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A Framework of Analysis for the Law of Agency

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A FRAMEWORK OF ANALYSIS FOR THE LAW OF AGENCY

Ronald C. Wyse*

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I. INTRODUCTION

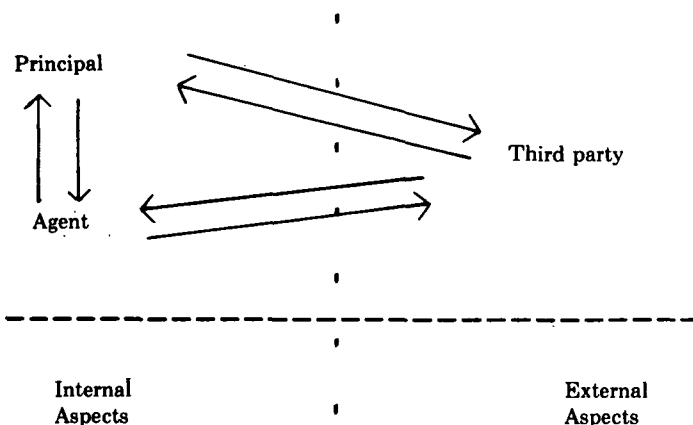
For several years I have been concerned about the degree of confused thinking reflected in some student examinations and many of the reported cases dealing with the law of agency. While some of the confusion can be traced to the inherent difficulty of the subject and its evolutionary development (or to inadequacies in the

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pedagogue's method), much of the difficulty results from an inability to perceive the skeletal framework of this body of law. Thus, the purpose of this monograph is simply to present the main thrust of agency law and to suggest an analytical framework which will facilitate solving agency problems and serve as a starting point for more detailed research into specific nuances.

To begin with, the law of agency pertains to those multi-party transactions where the agent acts for or on the behalf of a principal in various relationships with third parties. The recognition of the multi-party nature of the relationship is crucial if one is to appreciate the rights, duties, and liabilities created in these transactions. Every agency transaction includes at least three different sets of rights and duties, as illustrated by Figure 1:

Figure 1:



Another way of visualizing the necessary differences in the relationship is to consider the principal-agent aspects of a transaction as *internal* considerations, while principal-third party and agent-third party relations are *external* matters.

In addition to recognizing the multi-party nature of agency transactions, one should also distinguish the agency aspects of a problem from basic tort or contract law. Problems dealing with basic tort or contract principles generally require: (1) an analysis of whether or not there was a tort or contract duty; (2) whether that duty was breached; and (3) whether the defendant's breach caused compensable injury to the plaintiff. Agency analysis, however, is not concerned with whether there is *any* liability, but *to whom* the liability runs. Expressed differently, the basic tort or contract issue becomes a threshold question which must be resolved before considering the application of agency principles. If there is no underlying

tort or contract, one need not be concerned with the extension of liability to the principal arising out of the acts of the agent.

II. FORMATION OF THE AGENCY RELATIONSHIP

Once it has been determined that there is an underlying tort or contract, however, the initial step of any agency analysis must be to inquire if an agency relationship exists between the tortfeasor or person who entered into the contractual relationship and the putative principal. Thus, one must consider the elements of the basic agency relationship.

As stated in the Restatement (Second) of Agency § 1 (1958) (hereinafter Restatement), agency is the "fiduciary relation which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act." While the agency relationship is clearly consensual, it should be noted that there need not be a contract between the principal and the agent, although many common agency relationships are contractual. A simple manifestation of consent by the parties is sufficient and no consideration is necessary.¹ Further, the consent may either be express or implied from the conduct of the parties.

In many common multi-party transactions, the presence of an agency relationship is readily apparent and requires no analysis. Cases involving acts by salaried employees, attorneys for their clients or corporate officers for their corporations obviously create no problems in this regard as the requisite mutual consent is evident from the status of the actor. On the other hand, courts have had considerable difficulty in transactions where one party consents to act gratuitously for the benefit of another, and it is unclear from the facts whether the person whom the act benefited had knowledge of the activity. As this issue has arisen rather frequently in litigated cases, the courts have tended to look for the presence of three factors in determining whether an agency can be implied in the absence of express consent by the principal. The first of these is whether a manifestation of assent by the principal can be found. In two similar and widely cited cases, a finance company instructed an employee to repossess an auto and the employee obtained the assistance of another person to drive the repossessed car. While doing so, the assistant negligently injured a third party who sued the finance company as a principal. In *White v. Consumers Financial Service, Inc.*,² the Pennsylvania Supreme Court refused to find the necessary

