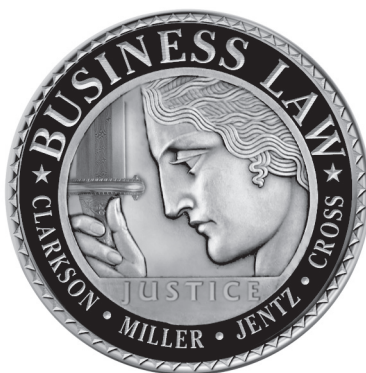


Chapter 32



Liability to Third Parties and Termination

☞ See Separate Lecture Outline System

INTRODUCTION

Once a principal-agent relationship has been created, attention often focuses on the rights of third persons who deal with an agent. This chapter discusses the rights of third parties when they contract with agents. A contract will make an agent's principal liable to a third party only if the agent had authority to make the contract or if the principal ratified, or was estopped from denying, the agent's acts. In other words, liability is determined by a careful examination of all the facts surrounding an agency relationship.

This chapter also discusses an agent's liability to third parties in contract and tort and a principal's liability to third parties because of an agent's torts. Again, liability is determined more by an examination of all the facts rather than looking merely at legal theory.

The chapter concludes with a discussion of how agency relationships are terminated. The material is generally self-explanatory and not difficult. It may be helpful to emphasize, however, that unless termination is by operation of law, a principal must give clear notice of termination to persons who dealt with the agent.

ADDITIONAL RESOURCES—

**AUDIO & VIDEO SUPPLEMENTS**

The following **audio and video supplements** relate to topics discussed in this chapter—

PowerPoint Slides

To highlight some of this chapter's key points, you might use the Lecture Review PowerPoint slides compiled for Chapter 32.

South-Western's Business Law Video Series

The situational video ***Employment Law*** illustrates some of the material included in this chapter.

Drama of the Law II

- Employer's Duty of Care and Issues of Compensation

CHAPTER OUTLINE**I. Scope of Agent's Authority****A. EXPRESS AUTHORITY**

Express authority is embodied in what a principal engages an agent to do. The text discusses here the equal dignity rule (which may determine when express authority must be in writing) and powers of attorney (which "is a written document and is usually notarized").

B. IMPLIED AUTHORITY

Implied authority is conferred by custom, inferred from an agent's position, or implied by virtue of being reasonably necessary to carry out express authority.

C. APPARENT AUTHORITY AND ESTOPPEL

Apparent authority exists when a principal causes a third party reasonably to believe that an agent has authority. If the third party changes position in reliance on the principal's representations, the principal may be estopped from denying that the agent had authority. The text includes examples that involve a pattern of conduct and an agent's possession of property.

CASE SYNOPSIS—

Case 32.1: Ermolan v. Desert Hospital

Desert Hospital in California established a comprehensive perinatal services program (CPSP) to provide obstetrical care to women who were uninsured. The CPSP was set up in an office suite across from the hospital and named "Desert Hospital Outpatient Maternity Services Clinic." The hospital contracted with a corporation controlled by Dr. Morton Gubin, which employed Dr. Masami Ogata, to provide services. Jackie Shahan was referred to the clinic by one of the hospital's emergency room physicians. Shahan's baby Amanda, was born with serious brain abnormalities. Amamda filed a suit in a California state court against the hospital, alleging "wrongful life." She claimed that a negligent

failure to advise her mother of her condition and the possibility of an abortion. The court ruled in the defendants' favor, holding that Drs. Gubin and Ogata were not the hospital's employees. Amanda appealed.

A state intermediate appellate court decided that Drs. Gubin and Ogata were "ostensible agents of the Hospital." The court noted the presence of "[t]he essential elements are representations by the principal, justifiable reliance thereon by a third party, and change of position or injury resulting from such reliance." The court affirmed the lower court's ruling, however, on Amanda's "wrongful life" claim, concluding that the physicians were not negligent in failing to advise Shahan to have an elective abortion.

Notes and Questions

Suppose that Drs. Gubin and Ogata had set up the "Desert Hospital Outpatient Maternity Services Clinic" with Desert Hospital's knowledge but without its consent. Would the decision with respect to "ostensible agency" have been different? Why or why not? Probably not, because "ostensible agency" or apparent authority exists when the principal cause a third party reasonably to believe that the agent has the authority to act. If the hospital had had no affiliation to the clinic, but had allowed it to operate under its name, a third party might have reasonably believed that the clinic and its physicians operated under the hospital's auspice.

ANSWER TO "THE ETHICAL DIMENSION" QUESTION IN CASE 32.1

Does a principal have an ethical responsibility to inform an unaware third party that an apparent agent does not in fact have the authority to act on the principal's behalf? A principal's ethical duty to notify a third party could depend on the specific circumstances. But if a principal acts to lead a third party reasonably to believe that an agency relationship exists, and the third party changes positions in reliance, it seems fair to impose legal liability on the principal. It seems likewise fair to hold the principal to an ethical responsibility to inform an unsuspecting third party in those same circumstances that no agency actually exists.

ANSWER TO "THE E-COMMERCE DIMENSION" QUESTION IN CASE 32.1

Could Amanda have established Drs. Gubin and Ogata's apparent authority if Desert Hospital had maintained a Web site that advertised the services of the CPSP clinic and stated clearly the physicians were not its employees? Explain. Yes. Although the physicians might have thereby established that they were not the hospital's employees, they could still have qualified as its independent contractors. An independent contractor can be a principal's agent..

D. EMERGENCY POWERS

When an emergency requires action to protect or preserve the property and rights of a principal, but an agent is unable to contact the principal, the agent has emergency power to act.

