



Business Law (6th edn)  
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p. 455 **18. Businesses and the Responsibility to Agents**

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### Abstract

This chapter identifies agency relationships, their prevalence in business, and how the agency exists to bind the principal in contracts with third parties. It begins by defining agency as the relationship that exists between two persons when one, called the agent, is considered in law to represent the other, called the principal, in such a way as to be able to affect the principal's legal position in respect to strangers to the relationship by the making of contracts or the disposition of property. Agencies exist in corporate organizations, sole trader, and partnership trading structures, and the law in this area applies to many relationships and is frequently seen in commercial enterprises, including high street retailers, between partners, and the directors of a corporation.

**Keywords:** agency relationships, agent, principal, legal position, making of contracts, disposition of property

It is essential to recognize that in a commercial world, many business transactions are completed through an agency relationship. An agent creates contracts between the person they are acting for (the principal) and the other (third) party. This contract is binding on the third party and will allow them to enforce the contract. An agent can gain authority to act for the principal implicitly, or through express agreements, and their actions can bind the principal in such contracts. The agent has responsibilities and rights through agreements to act for the principal, and it is necessary to appreciate how these are defined and limited by the courts and by statute.

## Business Scenario 18

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Rob owns a company operating under the name 'Robert's Burgers Ltd' which employs 10 part-time and casual staff. The company trades from a mobile burger van which has a weekly pitch at markets in Leeds, Bradford, and Wakefield, Yorkshire. However, the company makes the majority of its annual income from the sale of burgers at summer festivals held nationally.

Nine months ago, Rob decided to employ one particular part-time employee, Hugo Hamperman on a full-time basis. The aim of the appointment was that Rob would buy a second burger van which Hugo would manage. Accordingly, Rob purchased a van and for the last three months Hugo has been managing this side of the business which includes a responsibility of Hugo to purchase the raw ingredients to make the burgers for sale through the van. Rob issued to Hugo a list of suppliers with which he has had regular dealings. Further, one month later Rob imposed on Hugo a spending limit of £500 per week for raw ingredients.

Hugo purchased burger buns and condiments from Conway Meats plc, one of the suppliers on the list, at a total cost of £300. During the same week he then went to another supplier on the list, Conway Meats Ltd, but they had run out of the standard burger meat he usually bought. This meant Hugo was forced to buy premium quality burger meat from Pesto Meats Ltd at a cost of £420. Robert's Burgers Ltd is refusing to honour the contract with Pesto Meats Ltd.

Last month, on his way to a festival in Gloucestershire, Hugo realized that a freezer containing the raw burger patties was no longer working. He sent Rob a text message informing him of the situation and asking what he should do. After two hours and having received no response, Hugo sold all the burger patties to a local fast food restaurant at a loss.

p. 456 **Learning Outcomes**

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- Identify in which situations an agency agreement will be established (**18.3**)
- Explain the various forms of authority an agent may possess (**18.3.1–18.3.4**)
- Identify the duties and obligations imposed on an agent in relation to the principal (**18.4–18.4.4**)
- Explain where liability will be imposed on an agent in contracts made with authority (**18.5**)
- Explain the rights of agents when acting in their capacity (**18.6**)
- Explain the implications of the Commercial Agents (Council Directive) Regulations 1993 to agency contracts and the parties involved (**18.8–18.8.3**)
- Identify the procedures in terminating an agency relationship (**18.7; 18.8.3**).

## 18.1 Introduction

Agency is the relationship which exists between two persons when one, called the agent, is considered in law to represent the other, called the principal, in such a way as to be able to affect the principal's legal position in respect of strangers to the relationship by the making of contracts or the disposition of property (Fridman, G. H. L. (1996) 'The Law of Agency' (7th Edition) Butterworths: London).

The law in this area applies to many relationships and is frequently seen in commercial enterprises, including high street retailers, between partners, and the directors of a corporation. The agent's role is to act on the principal's behalf, in establishing contracts, for example; and when the agent has the required authority to act in this way, the contract will not be considered to bind the agent and the third party, but rather will bind the principal and the third party. By way of example, in retailing, the person who works as a 'shop assistant' is essentially acting as the agent of the shop's owner. When goods are sold at the retailer's establishment, the shop assistant is not personally trading the goods, but rather they are given the authority to complete the transaction for the sale, and the money paid is to the owner of the shop, not the shop assistant. With regard to this authority, where the third party has paid for the goods, and passed their money to the shop assistant, agency provides that even where the shop assistant fails to pass this money to the owner of the shop, it will be considered that the third party has paid for the goods and has good title to them, even though the shop assistant has not fulfilled their obligation to the owner. The agent has the authority to complete such transactions on behalf of the principal, and the third party has conducted their business on the basis of this authority. It is in this way that many (obvious) forms of agency are seen—the agent having authority to buy and sell goods.

## 18.2 Types of agent

There are several forms of agreement in which an agent may have authority to bind the principal, and simply because the word 'agent' is used, this does not create a situation where their actions will bind the principal. For example, an estate agent is a term in common usage, but it does not establish the legal implications and

p. 457 rights of an agent in its legal sense. ←

### Consider

The first issue to consider is the type of agent Hugo is.

Agents may take the following forms:

- *General agent:* This is the most common type of agency agreement, where the agent has the authority to act for the principal in the ordinary course of their business.

- *Special agent*: Denotes a similar form of agency agreement but the agent is only authorized to perform a particular act.
- *Commercial agent*: This is an agent, provided for under an EU Directive, which allows the agent greater protection (through the statute) than exists under the common law.
- *Commission agent*: This agent has the authority to buy and sell on the principal's behalf, but they are not authorized to establish privity of contract with the third party (see 6.3).
- *Del Credere Agent*: Here the agent binds the principal, but they are provided with an additional sum that guarantees that the agent will indemnify the principal in the event that the third party fails to pay money owed under the contract (e.g. when goods are sold on credit).