1. See, e.g., *Holmes v. McKey*, 383 P.2d 655, 665 (Okla. 1962).

2. 339 Pa. 416, 15 A.2d 142 (1940).

assent by the defendant finance company as it had not given its employee express authority to use an assistant and, in the court's opinion, could not have necessarily assumed that an assistant would be required to carry out the task it had given to its employee.³ A few months later, the Third Circuit, applying Pennsylvania law, distinguished *White* on similar facts and implied the necessary assent on the ground that the finance company should have known that its employee would need help in returning both his car and the repossessed auto.⁴ Thus, assent in this context seems to mean acquiescence or something like implied consent.

The second factor relating to the determination of whether an agency relationship exists is whether the act by the alleged agent provides some degree of benefit to the putative principal. This concept is helpful in distinguishing an agency relation from a simple bailment. For example, if Mr. X leaves his car in a parking lot which requires that the keys be left with the attendant so that the cars can be moved about, X has certainly assented to the limited movement of the vehicle by the attendants; but the "benefit" of being able to move the auto runs to the owner of the parking lot rather than to X. Thus an accident caused by the movement of X's auto would not justify imposing liability on X. Distinguish this from the typical use of a company auto by a salesman.

An extension of this "benefit" concept resulted in the so-called family purpose doctrine, in which courts find a fictitious benefit to the "business" of the family when the family auto is used by a member of the household for his own pleasure.⁵ By conjuring up a fictitious business, the courts manage to impose liability directly on the owner of the auto and indirectly on the owner's liability insurer. Such tortuous logic is no longer necessary since many states by statute make the owner of an auto liable for the negligence of any person who drives the car with the consent of the owner.⁶ In addition, most insurance policies now protect anyone driving with the express or implied consent of the owner, and such a provision is mandatory in Montana.⁷

The third factor is that the putative principal must have some element of control over the alleged agent. While control, or the right to control, is an essential element in determining whether a principal is to be held vicariously liable for the torts of his agent (which

3. *Id.* at 421, 15 A.2d at 144.

4. *Waggaman v. General Finance Co.*, 116 F.2d 254, 259 (3rd Cir. 1940).

5. See W. PROSSER, *HANDBOOK OF THE LAW OF TORTS* 483 (4th ed. 1971).

6. See PROSSER, *supra* note 5, at 486.

7. MONTANA CODE ANNOTATED [hereinafter cited as MCA] § 61-6-103 (1978) (formerly codified at REVISED CODES OF MONTANA (1947) [hereinafter cited as R.C.M. 1947], § 53-438).

is discussed at length below), the presence or lack of control of an individual's performance is clearly indicative of whether an agency relationship exists. For example, a grain elevator company sold grain to a corporate entity which subsequently resold the grain to a large livestock feedlot operator. When the corporate intermediary defaulted in payment, the elevator company sued the feedlot operator as an undisclosed principal. In upholding a jury verdict finding no agency, the Montana Supreme Court emphasized the lack of control the feedlot operator had over the alleged corporate agent, noting that the putative principal (1) owned no stock and had no financial interest in the corporation; (2) made no financial advances or loans to the corporation; (3) dealt with the intermediary in an arms-length manner through contracts; and (4) purchased grain from other such intermediaries.⁸ The retention of the right to specify the quality of grain to be received and the manner of delivery was not found to be inconsistent with this holding. Had the specified facts been found to be otherwise, it is likely that a contrary conclusion would have been reached.

It is also possible to create a form of agency by operation of law. Statutory agents are typically created for special limited purposes such as an agent for service of process. Examples include the qualification of foreign corporations where the qualification includes the designation of a "registered agent" for service of process or statutes that provide for service of process upon a state official if a non-resident is involved in a highway accident.⁹

Lastly, one should be aware that an agency can be created by estoppel. In Montana, such an agency is referred to as an "ostensible agency,"¹⁰ and as in ordinary estoppel cases, requires (1) a representation by the alleged principal that a particular individual is an agent that (2) induced a change of position in reliance upon such representation by the third party.¹¹

III. THE AGENCY RELATIONSHIP IN TORT

As pointed out above, basic tort problems tend to present relatively simple fact situations that involve discussion of whether any liability is created. Such problems can be shown by Figure 2:

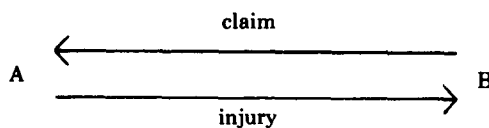
8. *Farmers Elevator Co. v. Pheister*, 153 Mont. 152, 157, 455 P.2d 325, 328 (1969).