E. RATIFICATION

Ratification is a principal's affirmation of an agent's previously unauthorized act. An entire transaction must be ratified; a principal cannot ratify part and reject the rest. The require-

ments for ratification are summarized in the text. The text emphasizes in particular the knowledge of the principal—the principal must know all of the terms of a contract to ratify it.

II. Liability for Contracts

A. AUTHORIZED ACTS

1. Disclosed or Partially Disclosed Principal

A disclosed or partially disclosed principal is liable to a third party for a contract made by an agent acting within the scope of authority. If a principal is disclosed, an agent is not normally liable. If, however, a principal is partially disclosed, in most states either principal or agent may be liable.

2. Undisclosed Principal

If the principal is undisclosed, the principal and the agent are bound to the contract. If the agent pays, however, he or she is entitled to indemnification. The undisclosed principal may also hold the third party to the contract unless—

- The undisclosed principal was expressly excluded as a party in the contract.
- The contract is a negotiable instrument, and it does not show the agent signed in a representative capacity.
- The agent's performance is personal to the contract, allowing the third party to refuse the principal's performance.

B. UNAUTHORIZED ACTS

If an agent without authority contracts purportedly on behalf of a disclosed principal, the principal is not liable, but the agent is. When an agent acts without authority and the third party relies on the agency status, the agent's liability is based on the theory of breach of implied warranty of authority. If the third party knew that the agent was mistaken, or the agent indicated to the third party uncertainty, about the extent of authority, the agent is not personally liable for breach of warranty.

C. ACTIONS BY E-AGENTS

E-agents include semi-autonomous computer programs capable of executing specific tasks. The text asks about the authority of e-agents. The Uniform Electronic Transactions Act states that e-agents may enter binding agreements on behalf of their principals [UETA 15]. If an e-agent does not give an opportunity to prevent errors at the time of a transaction, the other party can avoid it.

ENHANCING YOUR LECTURE—



IS ONLINE ADVERTISING EFFECTIVE IF ONLY AN E-AGENT “VIEWS” IT?



E-agents are computer programs that are used in e-commerce to perform certain tasks. For example, an e-agent can be used to search the Web for the best price on a particular compact disc and then offer links to the appropriate Web sites. Some e-agents can locate specific products in online catalogues and actually negotiate the acquisition and delivery of the product. E-agents used for shopping on the Web are commonly referred to as “bots” or “shopping bots.” The fact that numerous e-agents are out there robotically shopping for people has caused problems in the online advertising industry.

INTERNET ADVERTISING AND “IMPRESSIONS”

The effectiveness of Internet advertising is dependent, of course, on how many people—that is, human beings—actually view an ad online. Internet advertising firms frequently charge for their services based on the number of “impressions” an ad generates. The advertising industry does not have a universal definition of the term *impression* however. Consequently, Internet publishers use many different methods to measure ad impressions. Some companies define an impression as a single ad that appears on a Web page when the page is displayed on a (human) viewer’s screen; thus, these companies filter out the times the ad is found by an e-agent. Other companies include visits by automated e-agents in their definition of impressions, even though no human consumer has actually viewed the ad.

THE GO2NET CASE

In the online environment, the actions of an e-agent can at times create liability (debt) for the business that hired an advertising firm. Consider, for example, the dispute in *Go2Net, Inc. v. CI Host, Inc.*^a A Web hosting company (Host) hired an Internet advertising company (Go2Net) to publish a certain number of “impressions” on the Internet. Payment for Go2Net’s services was to be based on the number of impressions. Host and Go2Net did not specify what they meant by “impressions” in the two contracts into which they entered, however. Host assumed that “impressions” referred to the number of times the ad was sent to a computer screen and viewed by a human. Go2Net counted as “impressions” all of the times that the ads were found by e-agents, such as Web crawlers or bots.

When the ads did not generate significant sales, Host canceled the advertising and refused to pay Go2Net for the number of “impressions” it claimed to have produced. Go2Net filed suit. Host argued that the term *impressions* was ambiguous and that the court should allow parol evidence to establish the parties’ intent. Host wanted the court to rewrite the contract so that the term meant only the number of times the ad was actually sent to a computer screen. The trial court granted summary judgment for Go2Net, and the appellate court affirmed on appeal. The appellate court recognized that Host had presented “undisputed evidence in the record that there is no single industry-wide accepted definition of ‘impressions.’” Nevertheless, a clause in the parties’ contract stated that “all impressions billed are based on Go2Net’s ad engine count.” Thus, Go2Net was allowed to count as impressions the number of times that e-agents found the Internet ad.

FOR CRITICAL ANALYSIS

What might have been the result if the parties had not agreed that the number of impressions would be based on Go2Net’s count? Would the court have allowed Host to reform the contract to exclude from the number of impressions the times that e-agents found the advertisement?

^a 115 Wash.App. 73, 60 P.3d 1245 (2003).

III. Liability for Torts and Crimes

A. PRINCIPAL’S TORTIOUS CONDUCT

A principal acting through an agent may be liable for harm resulting from the principal’s negligence or recklessness.

B. PRINCIPAL’S AUTHORIZATION OF TORTIOUS CONDUCT

A principal who authorizes an agent to commit a tort may be liable to persons or property injured.

C. LIABILITY FOR AGENT'S MISREPRESENTATION

A principal is directly responsible for an agent's misrepresentation made within the scope of authority. Placing an agent in a position of apparent authority may result in the principal's liability for the agent's fraud.