## 18.3 Creation of agency

Agency agreements are very easy to establish (see **Table 18.1**).

**Table 18.1 Creating an agency**

Through a contract (although in most situations this is not necessary)
Through verbal agreement
Where an agent is appointed to execute a deed (and have a 'power of attorney'), under common Law, they must be appointed by deed
Implicitly where the intentions of the parties provide guidance as to the true relationship (see <i>Chaudhry v Prabhakar</i> )
and
Agency may be imposed on the parties by statute (e.g. Consumer Credit Act 1974, s. 56(2)), through necessity, and through cohabitation

As there is no compulsion on agents to register with a governmental body to demonstrate their status as agents, or to work under a set of clear guidelines, the common law has assisted in identifying the powers of an agent. However, before the rights and duties of the agent and principal are considered, the source and implications of the form of authority that the agent possesses must be identified. Such authority may be based on 'actual' authority provided (either expressly or through implication); it may be 'apparent' through a representation made to the third party; it may exist through the principal's subsequent '**ratification**' of the contract; or the authority may have derived through 'necessity'. Note ← that the classic principle, that to create obligations under agency required the representation of this relationship to have derived from the principal and not the agent has been weakened, especially through the concept of apparent authority. Where the agent has authority from the principal to contract, the third party may rely on this in their enforcement of a contract.

## ***Chaudhry v Prabhakar (1988)***

### **Facts:**

The claimant was accompanied by her friend to inspect a used car with the intention of purchasing it. Despite obvious damage to the car's bonnet, the friend recommended the purchase on the advice that it 'was in good condition'. After the purchase it transpires the car was not in good condition and this led to the claimant's action against the friend.

### **Authority for:**

Even where a friend volunteers time and advice to help another person, an objective duty of care is imposed. The friend was aware that their opinion was to be relied on. However, similarly with contract law, the relationship between the parties is a material factor and opinions of friends in these circumstances (a social and domestic relationship) will not establish a duty of care.

### **18.3.1 Actual Authority**

When expressed, there is an agreement between the principal and the agent as to the powers that the agent will have to bind the principal (e.g. the owner of a shop may inform the shop assistant that they have the right to sell the goods in the shop for the price identified on the ticket with no discretion for discounts). As with other types of express agreements, this can be established in words or writing (through a contract; and this may be preferable to clearly identify the extent of any authority).

### **Consider**

Does Hugo have express actual authority? If so, how does the prohibition of spending more than £500 per week affect the actual authority? Further, as Hugo has the ability to go and trade with companies as provided for by Robert, would this amount to apparent authority?

There also exist situations where the authority may have been provided through implication due to the relationship/conduct between the agent and principal. Typical situations, relating to business, may occur where a director of a company may have been appointed incorrectly, or where they have not been appointed to a specific post (such as managing director), but the company has not made attempts to remove the authority p. 459 or deny this ← authority to third parties. Implied authority may work in providing, in its entirety, the binding agreement between the agent and principal.

## ***Hely-Hutchinson v Brayhead Ltd (1968)***

### **Facts:**

A company allowed its chairman to act in the way, and with the powers of, a managing director, without engaging him to this position. A managing director of a company would be assumed to have the authority to bind the company in most contractual dealings, and in this instance the chairman would not. The chairman established a contract that sought to bind the company and the Court of Appeal held the chairman had the implied authority to do this. It was the actions of the company that allowed for the chairman to act in this way, and hence it should be treated as if he had been given the position of managing director from the board of directors.

### **Authority for:**

Actual authority and apparent (ostensible) authority often overlap. Where the board invest the chairman (using the facts of the case as an example) with the actual authority of that position but also with apparent authority to act with the authority of a managing director, this apparent authority can exceed the actual authority. It seeks to protect innocent third parties who are unaware of the limitation of authority placed by the principal on the agent.

Implied authority may also have the effect of broadening existing powers.

## ***Waugh v HB Clifford and Sons Ltd (1982)***

### **Facts:**

A firm of solicitors were engaged by builders who required representation to protect against any legal action after they had negligently built houses. They expressly instructed the solicitor not to compromise on the basis of a substantial compensation payment. However, the solicitors disregarded the builders' instruction. It was common to allow solicitors in these situations to compromise on behalf of the principal. In the resultant action by the builders against the firm, the Court of Appeal held that as the builders had provided clear instructions not to compromise, and that express terms in a contract override implied terms (such as allowing the solicitors to compromise on the principal's behalf), the solicitors were in breach.

## Authority for:

The authority between the agent and the third party is different to that between the agent and the principal. Where express instructions are given from a principal to the agent, this removes the implied nature of any authority in contradiction of the express agreement.

p. 460 **18.3.1.1 Usual authority**

An unusual situation involving agency agreements occurred in *Watteau v Fenwick*.

### ***Watteau v Fenwick (1893)***

#### **Facts:**

The owner of a public house sold the property (and business), but was hired to be its manager. In his position as manager, he was provided with the authority to purchase bottled drinks on behalf of the new owner (the principal), but was expressly instructed not to purchase tobacco products on credit on the principal's behalf. The manager did purchase such goods from a salesman who had previous dealings with the manager (in his capacity as owner) and who was unaware of the change in management/ownership structure of the business (termed as an undisclosed principal). When the manager was unable to pay for the goods on credit he asserted that the principal was bound. It was held that the actions of the manager bound the principal.

#### **Authority for:**

This was a strange decision as the manager had no actual authority to act to bind the principal in this way; it could not be said there was apparent authority as the representation as to the agent's authority must move from the principal; the undisclosed principal was held liable for the actions of the agent, and hence the decision has been criticized. As such, it falls somewhere between actual and apparent authority, and has been termed 'usual' authority.