9. See MCA § 35-1-1009 (1978) (formerly codified at R.C.M. 1947, § 15-22-104) regarding qualification of a foreign corporation and MCA § 25-3-602 (1978) (formerly codified at R.C.M. 1947, § 53-202) pertaining to non-resident drivers.

10. MCA § 28-10-103 (1978) (formerly codified at R.C.M. 1947, § 2-106).

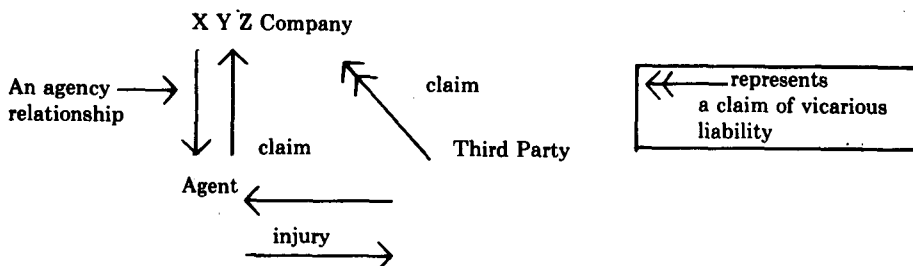
11. See *Calkins v. Oxbow Ranch, Inc.*, 159 Mont. 120, 126, 495 P.2d 1124, 1127 (1972).

Figure 2:



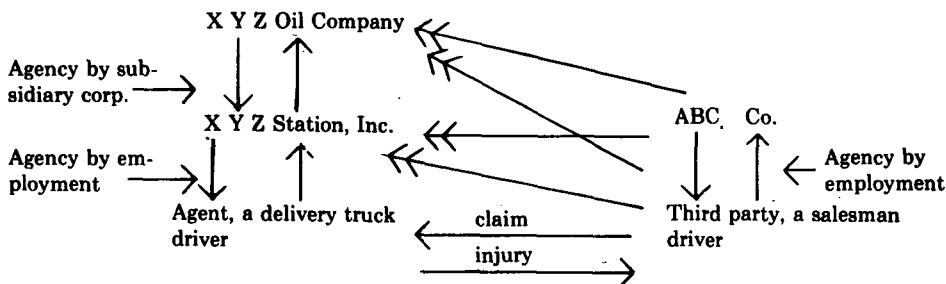
The typical multi-party agency situation involves a more complex organization. A typical problem can be shown by Figure 3:

Figure 3:



Even this illustration can over-simplify the realities of a transaction as indicated in Figure 4:

Figure 4:



Notwithstanding the complexity of potential problems, one can usually segregate the various legal issues created by such a transaction as follows:

1. The Agent-Third Party claim and injury is our basic tort question.
2. Questions regarding the rights and liabilities of XYZ Oil Co. to XYZ Station and Station to Agent, as well as the relationship between ABC Co. and Third Party, all relate to the internal aspects of those agency relations.

3. The claims of Third Party against Oil or Station, or ABC against Oil or Station, turn on the external aspects of the agency involving Agent truck driver. Since neither Oil nor Station is personally at fault in Figure 4, liability, if any, must be imposed vicariously.

A. *The Policy Basis of Vicarious Liability*

Since the object of vicarious liability is to impose tort liability upon one who is not personally at fault, a recognition of the policies supporting such a doctrine in general is useful before one considers the specific language used in agency law to impose liability on a principal for the torts of his agent. The following policy grounds have been identified as influencing courts' decisions to impose such liability.