CASE SYNOPSIS—**Case 32.2: *In re Selheimer & Co.***

Selheimer & Co. a securities broker-dealer partnership in Pennsylvania, closed in 1994 during an investigation by the Securities and Exchange Commission (SEC). Perry Selheimer, the managing partner, pleaded guilty to mail fraud. Other partners, including Edward Murphy, and the firm's clients, including Murphy's mother Jeanne Murphy, filed claims with the Securities Investor Protection Corp. (SIPC) to be reimbursed for their losses. The SIPC advanced over \$250,000 to pay the claims. With more than \$1 million in claims outstanding, the SIPC petitioned the firm into involuntary bankruptcy in 2002. The firm had few assets, so the SIPC asked the federal district court to use the partners' personal assets to cover the liability and filed a motion for summary judgment on this issue. Edward Murphy opposed it.

The court found that "Selheimer & Co. is deficient; that Murphy was a partner of Selheimer & Co.; and that he is vicariously liable under Pennsylvania law for the acts of Perry Selheimer which are chargeable to Selheimer & Co." on a theory of apparent authority. In Pennsylvania "a partner is jointly and severally liable for certain torts chargeable to the partnership" if those torts are committed within the ordinary course of the partnership business. "Apparent authority may result when a principal permits an agent to occupy a position which, according to the ordinary experience and habits of mankind, it is usual for that occupant to have authority of a particular kind." The court issued a summary judgment "in a liquidated amount for the \$251,158.12 in claims advanced by SIPC and an additional \$840,667 for the customer claim of Jeanne Murphy."

Notes and Questions

How does a court discover what assets a party might own to cover any liability? In this case, the court ordered "that within thirty (30) days of the date of entry of this Order, Murphy shall furnish SIPC with a written statement of his assets and liabilities," according to a provision of the Bankruptcy Code.

In some countries, a failure to rescue a person in distress is regarded as negligence. On that theory, could liability have been imposed on the partners in this case for the "distress" experienced by the investors and others? On the ground that a failure to rescue a person in distress is negligence liability might be imposed in the circumstances of this case if the elements of the cause could be established: there must be a duty, a breach of the duty, causation-in-fact and proximate cause, and an injury. The finding of a duty, or its lack, might be the hinge on which liability in these circumstances would revolve. What is the degree of care that should have been exercised, considering the occupation of the defendants, their relationship to the plaintiffs, and other factors, including their awareness of Selheimer's activities? How would a reasonable person in the defendants' position have acted?

ANSWER TO “WHAT IF THE FACTS WERE DIFFERENT?” IN CASE 32.2

If Selheimer & Company had not had the authority to accept funds for investment, did not authorize its manager to accept such funds, and did not represent that the manager or the firm had this authority, would the outcome in this case have been different? Explain. Probably. A principal's liability for its agent's misrepresentation depends on whether the agent was actually or apparently authorized to make representations and whether those representations were within the scope of the agency. Under the facts in this question, the principal could not grant its agent authority to be in a position to defraud clients, because the firm would not have the authority to be in such a position itself. Thus, any such representations would be outside the scope of the agency.

ANSWER TO “THE GLOBAL DIMENSION” QUESTION IN CASE 32.2

Suppose that Selheimer & Company handled accounts for a number of clients located in foreign countries. Would those foreign clients be able to sue under U.S. agency law and hold Murphy indirectly liable for the acts of his partner Selheimer? Why or why not? Assuming that the court had jurisdiction and the foreign clients could establish their claims, the law applied in the *Selheimer* case could support an imposition of liability on Murphy for the acts of his partner. An important consideration, however, is whether those clients could recover. The framework of the proceeding in the *Selheimer* case is the firm's involuntary bankruptcy and Murphy was ordered to pay more than \$1 million in claims. There may be no further assets.

D. LIABILITY FOR AGENT'S NEGLIGENCE

Under the doctrine of *respondeat superior*, a principal is vicariously liable for any harm caused to a third party by an agent acting in the *scope of employment*.

1. Determining the Scope of Employment

Factors from the *Restatement (Second) of Agency*, Section 229, for determining whether or not an act occurred within the scope of employment are enumerated in the text.

2. The Distinction between a “Detour” and a “Frolic”

The text notes that if a servant takes a detour from his master's business, the master is liable for any ensuing tort. If the servant is on a frolic of his or her own, however, the master is not responsible.

3. Employee Travel Time

Commutes to and from work or meals is normally outside the scope of employment unless traveling is part of the job.

4. Notice of Dangerous Conditions

Knowledge of a dangerous condition discovered by an employee and pertinent to the employment situation is imputed to the employer.

5. Borrowed Servants

Also discussed is that when an employer lends an employee's services to another employer, the employer who is liable for injuries caused by the employee's negligence is the employer who had the primary right to control the employee.

CASE SYNOPSIS—

Case 32.3: *Galvao v. G.R. Robert Construction Co.*

George Harms is the owner of George Harms Construction Co. (GHCC), which includes two subsidiaries, George Harms Excavating Co. (Excavating) and G.R. Robert Construction Co. (Robert). Excavating and Robert's only business is to supply employees to GHCC, which reimburses the firms' payroll expenses. GHCC contracted with the New Jersey Department of Transportation (DOT) to replace a viaduct. GHCC directly supervised and controlled all of the work and the workers, including Sergio Galvao, whose wages were paid by Excavating. Galvao was injured on the job, received workers' compensation benefits from GHCC, and filed a suit in a New Jersey state court against Robert, asserting liability under the doctrine of *respondeat superior*. The court dismissed the complaint, and a state intermediate appellate court affirmed. Galvao appealed.

The New Jersey Supreme Court affirmed. "Robert did not have the type of broad influence over the Project from which we might infer the right to control ***. For that reason alone, we conclude that Robert cannot be held vicariously liable under *respondeat superior* for plaintiff's injuries." Also, "Robert did not derive any economic benefit by providing special employees to GHCC. Robert's only income was reimbursement from GHCC for its payroll expenses, a pass-through transaction. Any benefit derived from the use of Robert's employees on the Project, economic or otherwise, was GHCC's alone."

