authorized to do so. Her belief is based on manifestations from a superior agent (her appointment to the position of purchasing; the memo of internal procedures). Those manifestations are within the superior agent's actual authority and are therefore attributable to the principal. In short, Rachael has actual authority.

**PROBLEM 13**

Over the next three months, Rachael places several more orders with Samuel Equipment Company, each properly requested by a Rollerskating vice president and each costing between $10,000 and $24,000. In due course Samuel Equipment delivers the equipment and bills Rollerskating. The bills come to the Rollerskating comptroller, whom the CEO has made responsible for reviewing and approving for payment all invoices over $1,000. The comptroller reviews the invoices, notes that each order was properly authorized and has been fulfilled, okays the payment, and signs and sends to Samuel Equipment a payment for the invoiced amount.

Subsequently, Rachael is promoted out of the purchasing department and is replaced by Herman. Rachael's last responsibility as purchasing agent is to brief Herman on his new responsibilities. Rachael does so, directing Herman's attention to the CEO's memo on internal approvals. Herman reads the memo but promptly forgets its provisions.

The next day Herman receives a rush request to order another Model 5400 Wodget from Samuel Equipment Company at a price of $15,000. The request comes from a
department manager, not a vice president, but Herman places the order anyway. Does Herman's order bind Rollerskating?

**<E>Explanation**

**<TEXT>**After having read the CEO's memo, Herman lacked actual authority to place the order. He could not *reasonably* have believed himself authorized. He did, however, have apparent authority. Rollerskating is therefore bound.

The apparent authority arises from manifestations attributable to Rollerskating, Herman's principal. Those manifestations were (i) Herman's position as Rollerskating's purchasing agent, and (ii) Rollerskating's conduct on past orders placed with Samuel Equipment by a Rollerskating purchasing agent. On each prior occasion, Rollerskating's comptroller approved and sent payments. The comptroller was acting within her actual authority, so her actions are attributable to Rollerskating. The sequence of events—order from a purchasing agent followed by payment without protest—presumably led Samuel Equipment to believe that Rollerskating purchasing agents have authority to place such orders. In light of the past events, that belief was certainly reasonable.

Herman may also have had inherent agency power. He was a general agent, acting in his principal's interest. Ordering the Model 5400 could be seen as an act usual or necessary to serving Herman's authorized purpose.\(^\text{130}\)

**<EN>PROBLEM 14**

**<TEXT>**A large corporation is facing a large number of product liability suits venued around the country but involving the same product. For efficiency's sake, the corporation hires a large firm of experienced and expensive lawyers ("Big Firm") to serve as national coordinating counsel to the corporation. In that capacity, Big Firm acts on the corporation's behalf to (i) retain local counsel to represent the corporation in the various lawsuits, (ii) facilitate and coordinate the exchange of information and work product among the various local counsel, and (iii) to supervise the work of the local counsel.

Big Firm uses due care in carrying out its duties. Unfortunately, however, local counsel in one case commits discovery abuses that result in a $50,000 sanction being assessed against the corporation. Is Big Firm liable to the corporation for some or all of this amount?

**<E>Explanation**

\(^{130}\) In one respect, this explanation is unrealistically "flat." The third party, Samuel Equipment, has no mind in which to form or harbor beliefs and therefore cannot *directly* believe anything about Herman's authority. The relevant beliefs are those of Samuel Equipment's agents, which are attributable to their principal according to agency law. Whether those attributed beliefs are reasonable depends in part on what Samuel Equipment knows or has reason to know. Since Samuel Equipment cannot *directly* know anything, what it knows or has reason to know likewise depends on the attribution rules of agency law.
No, because local counsel is a subordinate agent of the corporation and not a subagent of Big Firm. Distinguishing between a subordinate agent and a subagent involves focusing on the manifestations of the principal. In this instance, the principal (the corporation) told the intermediary (Big Firm) to "retain local counsel to represent the corporation"; that is, to retain counsel to act as agents of the corporation. Therefore, Big Firm and local counsel are co-agents of the corporation, and Big Firm is a supervisory agent vis-à-vis local counsel. In that capacity, Big Firm is not the guarantor of local counsel's conduct and would be liable for local counsel's mistakes only if Big Firm had breached its duty of care in supervising local counsel.

**PROBLEM 15**

The _____ Law School Exam Conflict and Make-Up Policy, printed in the Student Handbook, states in part:

Students will take exams at the time and place announced in the exam schedule unless:

1. A student is prevented from taking the exams because of his or her illness or illness or death in the student's immediate family;
2. A student has two exams scheduled on the same day;
3. A student has three exams scheduled within a period of three calendar days;
4. A student has two exams scheduled to begin within 23 hours of each other;
5. A student has exceptional circumstances that, in the discretion of the Dean of Students, justify a rescheduling. Exceptional circumstances must relate to personal situations, not to a burdensome examination schedule.

No make-up exam will be given more than one week after the end of the regular exam period, except when such a delay is necessitated by illness or other exceptional circumstances.

No student shall take any exam before the regularly scheduled time for the exam.

On account of a serious illness in the immediate family, a student requests permission to reschedule an exam. Due to long-standing and significant employment responsibilities, the only practical time for the make-up exam is three days before the regularly scheduled time. The dean of students grants the request, and the student buys two nonrefundable airline tickets. The dean is aware that the student will be purchasing airline tickets but not that the tickets will be nonrefundable.
Subsequently, the professor whose exam is involved learns that an unidentified student will take a make-up in advance of the rest of the class. The professor objects and asserts that an advance make-up violates the policy quoted above. Has the action of the dean of students bound the college to allow the advance make-up?

**Explanation**

The dean can bind the college through some form of agency power (actual authority, apparent authority, inherent agency power) or through estoppel. In this matter, none of these attribution rules apply and the college is not bound.

For actual authority to exist, some manifestation of the principal must cause the agent to reasonably believe the agent has the right to bind the principal. The most salient manifestation given by the facts is the Student Handbook. That handbook expressly precludes the scheduling of advance make-ups. The dean's discretion, mentioned in item 5, relates to adequate cause for a make-up and does not override the subsequent, express prohibition on advance make-ups. The dean could not reasonably believe that he or she has the right to schedule advance make-ups.

For similar reasons, apparent authority will not help the student. For apparent authority to exist, some manifestation of the principal must cause the third party (here, the student) to reasonably believe the agent has the right to bind the principal. Arguably, at least, the dean's position constitutes a manifestation, as does the handbook's reference to the dean as the person who authorizes make-ups. However, those who rely on the appearance of authority have a duty of reasonable diligence. For a law student, that duty encompasses knowing the contents of the Student Handbook. Therefore, the student could not reasonably believe that the dean has the authority to violate the policy.

Inherent authority also will not help the student, even though the dean is a general agent (i.e., authorized "to conduct a series of transactions involving a continuity of service"). In some circumstances a general agent has the inherent power to bind its principal even through an unauthorized act. However, the power does not exist when the third party has reason to know that the act is unauthorized.

Estoppel is likewise unavailing. The student may have believed the dean to be authorized to permit an advance make-up, but, given the clear statement in the Student Handbook, the college cannot be said to have "intentionally or carelessly caused such belief." Moreover, through the Student Handbook, the college had taken "reasonable steps to notify [the student] of the facts."

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131 R.2d, §8B(1)(a), discussed in section 2.5.
132 R.2d, §8B(1)(b), discussed in section 2.5.