First, the imposition of vicarious liability will encourage principals to use care in the selection of their agents. While obviously a negligent selection of an agent (hiring a school bus driver without first inquiring into the applicant's driving history, for instance) would make the principal directly rather than vicariously liable, a principal can insulate himself from direct liability for negligence by simply instituting reasonable hiring and supervisory procedures. Vicarious liability, however, by making the principal liable without personal fault, tends to cause principals to hire the best applicants and to take steps to avoid accidents to third parties beyond those required by the hypothetical reasonably prudent person. This extra burden has been described somewhat hyperbolically as "the most valuable check in the conduct of social life."¹²

Others have noted that the "real reason" for imposing vicarious liability is simply a "deep pocket": since the agent (employee) is unlikely to possess sufficient assets to permit compensation of the injured party, the liability is shifted to the principal (employer) who is more likely to be able to pay.¹³ The more generally accepted view, however, has focused on the ability of principals, especially in a commercial setting, to distribute the risk of loss arising out of the torts of their agents by either increasing the sale price of the goods or services that they sell, or by obtaining insurance.¹⁴

B. *The General Rule of Vicarious Liability*

While courts seldom enunciate the policy factors underlying their decisions, the recognition of the policies often assists the

12. Laski, *The Basis of Vicarious Liability*, 26 YALE L. J. 105, 114 (1916).

13. See, e.g., BATY, *VICARIOUS LIABILITY* 154 (1916).

14. See Smith, *Frolic and Detour*, 23 COL. L. REV. 444, 456, 461 (1923).

reader in understanding why the court reached its conclusion. Further, these policies support the general rule of liability of a principal for the torts of his agent which can be stated as follows:

A principal will be vicariously liable for the physical harm caused by the torts of his agent if:

- (1) the principal controls or has the right to control the physical conduct of the agent in the performance of the agent's duties, and
- (2) the injury occurred while the agent was acting within the scope of his employment.

C. Issues To Be Considered in the Application of the General Rule of Vicarious Liability

In order to apply the general rule and conclude that the principal is liable for the torts of his agent, one must consider four separate issues:

1. Does any agency relations exist between the alleged principal and the person who caused the injury?
2. Having concluded that there was some kind of agency relation, was it the particular kind of relation that permits the imposition of vicarious liability? In other words, did a master-servant relationship exist?
3. Was the servant acting within the scope of his employment when the injury occurred?
4. Was the tort committed by the servant the kind of tort that supports the imposition of vicarious liability?

While each of these issues will be discussed in more detail, one should remember two other points at this time. In a tort setting, the agent is personally liable for his own tortious acts. Thus, while our main inquiry is whether or not liability should be vicariously extended to the principal, the agent is always liable to the injured party under ordinary tort principles. Secondly, one should also remember that the general rule is not all inclusive. There are several exceptions to it that one must also consider. These too are discussed below.

1. Does an Agency Relationship Exist?

Returning to the four issues included in the application of the general rule, the first issue requires a determination that some agency exists. As previously mentioned, in many instances, the existence of the relationship is uncontroverted. In other cases, the courts tend to apply the "assent, benefit, and control test" described earlier. The point here is to simply emphasize that the exist-

ence of an agency relationship is a necessary precedent to an analysis of vicarious liability.¹⁵

2. *Does a Master-Servant Relationship Exist?*

Having found an agency relationship, one must then determine whether or not this is the particular kind of agency that supports vicarious liability. The general rule indicates that a principal will only be liable for torts committed by those agents "whose physical conduct in the performance of the [principal's] service is controlled or is subject to the right to control by the [principal]."¹⁶ If the principal has this necessary control of or right to control the physical conduct of the agent, then our principal is called a *master*, and the agent who is subject to such control is called a *servant*. Obviously, every master is a principal, but every principal is not a master. Likewise, every servant is an agent, but every agent is not a servant. The control of or right to control the physical conduct of the agent in the performance of the principal's service is the key to imposing vicarious liability in agency law. This is the crucial distinction between a simple agency such as that which exists between an attorney and his client, and the kind of agency that supports the imposition of vicarious liability. While this distinction may appear artificial, limiting the imposition of vicarious liability to master-servant cases is consistent with the general policies supporting vicarious liability. As the master-servant relationship tends to arise in employment transactions, we are usually dealing with circumstances where risk distribution, deep pockets, and the ability to use care in the selection of employees are relevant.