Notes and Questions

Is there anything wrong with either part of the test applied by the court in the Galvao case? Yes, and the court acknowledges this. For example, "[t]here has not been a consistent definition of what is meant by the notion of 'control'" and "[t]he results [under the other part of the test] are unpredictable, uncertain, and in many cases probably unjust. Moreover, both tests reason to results that seemingly require exclusive liability for one or the other employer," which is "unrealistic because commonly both employers have a measure of control and the business of both is being done."

ANSWERS TO QUESTIONS AT THE END OF CASE 32.3

1. What are the two "prongs" of the test for liability for injuries caused by the negligence of borrowed servants under the doctrine of respondeat superior, according to the court in the Galvao case? The court identifies a two-part test for determining whether a "general" employer—a "lending" employer—may be held vicariously liable for the alleged negligence of its employee loaned to a "special" employer—the "borrowing" employer. The first question is whether the general employer controlled the "borrowed" employee on the site. If so, then it must be determined whether the employee furthered the business of the general employer. If the answer to either question is no, there is no liability. In this case, the answers to both questions were no.

2. How does the basis for the second "prong" of this test resemble the basis for the imposition of strict liability in other cases? The court recognized that "the modern justification for vicarious liability is a rule of policy, a deliberate allocation of a risk[,] ... [a]s in other cases of strict liability The losses caused by torts of the servant which are more or less certain to occur in the conduct of the master's enterprise, and are closely connected with it, are placed upon the employer because he is better able to bear them, and to distribute them, through prices, rates or liability in-

surance, to the public. Stated otherwise, it is generally understood that in conducting its business, a party may choose to defray the costs of its liability by passing those costs along to consumers, or through the purchase of insurance.”

ENHANCING YOUR LECTURE—

☆☆ “ THE DOCTRINE OF *RESPONDEAT SUPERIOR* ” ☆☆

The idea that a master (employer) must respond to third persons for losses negligently caused by the master’s servant (employee) first appeared in Lord Holt’s opinion in *Jones v. Hart* (1698).^a By the early nineteenth century, this maxim had been adopted by most courts and was referred to as the doctrine of *respondeat superior*.

THEORIES OF LIABILITY

The vicarious (indirect) liability of the master for the acts of the servant has been supported primarily by two theories. The first theory rests on the issue of *control*, or *fault*: the master has control over the acts of the servant and is thus responsible for injuries arising out of such service. The second theory is economic in nature: because the master takes the benefits or profits of the servant’s service, he or she should also suffer the losses; moreover, the master is better able than the servant to absorb such losses.

The *control* theory is clearly recognized in the *Restatement (Second) of Agency*, which defines a master as “a principal who employs an agent to perform service in his [or her] affairs and who controls, or has the right to control, the physical conduct of the other in the performance of the service.” Accordingly, a servant is defined as “an agent employed by a master to perform service in his [or her] affairs whose physical conduct in his [or her] performance of the service is controlled, or is subject to control, by the master.”

LIMITATIONS ON THE EMPLOYER’S LIABILITY

There are limitations on the master’s liability for the acts of the servant, however. An employer (master) is only responsible for the wrongful conduct of an employee (servant) that occurs in “the scope of employment.” The criteria used by the courts in determining whether an employee is acting within the scope of employment are set forth in the *Restatement (Second) of Agency* and will be discussed shortly. Generally, the act must be of a kind the servant was employed to do; must have occurred within “authorized time and space limits”; and must have been “activated, at least in part, by a purpose to serve the master.”

APPLICATION TO TODAY’S WORLD

The courts have accepted the doctrine of *respondeat superior* for nearly two centuries. This theory of vicarious liability is laden with practical implications in all situations in which a principal-agent (master-servant, employer-employee) relationship exists. Today, the small-town grocer with one clerk and the multinational corporation with thousands of employees are equally subject to the doctrinal demand of “let the master respond.”

a. K.B. 642, 90 Eng. Reprint 1255 (1698).

ENHANCING YOUR LECTURE—



ISLAMIC LAW AND *RESPONDEAT SUPERIOR*



The doctrine of *respondeat superior* is well established in the legal systems of the United States and most Western countries. As you have already read, under this doctrine employers can be held liable for the acts of their agents, including employees. Middle Eastern countries, in contrast, do not follow this practice. Islamic law holds to a strict belief that responsibility for human actions lies with the individual and cannot be vicariously extended to others. This belief and other concepts of Islamic law are based on the sayings of Muhammad, the seventh-century prophet and founder of Islam.

FOR CRITICAL ANALYSIS

How would U.S. society be affected if employers could not be held vicariously liable for their employees' torts?

ADDITIONAL BACKGROUND—

Scope of Employment

The phrase **scope of employment** is used for determining the liability of an employer for employees' acts. Acts within the scope of employment include only acts of a kind authorized by an employer, done within the time and at the place of employment. An employee is authorized to do anything that is reasonably regarded as incidental to the work or that is ordinarily done with the work. Not all acts of the kind authorized and done within the time and at the place of employment are within the scope of employment—only those which an employee does in some part for the purpose of giving service to the employer are included—but the scope of employment includes acts that, as between employer and employee, an employee is not privileged to do.

The limits of the scope of employment depend on the facts of each case. The ultimate question is whether or not it is just that harm resulting from an employee's acts should be considered as a normal risk to be borne by the business in which the employee is employed. The factors to be considered in determining whether an unauthorized act is within the scope of employment are listed in the *Restatement (Second) of Agency*, Section 229. The following hypotheticals accompany the *Restatement (Second) of Agency*, Sections 229, 230, and 231, and illustrate the factors.