The reasoning for the decision was based on the manager being the previous owner and still having his name above the door (as required of licensed premises). He had not identified to the salesmen/traders in the area who had previous contact with the manager as to the change in organizational structure (and the change in authority), and as such it could be considered that the manager had authority to act, and the third party required protection. Despite the principal being bound by the agent's actions, this does not prevent him taking action against the agent for the breach.

### 18.3.2 Apparent Authority

Apparent authority (or ostensible authority, as it is referred to in some legal texts) exists outside of the actual authority previously identified. Whereas express and implied authority derives from the agreement between the principal and agent, apparent authority is applicable where the principal (or someone acting for them) has represented to the third party that the agent has the authority to act on their behalf. The consequence is that where the third party has been given this impression of authority of the agent, an agreement that is subsequently concluded between the agent and third party may bind the principal, who is unable to deny the representation made.

Therefore, to establish apparent authority, the following criteria must be demonstrated:

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1. there must have been a representation regarding the person as an agent;
  2. the principal must have conveyed this representation (or someone acting on their behalf);
  3. the third party must have acted based on this representation.

An example of the effects of apparent authority was demonstrated in the previously discussed case of *Hely-Hutchinson* (as apparent and actual authority often overlap).

This point was made in the following case:

#### ***Freeman & Lockyer v Buckhurst Park Properties Ltd (1964)***

##### **Facts:**

A director was given authority to act in the manner expected of a managing director, and in this capacity he engaged a firm of architects to act for the company. The company refused to pay the firm for the work on the basis that the director who had agreed the contract lacked the (actual) authority to bind the company. The Court of Appeal held that there was a contract between the firm and the company.

##### **Authority for:**

There had been an impression that the director had the authority to bind the company in the agreement, and therefore the principal was liable under the contract established on its behalf. The representation, moving from the principal, is usually provided (in the case of corporations) by the company's board of directors.

And again:

## ***First Energy (UK) Ltd v Hungarian International Bank Ltd (1993)***

### **Facts:**

The claimants had sought credit from the bank and in negotiating on this matter had dealt with a senior manager. During the negotiations the manager disclaimed any right that he may have to bind the bank as he lacked the actual authority to guarantee credit. However, later the manager wrote to the claimants stating that the credit requested by the claimants had been authorized by the bank, even though this was not the case. The Court of Appeal held that the bank was bound under the offer made by the manager. Whilst the Court accepted that the manager had informed the claimants of his lack of capacity to contract on behalf of the bank, he did possess the authority to communicate matters from the bank to clients. As such, the bank had represented that the manager had authority to pass on decisions made by it, and the claimants could rely on this decision.

### **Authority for:**

Businesses contract through the use of agents. As such, third parties dealing with them must be enabled to rely on their appearance (here as an authorized agent of the bank).

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- ← It must be noted that where the agent acts on apparent authority, but in fact does not possess actual authority, they may be held liable if the principal decides to bring an action against them for disobeying the principal's instructions. If, on the other hand the agent had actual authority to take the actions that bound the principal, no claim is allowed by the principal against the agent (and the agent would be entitled to any payment under this agency agreement).

### **18.3.3 Authority Through Ratification**

An agent who purports to act for the principal may enter into a contract that they were unauthorized to make. At this stage it may not bind the principal but when the principal is aware of the contract established by the agent on their behalf, and the principal accepts the agreement, they will be bound by it. The ratification must be given within a reasonable time of the agreement. Ratification allows for the retrospective acceptance of a contract and it will entitle the principal to all the rights and obligations provided under a contractual agreement. As such, they are empowered to compel the completion of the contract even where the third party no longer wishes to be bound.

## ***Re Tiedemann and Ledermann Freres (1899)***

### **Facts:**

An agent used the principal's name to enter into a contract but he did so to avail himself of the benefits of the agreement. On discovery of the truth, the third party attempted to end the contract due to a misrepresentation.

### **Authority for:**

Where the principal ratifies the contract, the third party is bound.

## ***Bolton Partners v Lambert (1889)***

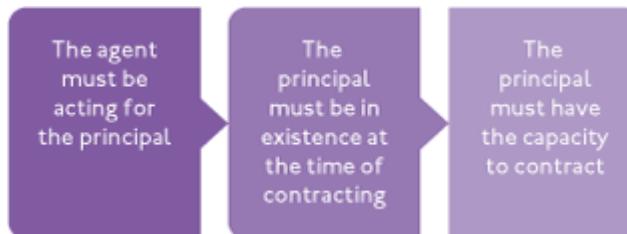
### **Facts:**

The defendant had communicated to the managing director of a company his offer to purchase the company. Following this communication, on 13 December 1886, a committee decided that it would accept the offer (even though the committee had no such power to accept) and this was in return communicated to the defendant. In January the defendant attempted to revoke the offer, but the company sought to enforce this through an action for specific performance. The Court of Appeal held that as the board of the company had ratified the agreement, its effect was to bind the parties following the acceptance of the offer. The acceptance of the company was retrospectively applied to the December meeting of the committee and hence the defendant's attempted revocation in January was too late and consequently ineffective.

### **Authority for:**

Ratification by a principal of acts done by an assumed agent is 'thrown back' to the date of the act done, and the agent is put in the same position as if they had authority to do that act.

p. 463 ← The steps required to enable ratification are outlined in Figure 18.1.



**Figure 18.1** Steps to enable ratification

- *The agent must be acting for the principal:* Because of the nature of ratification, and the requirement for the agent to be acting for the principal, the third party must be aware that a principal exists. Without such knowledge, the third party will assume they are contracting with the agent and the agent will be bound by the agreement. This is vitally important as an undisclosed principal cannot later ratify, even if the parties want this.