Modern courts have indicated a willingness to find a theoretical "right to control" in cases where the policy grounds for imposing vicarious liability are strong. Thus, an argument for imposing liability can be made by emphasizing those aspects of a relationship that could be directed by the principal even though very little actual control was exercised. For example, an appliance store sold a new furnace to a homeowner and agreed to remove the old furnace. The company hired a part-time, casual laborer to dismantle and haul away the old furnace. The laborer negligently injured the homeowner while attempting to break up the old furnace with a sledge hammer. There was no evidence that the agent laborer was directed to break up the old furnace nor was any representative of the selling store present to actually supervise or control their agent's actions. In addition, it was clear that once the hammer began its swing, no

15. See *Harri v. Isaac*, 111 Mont. 152, 162, 107 P.2d 137, 142 (1940).

16. RESTATEMENT (SECOND) OF AGENCY [hereinafter cited as RESTATEMENT] § 2 (1958).

one could in fact direct its control. A Missouri Court of Appeals in 1969, however, had no trouble upholding a jury verdict imposing liability in a similar case on the grounds that the employer had a right to control the laborer's conduct in the performance of these duties had it chosen to exercise that right.¹⁷

Another typical class of cases involving the "right to control" issue arises when a traveling salesman negligently injures a third party while driving his own car between cities where customers are located. Obviously, the principal has no actual control over the auto at the time of the accident, but courts that have imposed liability have emphasized (1) the right of the principal to direct that the agent use a particular route, (2) that the agent call upon a particular customer at a specified time, and (3) that the nature of the job required the use of an auto.¹⁸

3. *Was the Servant Acting within the Scope of His Employment When the Tortious Act Was Committed?*

Having concluded that our tortious agent falls within the master-servant classification, one must then determine if the injury occurred while the agent was acting within the scope of his employment. In general, a determination of the scope or course of employment is nothing more than a determination of what duties the agent (servant) was engaged to perform. Courts have been fairly willing to extend the scope of employment to any activity reasonably related to the main job the agent was to perform. For example, a ranch worker who was required to perform duties some distance from any eating place was normally furnished a box lunch by his employer. On a day that the lunch was not furnished the worker negligently started a fire while attempting to prepare a meal. The employer was held liable since the nature of the duties required some means of feeding workers on the job. Thus the worker's negligence was within the scope of employment.¹⁹

17. *Bonenberger v. Sears, Roebuck and Co.*, 449 S.W.2d 385, 390 (Mo. App. 1969). The sheet metal company hired by the appliance store to install the furnace was found by the court to have the right to control the manner in which its agent performed his services because it was the company's duty to dispose of the furnace, the company undertook to dispose of the furnace's parts, and the agent was directed to get the parts and dispose of them. *Id.*

18. *Compare Peterson v. Brinn & Jensen Co.*, 134 Neb. 909, 911-12, 280 N.W. 171, 172 (1938) (salesman required to use own car and subject to right of employer to direct his route was an "employee," and employer liability thus attached) with *Harrington v. H.D. Lee Mercantile Co.*, 97 Mont. 40, 56, 33 P.2d 553, 558-59 (1934) (salesman owning and operating automobile at his expense, working on a commission, and following his own itinerary was not a "servant," and thus no employer liability attached).

19. *Bugge v. Brown*, 26 C.L.R. 110, 128 (Australia 1919).

In another widely cited case, *Nelson v. American-West African Line, Inc.*,²⁰ the boatswain of a commercial ship, whose duties generally included supervision of the ship's merchant seamen, returned to ship "roaring drunk" amid "much noise, disorder and violence." Although the plaintiff was not due to go on watch for 30 minutes, the boatswain decided that he should get up and go on deck at once. Crying out, "Get up, you big son of a bitch, and turn to," he struck the plaintiff across the face with a wooden bench while he lay in his bunk. Judge Learned Hand had no problem finding that those facts supported a cause of action against the boatswain's employer, on the ground that while the motives of the boatswain may have been mixed, that "if the boatswain intended to act for the ship at all, his command was within his powers"²¹ In other words, having given A the general power to direct the seamen on the ship, the principal would be liable even if this power was abused by A so long as a jury could find that some part of the boatswain's motive was to perform the principal's business.