Illustrations:

1. P directs his woodchoppers to cut down specific trees, his directions being such that A, a woodchopper, mistakenly cuts an unspecified tree. While cutting, A negligently injures T. P is subject to liability to T.
2. P employs A as a general farm hand, B as a milker of cows. He directs A not to do any mowing until instructed to do so. In the absence of P and thinking that the grass should be cut immediately, A and B cut the grass. If the cutting of grass is within the duties that A is employed to perform, the fact that P forbids cutting temporarily does not prevent it from being within the scope of A's employment. It is not within the scope of B's employment.
3. A has been employed by P as a general assistant in a machine shop to do odd jobs around the place. As he develops more skill, he is assigned to a particular lathe. A assists another operative in

this shop upon a difficult piece of work. The fact that A has not been directed to assist the other operative does not prevent his act in doing so from being within the scope of the employment.

4. P operates a small store employing two clerks and a delivery boy. One of the clerks, during the absence of P and of the delivery boy, to oblige a customer, although his ordinary employment does not include such service, delivers a package to a point close to the store, using a bicycle supplied for the delivery boy's use. It may be found that the conduct of the clerk was within the scope of employment.

5. Same facts as in Illustration 4, except that P has no delivery boy, makes no deliveries, and A uses his own bicycle. The act was not within the scope of employment.

6. P is the owner of an apartment house in a district in which the boys constantly annoy the janitor and interfere with his work. P discharges one janitor who had punished a neighbor's boy for such interference and directs A, the new janitor, to leave boys alone. A does not touch the boys but puts broken glass at the place on the wall where boys customarily climb, in order to exclude them. If it is part of his job to prevent intrusions by defensive means and if his purpose is to prevent intrusions, such act is within the scope of his employment.

7. Same facts as in Illustration 6, except that the janitor has in mind chiefly the punishment of a particular boy whom he dislikes. The addition of this element is sufficient to support a verdict that the act is not within the scope of employment.

8. P, an engraver, requires all [employees] employed in finishing work to wash their hands in his wash room before beginning work. The washing of the hands by the employees as part of their daily work is within the scope of employment.

9. P, employing ball players, requires them to eat what he directs and under his supervision. The conduct of the players during meals while under P's control is within the scope of employment.

10. P furnishes a lavatory in which employees may wash, if they wish, before or after working hours, P retaining no control over it except with regard to keeping it clean. An employee turns on the water to wash his hands after hours and fails to turn it off. This act is not within the scope of employment.

11. P employs A as a chauffeur, requesting him to drive the car to A's own garage for the night at the termination of the day's work, in order that A can arrive early in the morning. In driving to and from the garage to P's place of business, A is within the scope of employment.

12. P employs A, who lives two miles from P's office. Because A has difficulty in getting to the office on time, he persuades P to allow him to use an old car belonging to P. In driving to the office in this car A is not in the scope of employment.

13. P employs men to do logging five miles from the nearest habitation. In order to be certain that they arrive on time, P habitually supplies and keeps in repair a truck which his workmen, who live in the nearest town, use in going to and from work. It is driven usually, but not invariably, by the one acknowledged to be the best driver. These facts will support a verdict that in driving to and from work, the driver is within the scope of employment.

[14.] P directs his salesman, in selling guns, never to insert a cartridge while exhibiting a gun. A, a salesman, does so. This act is within the scope of employment.

[15.] A, P's chauffeur, to avoid a rough spot in the road while upon an errand for P, unlawfully drives upon the sidewalk. This conduct is within the scope of employment.

E. LIABILITY FOR AGENT'S INTENTIONAL TORTS

The doctrine of *respondeat superior* can also apply to these torts. The principal is liable if he or she knows, for example, that an employee has a propensity for tortious acts and places the employee in a position to commit those acts. A principal may also be liable for allowing an agent to commit reckless acts. Insurance may cover the potential liability.

F. LIABILITY FOR INDEPENDENT CONTRACTOR'S TORTS

A principal is generally not responsible for an independent contractor's torts (unless exceptionally hazardous activities are involved, in which case strict liability is imposed).

G. LIABILITY FOR AGENT'S CRIMES

An agent is liable for his or her own crimes, and a principal is not, unless the principal participated by conspiracy or other act. In some states, a principal may be liable for an agent's regulatory violations.

IV. Termination of an Agency**A. TERMINATION BY ACT OF THE PARTIES****1. Lapse of Time**

An agency may terminate if it is limited to a specific time and the time passes.

2. Purpose Achieved, Occurrence of a Specific Event, or Mutual Agreement

An agency may terminate if it is limited to a particular purpose and the purpose is achieved, or subject to a specific event that occurs (or doesn't occur), or the parties agree to end it.

3. At the Option of One Party

Generally, either party can terminate an agency—the agent by renunciation of authority, the principal by revocation of authority—that is, both parties have the power. But they may not possess the right: wrongful termination may subject a party to a suit for damages for breach. An agency that a principal may have the right to revoke is an agency coupled with an interest.

4. Notice of Termination

If the parties terminate an agency, the principal must directly inform any third parties who the principal knows has dealt with an agent. For third persons who have heard about the agency but who have not dealt with the agent, constructive notice is sufficient. An agent's actual authority continues until the agent receives notice of termination; an agent's apparent authority continues until the third person learns that the authority has been terminated.

B. TERMINATION BY OPERATION OF LAW**1. Death or Insanity**

Either party's death or insanity automatically and immediately terminates an agency.

2. Impossibility

When the specific subject matter of an agency is destroyed or lost, the agency terminates.