***Keighly Maxted & Co. v Durrant (1901)*****Facts:**

An agent had made a contract for wheat based at a higher price for the principal than had been agreed. The principal agreed to ratify the contract.

**Authority for:**

The House of Lords prevented the ratification as the agent had not informed the third party of the principal's existence at the time of contracting.

- *The principal must be in existence at the time of the contract:* This aspect applies particularly to companies that have been newly formed. Where the promoters of the company (its 'agents') have entered into a contract before the company has completed the registration process and been granted the certificate of incorporation, the agents are personally liable and the company may not, once it has been formed, later ratify the agreement.
- *The principal must have the capacity to contract:* The capacity to contract refers to elements such as whether the principal would have been able to enter into the contract that the agent actually formed. For example, corporations may lack the ability (capacity) to enter into the type of contract relevant to the claim, and hence there is no possibility of ratification. To avoid situations where ratification may cause problems between the parties, the agreement may be stated as being 'subject to ratification' and hence enable a withdrawal from the contract before ratification takes place.

**18.3.4 Authority Through Necessity**

Where the agent acts in relation to necessity (e.g. protecting property owned by the principal), then the courts may bind the principal in the actions of the agent even though they have no actual or apparent authority to act in the particular way. These cases have often occurred in emergencies at sea or where perishable goods are

p. 464 involved. ↵

## Consider

Consider Hugo's express actual authority and how this may have been affected by the availability of the meat. The operation of the law of necessity and the criteria required should be assessed.

Significantly, the fact that Hugo must be unable to communicate with Robert should be applied to this situation to identify if such an authority could be established.

The requirements to bind the principal in this way involve satisfying the following criteria:

1. the agent must have had responsibility for the control over the property belonging to the principal;
2. it was not possible for the agent to discuss the issue with the principal and gain their instructions as to the action to be taken;
3. the situation must be considered an emergency;
4. the agent must have acted in good faith.

## *Springer v Great Western Railway (1921)*

### Facts:

The agent was not permitted to sell tomatoes (when engaged to carry these). However, due to weather and transport problems the agent did sell the goods on behalf of the principal as the tomatoes were perishing in the heat. This had occurred on land and it was possible and reasonable for the carriers to contact the principal and obtain his instructions before taking the action.

### Authority for:

It was held that such a situation did not amount to an emergency and was an unauthorized act.

## 18.4 Duties of the agent

Due to the nature of the agreement between the agent and principal, and the fact that the agent is given authority to act on the principal's behalf, trust and confidence are paramount in such dealings. The agent must respect the instructions of the principal and act in their best interests.

## Consider

Hugo is subject to contractual duties which he has breached—in particular, the duty of performance of the undertaking and the duty to obey reasonable instructions need to be considered.

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↳ Duties that have been imposed on agents include:

- *An obligation to obey lawful instructions:* An agent may have agreed with the principal the parameters of the (actual) authority, and these may have been established in a contract. Where this is so, a failure on the side of the agent to follow the requirements of the contract will amount to a breach, even if this was performed in good faith. Therefore, even if, in not following instructions, the agent considered their actions to be the most appropriate course for the principal, a breach is still committed.
- *Non-delegation of duties:* There is a general duty that the agent should not delegate (and in essence this would amount to sub-delegation) the principal's authority, and should perform the task personally. However, this general duty will be removed where the principal expressly agrees for the agent to delegate, where such authority to delegate may be implied from the circumstances of the case, and if the delegation is required due to some unforeseen event.
- *To exercise care and skill:* When conducting the business of the principal, the agent must use the appropriate care and skill in the execution of their duties (based on the nature of the task and the skills they profess to hold. The most common examples of the nature of care and skill in professional occupations include agents in solicitors and accountancy practices—see *Chaudhry v Prabhakar* at 18.3).
- *Fiduciary duties:* The **fiduciary duties** are imposed due to the nature of the relationship between the agent and principal, and the authority the agent exercises for the principal. If a breach of the duty is discovered, the principal may seek to recover any secret profit made by the agent, and/or any bribe that has been paid. In such a situation the principal may seek damages for the fraud committed. The principal may have the option to refuse to pay the commission or salary of the agent. The agent's contract with the principal may be terminated, and the agreement with the third party may be rescinded. The use of these options is determined by the courts depending on the actions of the parties and what is fair and reasonable in the circumstances.

The examples of fiduciary duties given at 18.4.1–18.4.4 are artificially separated in this section for ease of reference, and they frequently overlap.

### 18.4.1 Duty Not to Take Bribes

One of the most important duties placed on an agent is to ensure that they do not take bribes in the exercise of the authority for the principal. Clearly, good faith requires that the agent acts in the best interest of the principal, and for their, rather than the agent's benefit. As such, a bribe to, for example, secure the award of a contract would place the agent's motives and the best interests of the principal in conflict. It is this element of inducement that may give rise to accusations of accepting bribes, and this may not be confined to money, but

could include free samples for the agent, the agent being invited to hospitality events, or any other gift in kind. Where the principal discovers the bribe they may terminate the arrangement with the agent and recover any commission paid, recover the bribe provided, consider the bribe to be held by the agent on trust, recover damages from the third party that provided the bribe for any losses attributable (rather than recovering the p. 466 bribe), and they may rescind the contract between the principal and the third party. ←

### ***Attorney General for Hong Kong v Reid (1994)***

#### **Facts:**

Mr Reid, during his career at the legal service of the Government of Hong Kong, accepted bribes in breach of his fiduciary duties. He used the money to buy properties which had gained in value. The properties were deemed to be held in trust for the Government.

#### **Authority for:**

When a bribe is accepted by a fiduciary (the agent) in breach of their duty, the bribe is held on trust for the person to whom the duty is owed (the principal).