Another class of cases that arises within the scope of employment issues includes those characterized by "frolic and detour"—those cases in which the servant clearly deviates from his assigned duties in order to accomplish a personal objective and negligently injures a third party before clearly returning to his duties. The traditional language is that the employer shall not be liable if the servant causes the injury while engaged on a personal frolic, but shall be liable if the servant had merely detoured from his assigned tasks.²²

Whether a servant had returned to his master's task was the critical issue in two well-known cases. In *Riley v. Standard Oil Co.*,²³ the agent was directed by his employer to deliver goods by truck to a freight yard and to return. After delivering the items, he picked up a load of scrap lumber at the freight yard and took it to his sister's house some four blocks away. On his way back toward the freight yard and his employer's place of business, the agent negligently injured the plaintiff. The New York Court of Appeals held that while the trip to the sister's house was probably not within the scope of the agent's employment, a jury could find that the agent had returned to his duties when the accident occurred.²⁴

The same court that decided *Riley* had an opportunity to consider the issue again the next year in another case involving an agent

20. 86 F.2d 730 (2d. Cir. 1936).

21. *Id.* at 732.

22. See *Harrington v. H.D. Lee Mercantile Co.*, 97 Mont. 40, 59, 33 P.2d 553, 558 (1934).

23. 231 N.Y. 301, 132 N.E. 97 (1921).

24. *Id.* at 306, 132 N.E. at 98.

truck driver who deviated from his master's instructions to satisfy a personal desire. In *Fiocco v. Carver*,²⁵ the driver had been instructed to return the truck to its garage on the west side of New York after making a delivery but instead drove the vehicle to the east side of town where a street carnival was in progress. After giving a ride on the truck through the district to a number of children, the driver stopped at a pool hall to visit a friend. The plaintiff, an eleven-year-old, was injured as the truck departed from in front of the pool hall as the driver started to return the truck to the garage. The court held that as a matter of law the driver had not returned to his master's business at the time of the accident and distinguished the holding in *Riley* on the ground that this issue is not to be decided "by tests that are merely mechanical or formal." Rather, the facts of each case must be analyzed in order to determine whether the "dormant purpose" of the agent at the time of the accident was the performance of the master's business. As the deviation from the authorized route in this case was considerably greater than the deviation in *Riley* in both length of time and distance, and as the injury occurred just as the vehicle commenced to move after a clearly unauthorized stop, a jury could not be permitted to find that the driver had returned within the scope of his employment.²⁶

The degree of deviation from instructions and the foreseeability that some deviation might well occur was the basis of the holding in another similar case. In this instance, the agent, when directed by his employer to proceed to a particular destination over 100 miles to the west of the employer's place of business over a particular route, deviated about 18 miles north of that route to accomplish a personal task. He then proceeded on a parallel route to a point approximately 20 miles due north of the assigned destination when he negligently injured the plaintiff. Liability was imposed on the employer on the grounds that a jury could conclude that the driver was clearly proceeding towards the assigned destination when the accident occurred, and that the employer should have foreseen that some deviation from the exact route would occur on a trip of this length. Therefore, the driver had returned to the business of his master when the injury occurred.²⁷

A problem that is related to the scope of employment issue arises when the agent (servant) of principal #1 commits a tort while working for principal #2. This is the "loaned or borrowed servant"

25. 234 N.Y. 219, 137 N.E. 309 (1922).

26. *Id.* at 224, 137 N.E. at 311.

27. *Kohlman v. Hyland*, 54 N.D. 710, 718, 210 N.W. 643, 645-46 (1926).

class of cases and has given the courts some difficulty in finding a basis for liability due to a common law concept that stated that a servant could only have a single master. While this may have been a useful concept in feudal England, it is not very satisfactory today. For example, the loaned servant issue typically arises today when principal #1 leases heavy machinery such as a crane or tractor and trailer with a skilled operator to principal #2. The tort is committed while using the machinery under the general direction of principal #2. In cases where both principals have a sufficient right to control the operator to meet the usual master-servant test, the courts have had difficulty deciding which principal should be subject to vicarious liability.²⁸ In cases like these the courts have tended to place liability on either: (1) the principal who was exercising control at the time the injury occurred, or (2) to look to whose business was primarily being served at the time of the injury.²⁹ Section 226 of the Restatement now recognizes the possibility of a servant having more than one master while recognizing the "control at the time" and "whose business" distinctions noted above. In *Gordon v. S.M. Byers Motor Car Co.*,³⁰ the Pennsylvania Supreme Court found both principals liable in a case where the control was approximately equal and both businesses were being served.³¹ Further, a recent California appellate court decision was quite critical of using the control test in a dual employment case, and upheld a jury verdict against both employers expressly on policy grounds in that each employer was in a position to obtain insurance and thus distribute the risk of loss.³² One can anticipate that future cases in this area are likely to apply similar rationales and thus are more likely to find both masters liable.