3. Changed Circumstances

When an event has such an unusual effect on the subject matter of an agency that an agent can reasonably infer that the principal would not want the agency to continue, it terminates.

4. Bankruptcy

The bankruptcy of either party usually terminates an agency.

5. War

War between a principal's country and an agent's country terminates an agency.

TEACHING SUGGESTIONS

1. Hypotheticals that may be used to illustrate and discuss the principles of actual and apparent authority include the following.

Mark writes to Tom directing Tom to act as Mark's agent for the purchase of grain. Mark adds a postscript telling Tom to make no purchase until after communicating with Mark. Mark sends a copy of the letter without the postscript to Jane, a farmer and prospective seller. Does Tom have actual authority to buy grain for Mark? Does Tom have apparent authority to buy grain for Mark from Jane? The answer to the first question is no; the answer to the second question is yes. The *Restatement (Second) of Agency*, Section 8, Comment a, says, "Apparent authority results from a manifestation by a person that another is his agent, the manifestation being made to a third person and not, as when authority is created, to the agent. It is entirely distinct from authority, either express or implied."

Imagine that in the previous question Tom never receives the letter from Mark. Jane, however, does receive the letter, without the postscript. Under those circumstances, does Tom have actual authority to buy grain for Mark? Does Tom have apparent authority to buy grain for Mark from Jane? The answers to these questions are the same as the answers to the same questions in the previous problem, for the same reasons. It is what a person manifests to a third person that results in apparent authority.

2. The different policy considerations involved in contract and tort law may be underscored to explain the differences in the parties' contract and tort liability. When a party enters into a contract, he or she decides whether or not to contract; when a party is the victim of a tort, he or she often had no choice in the matter.
3. It may be useful to compare the events that terminate an agency with the events that discharge a contract (Chapter 17) or the events that terminate an offer (Chapter 11).

Cyberlaw Link

How can the problems of anonymity and accountability, in terms of agency law, be dealt with in cyberspace?

DISCUSSION QUESTIONS

1. ***What effect do a principal's representations giving apparent authority to an agent have on the principal's liability?*** If a third party changes position in reliance on a principal's representations, the principal may be estopped from denying that the agent had authority. When a principal goes beyond mere statements to "clothe" an agent with, for instance, possession and apparent ownership of the principal's property, the agent can deal with the property as if he or she were the owner. When land is involved, possession is not a sufficient indicator of ownership, but if an agent also has a deed to the land and sells the land

against the principal's wishes to an innocent buyer, the principal ordinarily cannot cancel the sale or assert a claim to title.

2. *What happens if a principal does not ratify an agent's unauthorized act?* Absent ratification, a principal is not bound. An agent's unauthorized agreement with a third party is an unaccepted offer, which the third party can revoke without liability (although the agent may be liable for misrepresenting his or her authority) and which the third party's death or incapacity will void. An intervening, extraordinary circumstance may allow a ratification to be set aside to permit a third party to revoke (if a house is destroyed between the time an agent contracts for its sale and the principal ratifies the contract, for instance, the buyer may avoid the sale despite ratification).

3. *Are disclosed principals or partially disclosed principals liable under contracts made by their agents with third parties?* A disclosed or partially disclosed principal is liable to a third party for a contract made by an agent acting within the scope of authority. If a principal is disclosed, an agent is not ordinarily liable for nonperformance by the principal or the third party. If a principal is partially disclosed, either principal or agent may be liable for nonperformance (in most states). If an agent without authority purports to contract on behalf of a disclosed principal, the principal is not liable in contract, but the agent is liable on a warranty theory.

4. *Are undisclosed principals and their agents liable under contracts made by the agents with third parties?* If an agent signs a contract without revealing the agency relation or the principal, and the principal does not perform, the third party can hold the agent liable, although if the agent acted within the scope of authority, he or she is entitled to indemnification. If an agent acts within the scope of authority, an undisclosed principal is bound to perform unless (1) the undisclosed principal was expressly excluded as a party in the contract; (2) the contract is a negotiable instrument; (3) the agent's performance is personal to the contract, permitting a third party to refuse the principal's performance; or (4) the third party would not have contracted with the principal, the agent or the principal knew it, and the third party cancels the contract. Once an undisclosed principal's identity is revealed, a third party can hold either principal or agent liable.

5. *How can a principal be liable for an agent's torts?* A principal acting through an agent may be liable for harm resulting from the principal's negligence or recklessness (for example, giving the agent improper instructions or authorizing the use of improper materials or tools). A principal who authorizes an agent to commit a tort may be liable to persons or property injured (for instance, a principal who directs an agent to cut timber on specific property, which neither has the right to, is liable to the owner in trespass). A principal is liable for loss due to an agent's misrepresentation if the misrepresentation was made within the scope of the agency and the agent's scope of authority (for instance, a financial institution is liable if its loan officer defrauds a borrower by falsely requiring additional collateral that the officer converts). The misrepresentation may be fraudulent or non-fraudulent (a principal who authorizes an agent to answer customers' questions is liable if the agent innocently makes false claims that result in harm). Under the doctrine of *respondeat superior*, a principal-employer is liable for any harm caused to a third party by an agent-employee in the scope of employment. The employer is vicariously liable—liable without regard to personal fault.

6. *Is an employer liable for an employee's torts?* Most employees' torts are not related to their employment, and employers are not liable. If an employee commits a tort while acting within the scope of employment, however, a person injured by the tort can sue the employee or the employer. When an employer lends an employee's services to another employer, the employer who had the primary right to control the employee is liable for injuries caused by the employee's negligence. An employer who knows or should know that an employee has a propensity for committing tortious acts is liable for the employee's acts even if they would not ordinarily be considered within the scope of employment (for instance, an employer who retains a bouncer with a record of arrests for battery is liable when the bouncer arbitrarily attacks a patron). An employer is liable for allowing an employee to engage in reckless acts that can injure others. An employee

acting at an employer's direction can be liable with the employer, even if the employee is unaware of the wrongfulness of an act.