As can be observed, the effects of bribes can be catastrophic to the relationship between all the parties.

#### **18.4.2 Secret Profits**

The agent must ensure that the profits accrued from the agreement(s) with the third party are agreed between the agent and principal. The agent should not make a profit that has not been previously agreed (such as the agent's commission/salary). This may be particularly so when the agent is asked to dispose of goods and they do so at a higher price than requested by the principal (and the agent retains the 'extra' amount), or the agent uses the principal's property for their own purposes. It is important to remember that such situations do not have to cause the principal any loss, but it is the abuse of the position of trust and authority that is at issue. Where an agent has made a secret profit but has not been dishonest the court will usually award the principal with the profit rather than impose more harsh penalties.

#### **18.4.3 Avoid a Conflict of Interest**

In the same way as a duty exists to prevent the agent making a secret profit when acting for the principal, the agent must also not allow their own interests to conflict with those of the principal. The agency agreement is predicated on the basis of the agent acting in the best interests of the principal, and this is the case even where an agent acts, but not with the intention to defraud or mislead the principal, and there is the appearance of a conflict. As such, where a conflict of interest may arise, the agent should offer a full disclosure to the principal so an informed choice may be made.

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## ***Armstrong v Jackson (1917)***

### **Facts:**

The agent was a stockbroker. The principal wished to purchase shares in a particular company, and the agent obtained these shares (but they were in reality his own). The agent had informed the principal that he had purchased the shares, whilst the real situation was that ← the stockbroker was a promoter of the company when it was formed. When this fact was later discovered, the principal was successful in having the contract set aside.

### **Authority for:**

The court held that the agent had a duty to disclose this potential conflict to the principal and had breached his duty in not so doing.

### **18.4.4 Duty to Account**

The agent must maintain adequate records of their dealings on behalf of the principal and make these available for inspection when requested. As agents may work under the authority of several principals it is their duty to maintain records in a manner that allows for the separation of the principals' accounts. This is the case where information is maintained in computer form (e.g. on a database) and the principal is entitled to view their own accounts. Where the agent cannot separate the principal's accounts, the principal is entitled to see all of the accounts held by the agent. This further has an impact on the agent's duty of confidentiality, and the continuing nature of this obligation following the cessation of the agency agreement.

## ***Bolkiah v KPMG (1999)***

### **Facts:**

KPMG had confidential information regarding Prince Bolkiah (a former client) which may have been relevant to an investigation about the use of assets which, it was suggested, Bolkiah had used for his personal benefit. The investigation was being undertaken by the Brunei Investment Agency (BIA) who had instructed KPMG to act for it.

### **Authority for:**

The House of Lords granted an injunction against KPMG from acting for the BIA. A fiduciary cannot act for and against a client at the same time. A duty exists which goes beyond mere non-deliberate disclosure to ensure a client is not put at risk.

## 18.5 Liability of the agent

In situations where it has been established that the agent acted beyond their authority and therefore did not bind the principal, it has to be determined what happens to the agreement with the third party. The third party has entered into an agreement and is entitled to have the other party (the agent) honour their side of the bargain. Where the agent has identified themselves as such, and established the contract on the principal's behalf, then the contract is between the principal and the third party, and the agent has no liability. If, on the other hand, the agent has not disclosed that they were acting for a principal, then the contract will exist

- p. 468 between the agent and the third party and the usual ← rights and liabilities in a contractual agreement will apply. When the agent discloses the principal to the third party, and the agent was acting under actual authority, liability of the third party to the agent ceases and is transferred to the principal, but the agent and the principal will be jointly liable to the third party. The third party may then choose to enforce the contract against the agent or principal, but once the decision is made it cannot be changed. In a situation where the agent acted without actual authority, the principal will not be bound by the agreement.

Situations exist where an agent has not disclosed the existence of a principal and the principal is then prohibited from concluding the contract. Where the principal was not disclosed, and if they had been, the third party would not have agreed to the contract, this will prevent the principal from acting on it. Such a situation requires some 'personal element' in the decision (e.g. it may be permissible to prevent a reviewer who has had previous negative dealings with the third party from procuring a ticket to provide a review of the third party's production, but may not be so in the sale of land, which lacks this personal element). Clearly, the contract will not be enforced where the third party specifically asks the agent to identify the principal and they withhold this information or misrepresent the position.

### **Archer v Stone (1898)**

#### **Facts:**

The defendant had asked the claimant if he was acting for a certain third party and was informed that he was not. This was untrue.

#### **Authority for:**

The contract was induced through a misrepresentation and as such, the party who told the lie cannot enforce the contract.

The principal cannot enforce the contract if it identifies that a contract under agency is excluded. Further, if the third party establishes the contract with the agent personally, rather than wishing to contract with a principal, this will stop the principal from acting on the contract.

- *Rights of the undisclosed principal:* Guidance was provided in *Siu Yin Kwan v Eastern Insurance Co.* regarding situations where an agent has failed to disclose the principal to a third party.

## ***Siu Yin Kwan v Eastern Insurance Co. (1994)***

### **Facts:**

The third party intended to claim on the insurance of an agent company. However, the company was wound up before the claim could be made. The court had to determine whether such a claim was possible against an undisclosed principal.

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### **Authority for:**

Where an agent fails to disclose the principal to a third party, the agent who possessed actual authority to contract will enable the principal to enforce the contract (and the principal will also be subject to claims against them). The agent will also be allowed to sue and be sued as to the terms of the contract. Any defences available to the third party against the agent would be exercisable against the principal. The agent must have intended to act for the principal when establishing the contract, and the contract may stipulate that the principal has no right to enforce the contract, or be sued under the contract.