4. *Was the Tortious Act within the Class Which Supports Imposition of Vicarious Liability?*

The fourth issue that must be considered in order to apply the general rule of vicarious liability is whether the tort committed by the servant was the kind of tort that traditionally supported the imposition of vicarious liability. Generally speaking, vicarious liability is limited to negligent acts of agents. Thus, a special problem is presented when the injured party is harmed by the intentional act of the agent. To a degree, this issue is closely related to the scope

28. See, e.g., *Aluminum Co. of America v. Ward*, 231 F.2d 376 (6th Cir. 1956).

29. *Id.* at 379.

30. 309 Pa. 453, 164 A. 334 (1932).

31. *Id.* at 459, 164 A. at 336.

32. *Strait v. Hale Construction Co.*, 26 Cal. App. 3d 941, 103 Cal. Rptr. 487 (1973).

of employment problem in that an agent is seldom acting within the scope of his employment when he commits an intentional tort such as battery. It should be recognized, however, that some kinds of employment involve potential physical force (such as with guards and armed watchmen), and, as indicated in the *Nelson* case, which involved the drunk boatswain, a servant can commit intentional torts while attempting to carry out his duties.

While intentional torts can be found to be within the scope of one's employment, generally courts have not so found if the act is especially violent and unforeseeable. Thus, a court has imposed liability on the employer of a truck driver who got into a fist fight with another trucker after arguing over a parking space at a delivery dock. The driver was attempting to further the principal's business and arguments and fist fights are not totally foreign to the trucking business.³³ In contrast, however, another court refused to hold the employer of a bus driver liable when he shot the driver of a car that had cut in front of the bus which had led to harsh words and a confrontation.³⁴ Consistent with this approach, the Montana Supreme Court upheld a jury verdict against an employer for injuries which arose out of an assault by the employer's agent upon the plaintiff. In doing so, the court emphasized that under the circumstances, the employer should have foreseen that an altercation might occur as the agent had been sent to repair an earthen dam that had been the subject of a long-standing controversy between the plaintiff and defendant employer.³⁵

D. *Limitations upon the Application of the General Rule of Vicarious Liability*

As a more general limitation on the imposition of vicarious liability, one should note that the general rule is limited to torts that cause tangible personal injury or property damage to third persons. Tortious acts by agents causing economic injury only, such as fraud or deceit, are not grounds for the imposition of liability on the principal unless the agent is authorized to make statements such as the one made.³⁶ This is the only time authorization is an issue in determining the principal's liability for an agent's tort. The discussion of authority with reference to contractual matters which follows is relevant here. One should also note that the agent need not be

33. *Schisano v. Brickseal Refractory Co.*, 62 N.J. Super. 269, 162 A.2d 904 (1960).

34. *Birmingham Electric Co. v. Hawkins*, 37 Ala. App. 282, 67 So.2d 56 (1953).

35. *Kornec v. Mike Horse Mining & Milling Co.*, 120 Mont. 1, 10, 180 P.2d 252, 257 (1947).

36. See RESTATEMENT, *supra* note 16, § 257.

authorized to make the false or misleading statement, but merely be authorized to make statements of the type that were false in the given case. That is, if a salesman is authorized to make statements regarding the quality of P's goods, P will be liable if the salesman makes a false statement regarding quality.³⁷

The converse of the general rule for the imposition of vicarious liability is that an alleged principal is not liable for the torts of independent contractors. Since the term independent contractor is defined to include all persons who contract to do something for another, but are not controlled or subject to the right of control with respect to the physical performance of the undertaking by that other person, it should be clear that this is not truly an exception to the general rule, but simply another way of stating that rule. In short, the terms independent contractor and servant are mutually exclusive. An independent contractor may or may not be an agent; the key is simply control or right to control.³⁸

One should also watch for facts that make the alleged principal liable under ordinary tort principles for his own acts. Thus negligent supervision or selection of employees can be grounds for liability without reference to vicarious liability.³⁹ Likewise, the intentional direction of the agent to commit a tort by the principal would be grounds for liability under traditional tort rationales.⁴⁰