7. *Is an employer liable for an independent contractor's torts?* An employer generally is not liable for an independent contractor's torts, because an employer bargains with an independent contractor only for results and has no control over the manner in which the results are accomplished. When exceptionally hazardous activities are involved, strict liability is imposed—an employer cannot be shielded from liability by using an independent contractor.

8. *Is a principal liable for a subagent's acts?* If an agent is authorized to hire subagents, the principal is liable for the subagents' acts. An agent who hires for an undisclosed principal is responsible to the subagent in contract for wages and so on, but the undisclosed principal is generally liable for tort injuries under the doctrine of *respondeat superior*.

9. *What notice is required to third parties when an agency terminates?* When an agency terminates by operation of law, there is no duty to notify third persons, unless the agent's authority is coupled with an interest. If the parties terminate an agency, the principal must inform any third parties who are aware of the agency that it has terminated. A principal is expected to notify directly any third person who the principal knows has dealt with an agent. For third persons who have heard about the agency but have not dealt with the agent, constructive notice is sufficient. An agent's apparent authority continues until the third person learns that the authority has been terminated. A writing revoking an agent's written authority must be shown to all who saw the writing that established the agency. When written authorization contains an expiration date, the date's passing is sufficient notice to third parties.

EXPLANATIONS OF SELECTED FOOTNOTES IN THE TEXT

Footnote 4: Principals are classified as disclosed, partially disclosed, or undisclosed. These classifications are explained in the *Restatement (Second) of Agency*, Section 4. The following is the text of the section with selected comments.

§ 4. Disclosed Principal; Partially Disclosed Principal; Undisclosed Principal

- (1) If, at the time of a transaction conducted by an agent, the other party thereto has notice that the agent is acting for a principal and of the principal's identity, the principal is a disclosed principal.
- (2) If the other party has notice that the agent is or may be acting for a principal but has no notice of the principal's identity, the principal for whom the agent is acting is a partially disclosed principal.
- (3) If the other party has no notice that the agent is acting for a principal, the one for whom he acts is an undisclosed principal.

Comment:

a. The classification of principals into disclosed, partially disclosed, and undisclosed is for the purpose of simplifying the statement of the rules determining the legal relations of third persons with respect to the principal and the agent, since many of these relations are dependent upon whether or not the third person has notice of the existence and identity of the principal. The other party has notice of the existence or identity of the principal if he knows, has reason to know, or should know of it, or has been given a notification of the fact. ***

b. Intent of agent. A disclosed principal is a party to a contract made by an authorized agent who purports to act on the principal's account, regardless of the agent's intent. Thus if the principal au-

thorizes him to borrow and he borrows in the principal's name, the principal is liable on the contract even if the agent intended to embezzle money received on account of it. *** However, it is only because the agent intends to act on account of another that the doctrine of undisclosed principal exists. Thus, an agent authorized to buy a specific automobile in his own name who purchases the automobile, causes the principal to be a purchaser only if the agent so intended. The fact that it would be wrongful for him to purchase it for himself and that he would become a constructive trustee of it for the principal, does not make the latter a party to the transaction. ***

c. *Manifestations at time of transaction.* Whether a principal is a disclosed principal, a partially disclosed principal or an undisclosed principal depends upon the manifestations of principal or agent and the knowledge of the other party at the time of the transaction. The disclosure of the existence or identity of the principal subsequently has no bearing upon the relations created at the time of the transaction. The non-disclosure of the principal on the face of a document integrating the transaction does not of itself indicate that the principal is undisclosed, although it may affect the liability of the parties to the transaction. Thus, when a simple contract is made in the name of the agent, but the other party knows that the principal is the contracting party and intends to contract with him, the contract is with the principal as a disclosed principal, although his name does not appear in the instrument * * *; and this is so even though the agent, in a suit by the other party, may not be able to escape liability. * * *

Illustrations:

1. A contracts with T in his own name, T reasonably believing that A is acting for himself. After the execution of the contract, A reveals to T that he was acting as agent for P. P is an undisclosed principal.

2. A, acting as agent for P and so stating to T, executes a memorandum of the contract which he signs with his own name. P is a disclosed principal.

g. *Usage of terms.* There has been no uniform usage by the courts with respect to the terms here defined. The one here described as a "partially disclosed principal" has been called by some courts an "unidentified principal", which is a somewhat more accurate description. The term "undisclosed principal" has been used to describe not only a person whose existence is unknown, but also one whose identity has not been revealed and even one whose identity is known but whose name does not appear in the written contract.

Footnote 5: In most states, if a principal is partially disclosed, the principal and agent are treated as parties to the contract, and a third party can sue either for contractual nonperformance. This is explained in the *Restatement (Second) of Agency, Section 321*. The following is the text of the section with a selected comment.

§ 321. Principal Partially Disclosed

Unless otherwise agreed, a person purporting to make a contract with another for a partially disclosed principal is a party to the contract.

Comment:

b. *Separate liability of agent.* Unless agreed otherwise, the agent is subject to separate liability and may be sued individually without the joinder of the principal. As where the principal is fully disclosed, however, the parties can agree that the agent and the principal shall be liable jointly.

Likewise, there may be an agreement that the agent is to be liable until the disclosure of the identity of the principal and that thereafter the principal alone is to be liable.