## **18.6 Rights of an agent**

Having identified the obligations and duties that are placed on the agent, and their potential liability when acting without, or in excess of, authority, this section identifies the protection to which agents are entitled.

- *Indemnity:* The agent is entitled to indemnity from the principal with regard to any liability or for the costs associated in acting for the principal (to have any expenses repaid), unless this is specifically excluded in the agreement. Therefore, this provides protection for the agent where they may be exposed to costs or losses. However, this protection may be lost where the agent exceeds their authority or is liable for their own negligence.
- *Payment:* The agency agreement often involves a service being provided by the agent for the principal and this business transaction would involve the agent receiving some form of remuneration. This may be included in the contract between the parties as to the rate of remuneration and when payment will take place. In the absence of an express agreement to remuneration, this may be implied through the same mechanisms as it is with other contractual agreements, such as through the parties' conduct and what the court considers were the true intentions of the parties. The implied terms are important, but it is important to note that as with other implied terms, an express term will take precedence over inconsistent implied terms, even if this leads to unfairness.

- *To maintain the goods (lien):* An agent who is owed money from the principal or some other unsatisfied claim may maintain control over the property (or possess a lien over the goods) until the debt is satisfied. This right entitles the agent to the possession of the goods that they have lawfully come into possession of, but the right does not extend to disposing of the goods to realize the money owed.

This particular right is restricted to the goods/transactions relating to the debt owed and they must be in the agent's possession. Further, a lien exists where there is no exclusion to the right in the contract, and if the agent acts to waive their right (such as allowing the principal or their agent to take possession of the goods) then the agent loses the lien.

## 18.7 Termination at common law

An agency agreement may be terminated through many eventualities, including the death of either party, the mutual agreement of the parties, the fixed-term agreement coming to an end, the purpose of the agency

<sup>p. 470</sup> having been completed, through frustration, and issues ← concerning bankruptcy. If the contract is silent on the period of notice to be given, and the agent is not an employee and subject to the statutory minimum period, then a reasonable period of notice is due. This is determined on the facts of the case.

Whilst the statutory provisions of the Commercial Agents Regulations (18.8) provide for minimum periods of notice to bring the agency agreement to an end, at common law the agent acts for the principal under their authority. If the principal chooses to withdraw this authority, then the agency agreement ceases. When the principal chooses to terminate the agreement, it is prudent to inform third parties who may have had dealings with the agent acting for the principal to ensure that contracts under apparent authority are not established. However, where the agency agreement has been established through a contract, the terms of the contract, such as notice periods, must be adhered to or the principal may be liable for breach.

Commercial agency is a potentially very complex area and requires the parties to establish clear contractual terms and conditions to prevent problems.

### **Claramoda Limited v Zoomphase Limited (t/a Jenny Packham) (2009)**

#### **Facts:**

An agency continued to be held as a commercial agent beyond the point to which it had authority to negotiate, in accordance with the definition provided in the Commercial Agents Regulations 1993. Simon J held that an agency contract does not necessarily end when the agent stops negotiating sales on the principal's behalf.

### Authority for:

An intermediary must not conclude contracts in their own name (rather than that of the principal) or they will not be an agent for the purposes of the Commercial Agents Regulations.

## 18.8 The commercial agents (council directive) regulations 1993

The Regulations (as amended by S.I. 1993/3173) were established and brought into effect on 1 January 2004 to transpose Directive 86/653/EEC to harmonize legislation throughout the EU regarding contracts between commercial agents and principals, and to give additional protection to the status of agents in these relationships. The Regulations identify commercial agents as self-employed intermediaries (hence they do not apply to employee agents, but could apply to companies and partnerships) who have continuing authority to negotiate the sale or purchase of goods on behalf of/in the name of the principal (reg. 2(1)). The Regulations affected all agency contracts; however, the rights and obligations under this legislation are restricted to goods, rather than any services that an agent may provide. The Regulations also only protect those agents who are paid rather than volunteer their services (reg. 2).

The Regulations imposed duties onto commercial agents to act dutifully and in good faith for the principal, and to act in their interest. The Regulations codify the duties as ← outlined in 18.4 and require the agent to make proper efforts to 'negotiate, and where appropriate, conclude transactions that he is instructed to take care of; to communicate all necessary information to the principal; and to comply with reasonable instructions given by the principal' (reg. 3). The principal is obliged to act dutifully and in good faith in relation to the agent and in so doing must provide the agent with all necessary documentation relating to the goods; the principal must obtain for the agent information necessary for the performance of the contract, and (where appropriate) identify to the agent, within a reasonable period, once they anticipate that the volume of commercial transactions will be significantly lower than could reasonably have been expected; and the principal shall inform the agent within a reasonable time of their acceptance or refusal (or any non-execution) of a commercial transaction procured for the principal by the agent (reg. 4). Further, it is unlawful to attempt to contract out of these duties (reg. 5(1)).

The Regulations identify the rights of agents to remuneration in the absence of any agreement between the parties. The level of remuneration in such a circumstance shall be determined on the customary allowances in the locality of where the agent's activities are situated, and where no customary practice is present, this will be based on an assessment of reasonableness in relation to all aspects of the transaction (reg. 6(1)).

### 18.8.1 Indemnity and Compensation

The Regulations provide for indemnity or compensation payments on the termination of the contract (regs. 17 and 18) and the indemnity will not prevent the agent from seeking damages (reg. 17(5)). Indemnity is provided where the agent has brought the principal new customers or significantly increased the volume of business with the existing customers (reg. 17(3)(a)). The payment is equitable, having regard to all the circumstances

and, in particular, the commission lost by the commercial agent on the business transacted with such customers (reg. 17(3)(b)). The amount of indemnity cannot be in excess of a figure equivalent to an indemnity for one year, calculated by reference to the agent's actual pay over the previous five years or, where five years' work has not been completed, such time as has been worked (reg. 17(4)).

