Resolving Disputes Arising from Unauthorized Corporate Security Contracts in China: The Role of Agency Rules

The court’s task is to do justice according to law. The courts, however, may not always have enough rules to go on. This problem may be more acute in emerging economies, where the legal infrastructure may be lacking. One of the vexed issues that PRC courts have confronted in recent years is how to allocate risks for unauthorized contracts that give a security made in the name of a company. The issue is vexed because of the lack of rules on the rights of the person seeking to deal with a company. This legal lacuna is partly the result of (i) the nature of the corporate authority-delegation mechanism under the PRC legal framework (that the company, in dealing with outsiders, is represented by, instead of agents, a legal representative or LR), and (ii) the incapacitation of the rules on apparent authority by, ironically, a company law provision enacted to regulate corporate security contracts.

This paper makes a discovery on, and an evaluation of, how China’s High People’s Courts have resolved the issues raised. The discovery is made by way of a review of two years’ worth of High People’s Courts decisions on the issue raised. The case review reveals, among other things, that (i) in about eight percent of the instances, the court has allocated the risk for unauthorized corporate surety transactions to the alleged surety, (ii) this decision outcome has been achieved through various court-made approaches that make sense neither in the context of the PRC legal system nor in the world (the majority line of decisions), and (iii) the outcomes of the remaining twenty percent of the cases have been reached by rules on agency, which are more justifiable on both doctrinal and policy levels (the minority line of decisions).

Should the agency rule approach then be adopted to resolve the issues raised? The answer would arguably be ‘yes’ but for one difficulty. This is that while transactions in the minority line of cases were mostly entered into by a purporting agent (not the LR), where an application of rules on agency raises no issues, the role of rules on agency is uncertain where the transaction is entered into by the LR. The paper makes an attempt to resolve this difficulty through an examination of the ways in which the same question is answered in Japan and Taiwan, where a similar corporate authority-delegation mechanism is adopted. The analysis concludes that the Japanese approaches, which are based on a statutory rule-buttressed understanding that the LR is the company, would not be applicable in the context of the PRC legal system. It argues that a balanced protection of the disputants may be achieved by adopting the Taiwan approach, under which third parties’ position is decided by an analogous application of the rules on unauthorized agency and apparent authority.