ACTIVITY AND RESEARCH ASSIGNMENT

Ask students to talk to insurance agents, sales representatives, realtors, purchasing agents, and others to learn of some their experiences in the law of agency, looking particularly for events that relate to the material discussed in this chapter. Have the students share what they learn with the class.

ANSWERS TO ESSAY QUESTIONS IN STUDY GUIDE TO ACCOMPANY BUSINESS LAW, ELEVENTH EDITION BY HOLLOWELL & MILLER

1. **Identify and describe the categories of authority by which an agent can bind a principal and a third party in contract.** Actual authority—express authority. Express authority is authority expressly given by a principal to an agent. It is embodied in what a principal engages an agent to do. Express authority may be oral or written, although in some cases—a grant of a power of attorney or a grant under the equal dignity rule—it must be in writing. A principal may ratify in writing an act done without written authority. Actual authority—implied authority. Implied authority is authority implied by custom, inferred from the position in which a principal has placed an agent, or is implied because it is necessary to carry out expressly authorized duties and responsibilities. The test to determine whether an agent has implied authority to do a specific act is whether it is reasonable for the agent to believe that he or she has the authority. Apparent authority. Apparent authority is authority created when a principal's conduct or words leads a third party reasonably to believe that an agent, who has no actual authority, has authority.
2. **What are some of the situations in which a principal is liable for an agent's torts?** Principal's tortious conduct. A principal is liable for harm resulting from the principal's negligence or recklessness in acting through an agent (giving improper instructions, for example, or authorizing the use of improper materials or tools). Principal's authorization of tortious conduct. A principal who authorizes an agent to commit a tort is liable for harm to persons or property (for instance, if a principal authorizes an agent to cut timber on specific property, which neither owns nor has the right to, the cutting is a trespass, and the principal is liable to the owner). Misrepresentation within the scope of the agency and the agent's scope of authority. A principal is liable for harm caused by an agent's misrepresentation if the misrepresentation is made within the scope of the agency and the agent's scope of authority (for example, a bank is liable if its loan officer defrauds a borrower by falsely requiring additional collateral that the officer steals). The misrepresentation may be fraudulent or non-fraudulent (a principal who authorizes an agent to answer customers' questions is liable, for example, if the agent intentionally or innocently makes false claims that result in harm). Other torts within the scope of employment. Under the doctrine of *respondeat superior*, a principal–employer is liable for any harm caused to a third party by an agent–employee in the scope of employment. The liability is vicarious (without regard to personal fault). Factors determining whether or not an act falls within the scope of employment include: (1) whether the principal–employer authorized the act; (2) the time, place, and purpose of the act; (3) whether the act is one commonly performed by agent–employees on behalf of their principal–employers; (4) the extent to which the act advanced the principal–employer's interest; (5) the extent to which the agent–employee's private interests were involved; (6) whether the principal–employer furnished the means or instrumentality by which the injury was inflicted; (7) whether the principal–employer had reason to know that the agent–employee would do the act in question and whether the agent–employee had done it before; and (8) whether the act involved the commission of a serious crime. Commuting or going to and from meals is generally considered outside the scope of employment. Traveling on business is generally considered within the scope of employment. When traveling, departing from business to take care of personal

affairs is not generally considered within the scope of employment if the departure amounts to abandoning business (driving to a different city, for example).

REVIEWING—

★★★ **LIABILITY TO THIRD PARTIES AND TERMINATION** ★★★

Lynne Meyer, on her way to a business meeting and in a hurry, stopped by a Buy-Mart store for a new pair of nylons to wear to the meeting. There was a long line at one of the checkout counters, but a cashier, Valerie Watts, opened another counter and began loading the cash drawer. Meyer told Watts that she was in a hurry and asked Watts to work faster. Watts, however, only slowed her pace. At this point, Meyer hit Watts. It is not clear from the record whether Meyer hit Watts intentionally or, in an attempt to retrieve the nylons, hit her inadvertently. In response, Watts grabbed Meyer by the hair and hit her repeatedly in the back of the head, while Meyer screamed for help. Management personnel separated the two women and questioned them about the incident. Watts was immediately fired for violating the store's no-fighting policy. Meyer subsequently sued Buy-Mart, alleging that the store was liable for the tort (assault and battery) committed by its employee. Ask your students to answer the following questions, using the information presented in the chapter.

1. ***Under what doctrine discussed in this chapter might Buy-Mart be held liable for the tort committed by Watts?*** The doctrine of *respondeat superior*, under which employers may be held liable for the actions of their agents or employees, would apply in this situation. The concept of *respondeat superior* is based on the assumption that employers are usually in a better position to absorb the costs that may result from agents' or employees' torts.
2. ***What is the key factor in determining whether Buy-Mart is liable under this doctrine?*** Under the doctrine of *respondeat superior*, an employer is responsible for torts committed by agents or employees in the course and scope of their employment.
3. ***How is Buy-Mart's potential liability affected depending on whether Watts's behavior constituted an intentional tort or a tort of negligence?*** Buy-Mart would be liable in either case under the doctrine of *respondeat superior*, which does not distinguish between the two types of torts. If Watts's wrongful conduct occurred in the scope of employment, then Buy-Mart would be liable.
4. ***Suppose that when Watts applied for the job at Buy-Mart, she disclosed in her application that she had previously been convicted of felony assault and battery. Nevertheless, Buy-Mart hired Watts as a cashier. How might this fact affect Buy-Mart's liability for Watt's actions?*** An employer who knows or should know that an employee has a propensity for committing tortious acts is liable for the employee's acts even if they would not ordinarily be considered within the scope of employment. Thus, in this scenario, even if Watts's actions were not in the scope of employment (for instance, if Watts attacked Meyer in the parking lot), Buy-Mart would still be liable.