The compensation available is based on the damage suffered by the agent as a result (but not necessarily the fault of the principal) of the termination of the relations with the principal (reg. 17(6)). Damage is deemed to occur particularly when termination takes place in either or both of the following circumstances: those that deprive the agent of the commission that proper performance of the contract would have procured for them whilst providing the principal with substantial benefits; or those that have not enabled the agent to recoup (amortize) the costs and expense that they have incurred in the performance of the contract on the advice of the principal (reg. 17(7)(a) and (b)). Further, in relation to compensation payable, the House of Lords held in *Lonsdale v Howard and Hallam Ltd* [2007] that courts should look to the value of the income stream that the agency would have produced in assessing damages. In achieving this, expert testimony and elements such as the price that the agent could have achieved in selling the business will dictate the award of compensation.

These rights may not be waived by the agent through any agreement to their detriment (reg. 19), but the rights may be lost if the agent fails to inform the principal within one year of the termination of the agency contract that the agent intends to pursue the entitlement (reg. 17(9)).

### **p. 472 18.8.2 Excluding the Right to Indemnity and Compensation**

Regulation 19 states that the parties may not derogate from regs. 17 and 18 to the detriment of the agent before the contract expires. Regulation 18 provides where the compensation identified in reg. 17 shall not be payable. This situation exists where:

1. the principal has terminated the agency contract, justifiably, in relation to a breach of the contract identified in reg. 16;
2. the agent has terminated the contract (unless this termination is justified on circumstances attributable to the principal; or on grounds of the age, infirmity, or illness of the agent in consequence of which they cannot reasonably be required to continue his activities); or
3. the agent, with agreement from the principal, assigns their rights and duties under the contract to another person.

### **18.8.3 Termination of the Agency Under the Regulations**

An agency contract may be justifiably terminated and the Regulations will not apply where one of the parties has failed to carry out all or part of their obligations under the contract (or in the case of exceptional circumstances—reg. 16). Where the contract is not a fixed-term agreement, the Regulations provide for minimum notice periods of one month in the first year of the agency, two months' notice in the second year, and three months' notice after two years of the contract. As such, these are minimum periods that the parties

must adhere to, although they are free to negotiate longer terms if deemed appropriate and insofar as they are equal to both parties (reg. 15). Where a fixed-term contract continues beyond the term of the agreement, reg. 14 states that the contract is to be considered as an indefinite contract that is subject to reg. 15 procedures.

## Conclusion

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The chapter has identified agency relationships, their prevalence in business, and how the agency exists to bind the principal in contracts with third parties made on their behalf. Due to the nature of the agreement, obligations, potential liabilities, and rights exist for both the agent and the principal. It is essential that these are recognized, along with the statutory rights provided through the Commercial Agents (Council Directive) Regulations 1993, to minimize risk to the parties and to ensure the relationship is monitored and the authority of the agent is controlled. Contractual agreements specifically outlining the rights and limitations of the parties can assist in protecting all parties in agency.

The book continues by considering the various trading structures that may be formed to operate a business, and it offers a critique of the advantages and disadvantages each structure holds for the members.

## Summary of main points

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- Agency involves relationships between an agent, representing the principal in a way that may affect the principal's legal position, and third parties.
- Agency can apply to and affect the sole trader, partnerships, and corporations.
- Several types of agent exist depending upon their authority and how they may bind the principal.

### p. 473 Creation of agency

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- Agency agreements are easy to establish and may be formed through a contract, an agreement, by statute, through necessity, and through cohabitation.

## Authority of the agent

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### Actual authority

- An express agreement may be formed to establish the authority of the agent to bind the principal.
- Authority may be provided through implication.

### Apparent authority

- This occurs where the principal (or someone on their behalf) represents to the third party that the agent possesses the authority to act for the principal.
- To establish apparent authority there must have been a representation identifying the person as an agent; the principal, or someone on their behalf must have conveyed this representation; and the third party must have acted on the basis of it.

## Ratification

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- Where the agent (acting for the principal) has acted beyond their authority in establishing a contract with a third party, the principal may subsequently ratify the agreement.
- The agent must have been acting on the principal's behalf, the principal must have been in existence at the time of the contract being established, and the principal must possess the capacity to contract.

## Necessity

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- Where an agent has responsibility for the control of the principal's property, and in a situation involving an emergency, the agent may have the power to act and bind the principal where the agent does not possess actual or apparent authority. For this situation to take place the agent must have acted in good faith and it must have been impossible to communicate with the principal regarding the emergency and to gain their instructions.

## Duties of the agent

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- The agent must:
  - obey lawful instructions;
  - not delegate the duty without authorization;
  - exercise reasonable care and skill.
- The agent's fiduciary duties include:
  - not to take bribes;
  - not to make secret profits;
  - to avoid conflicts of interests;
  - to account to the principal.

## Liability of the agent

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- If the agent has acted beyond their authority, the third party is entitled to have the other party honour their side of the contract.
  - Generally, where the agent identifies they are working for the principal and establishes a contract on the principal's behalf, the agent has no liability under the contract with the third party.
- p. 474
- Where the agent has not identified the existence of the principal in the contract with the third party, the principal is prohibited from concluding the contract.

## Rights of the agent

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- The agent, in acting for the principal under the relevant authority, has the right to:
  - indemnity;
  - payment;
  - maintain goods (lien).

## The Commercial Agents Regulations 1993

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- The Regulations give rights and place obligations on commercial agents.
- The agent has to make proper efforts to negotiate and conclude the transactions required of them, to communicate relevant information to the principal, and to comply with the reasonable instructions of the principal.
- The principal is obliged to act in good faith to the agent in providing relevant information, the volume of commercial transactions if these are likely to be lower than anticipated, and their acceptance or otherwise of transactions procured by the agent.
- The Regulations identify issues of remuneration, indemnity, and compensation payable.

## Termination of the agency

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- At common law, the agreement may be terminated in compliance with the contract, or where the parties are no longer able to carry out their duties; in cases of bankruptcy, frustration, and so on.
- The termination of a commercial agency agreement is protected through the Commercial Agents (Council Directive) Regulations 1993.
- The Regulations provide for a minimum of one months' notice of termination in the first year of the agreement, two months' notice in the second year, and three months' notice after two years (although the parties can apply longer periods applicable to each other).

## Summary questions

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### Essay questions

1. ‘The fiduciary and contractual duties implied into the contract of an agent are fair, albeit they are demanding.’  
Discuss.
2. ‘The creation of agency by operation of the rules of common law are dated but still are considered good law.’  
Discuss the above in relation to necessity and cohabitation.

### Problem questions

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1. James operates a business, All Bright Consumables (ABC), which trades in DIY goods to electricians and traders. As James is expanding his business in other areas and has become too busy to manage ABC personally, he appoints Brenda to manage the operation. Brenda is engaged on a three-year fixed-term contract with payment by commission of 7 per cent of the sales the business makes. One stipulation James makes as part of the agreement with Brenda is that Brenda does not deal with ABC’s major rival business, XYZ.

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← At the beginning of the engagement, all parties are happy as business is good. However, soon afterwards the economy begins to move into recession and business slows. The result is Brenda’s commission from sales is dramatically reduced and despite her pleas to James to increase her rate of commission, James refuses. Brenda is soon approached by XYZ who offer her a business opportunity. If she agrees to sell XYZ’s electric shower for them to ABC customers, they will deliver the showers to the customers directly from XYZ’s warehouse. As this will be ‘their little secret’, James need never know and XYZ will give Brenda 30 per cent of the profits from the sales.

Sometime later, James is at a trade event where he is approached by an acquaintance who expresses to James his disappointment at the quality of the showers they are now selling. Further, he informs James that due to this choice of poor quality components he has had to suggest to his customers that they do not purchase from ABC. When James enquires about his acquaintance’s concerns, he is shocked to discover that the showers are from XYZ.

James immediately challenges Brenda about the truth of this situation, which she confirms. Brenda also says that she has had several customers return the showers as being of very poor quality and wanting a refund as they purchased them from the ABC store. Further, XYZ are refusing to accept any returns.

Explain the legal position of the parties using agency law.

2. ABC Ltd operates a business of selling specialist cars and difficult-to-source car spares to customers and at auctions. It manages this through engaging representatives for regions around the UK who source the goods on behalf of ABC Ltd. ABC Ltd appoint Billy as its representative for the North West of England, on contractual terms of a three-year irrevocable engagement, where he will receive a commission of 35 per cent of the profits

made by ABC Ltd on the sale of the goods he acquires. An important aspect of the contract is that Billy is instructed not to obtain Ford cars or spare parts as these can prove difficult to sell. Billy is issued with a letter of introduction from ABC Ltd identifying him as the company's 'associate for the North West'.

Two months after his engagement began (on 5 July), Billy was approached by Stock-Cars who informed him that they had a mint-condition 1967 Ford Mustang, which was currently on display at the National Museum of American History until 2 November, which he could buy for £25,000. In the negotiations with Stock-Cars, Billy identified that he was acting on behalf of 'a specialist car-buying company' and that 'his principal will wait until the conclusion of the exhibition before taking delivery of the vehicle'. Billy and Stock-Cars agree that payment in full will be made within 30 days of 2 November when the vehicle is available. Having concluded the deal, on 8 July Billy reaches an agreement to sell the vehicle to Jack Vegas, a specialist car enthusiast, for £40,000, with delivery being made on 5 November. Billy intends to keep the profit made as 'a perk' by not informing ABC Ltd of the deal.

Soon after the meeting on the 8 July, Jack Vegas spoke with Stock-Cars about another vehicle he was interested in, and mentioned the car he had agreed to buy from Billy. Stock-Cars thus realized that they had sold the Ford Mustang too cheaply, and having investigated Billy and found that the 'specialist car-buying company' he worked for was ABC Ltd, they informed ABC that they would not proceed with the sale. On 9 July, in an attempt to secure the profitable sale to Jack Vegas, ABC Ltd informed Stock-Cars that they refuse the repudiation of the contract made with Billy, and insist on delivery as agreed.

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In relation to the agency principles applicable to the problem, identify the rights of the parties. ←

You can find guidance on how to answer these questions **here** <<https://oup-arc.com/access/content/marson6e-student-resources/marson6e-chapter-18-indicative-answers-to-end-of-chapter-questions?options=name>>.

## Further reading

### Books and articles

Baskind, E., Osborne, G., and Roach, L. (2019) Commercial Law (3rd Edition) Oxford University Press: Oxford.

Korotana, M. S. (2002) 'Privity of Contract and the Law of Agency: A Sub-agent's Accountability to the Principal' *Business Law Review*, Vol. 23, p. 73.

Munday, R. (2016) Agency: Law and Principles (3rd Edition) Oxford University Press: Oxford.

### Websites

<http://www.legislation.gov.uk/uksi/1993/3053/contents/made> <<http://www.legislation.gov.uk/uksi/1993/3053/contents/made>>

The Commercial Agents (Council Directive) Regulations 1993.

## Online Resources

Visit the online resources [https://oup-arc.com/access/marson6e-student-resources#tag\\_chapter-18](https://oup-arc.com/access/marson6e-student-resources#tag_chapter-18) for further resources relating to this chapter, including self-test questions, an interactive glossary, and key case flashcards.

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