There are, however, several catch phrases used by courts to impose liability upon principals vicariously under circumstances where the normal application of the general rule would not apply. These phrases include, "inherently dangerous activities," "publicly franchised activities," and "estoppel," and can be thought of as exceptions to the general rule.⁴¹ It should be noted, however, that the parameters of these exceptions are rather vague and nebulous. In general, in the cases in which liability has been imposed, the facts reflect instances where the policy bases for imposing vicarious liability are particularly strong. Unfortunately, as courts are usually unwilling to expressly find liability on policy grounds, the cases tend to be difficult to reconcile on the language of the opinions. The recognition that the underlying rationale for a particular holding may be an unexpressed policy factor does, however, help one reconcile otherwise conflicting opinions and suggests a basis for arguing for liability in future cases notwithstanding adverse precedent. For

37. See, e.g., *Weise v. Red Owl Stores, Inc.*, 286 Minn. 199, 175 N.W.2d 184 (1970).

38. See *RESTATEMENT*, *supra* note 16, § 2.

39. See *PROSSER*, *supra* note 5, at 469-70.

40. See *W. SELL*, *AGENCY* 81 (1975).

41. See *PROSSER*, *supra* note 5, at 470-74; *Williamson v. Southwestern Bell Tel. Co.*, 265 S.W.2d 354 (Mo. 1954); *Santise v. Martins, Inc.*, 258 App. Div. 663, 17 N.Y.S.2d 741 (1940).

example, in *Elkins v. Husky Oil Co.*,⁴² the plaintiff was injured by fire resulting from a gas station attendant's carelessness in permitting gasoline to overflow while filling the tank of plaintiff's car. The plaintiff's theory of suit was that the owner of the station was the servant of defendant Husky Oil, and thus attempted to hold Husky liable vicariously. Although the court recognized the "intrinsically dangerous" exception to the general rule, the court refused to apply it in this case and affirmed the District Court's grant of a motion for summary judgment in favor of the defendant with a rather confused discussion relating to the difference between servants and independent contractors.⁴³ While part of the problem with the decision could have been rectified by a clearer enunciation of the difference between a servant and an independent contractor, an argument for liability based on policy grounds might have caused the court to make a more diligent effort to at least give the plaintiff a day in court.

Another group of cases which are hard to fit into the general rule are the cases involving accidents caused by smoking by employees. Obviously, very few employees' duties require them to smoke thus presenting a serious obstacle to application of the "scope of employment" issue. It is foreseeable, however, that employees will smoke and do so negligently, even though contrary to express instructions by the employer. In cases where the employee is required to work around flammable materials such as paint or petroleum products, some courts have imposed liability on the employer by characterizing the activity as "inherently dangerous" or "non-delegable."⁴⁴

Commercial activities that are granted a public franchise, and thus a limited monopoly, have also been denied the opportunity to avoid liability by having work done by persons who would otherwise be classified as independent contractors due to the lack of control. This "publicly franchised activity" exception can also be viewed as a non-delegable duty, in that the rationale includes the concept that the grant of the franchise requires an assumption of the burdens as well as the benefits. Note that the activity performed by the other person must be within the scope of the franchise — that part of the franchised activity that non-franchise holders are prohibited from doing.⁴⁵

42. 153 Mont. 159, 455 P.2d 329 (1969).

43. *Id.* at 167-68, 455 P.2d at 334.

44. Compare *Herr v. Simplex Paper Box Corp.*, 330 Pa. 129, 198 A. 309 (1938) (employer not liable), with *Maloney Tank Mfg. Co. v. Mid-Continent Petroleum Corp.*, 49 F.2d 146 (10th Cir. 1931) (employer liable because of "inherent danger").

45. See, e.g., *Williamson v. Southwestern Bell Tel. Co.*, 265 S.W.2d 354 (Mo. 1954).

Another class of cases which seems to be an exception to the general rule are those which involve principles of estoppel. As in ordinary estoppel cases, the exception here requires a holding out of a particular set of facts which induced detrimental reliance by the claimant. In this setting the alleged master manifests by his conduct that a particular person is an ordinary employee performing duties within the ordinary scope of the apparent employment, when in fact the relationship is that of independent contractor. For example, the alleged master was a corporation owning a large department store. In one corner of the main retail sales building the plaintiff attempted to buy shoes from the clerk working there and was injured negligently by the clerk in fitting a shoe that had a nail protruding from the inner sole. The corporation defended the suit on the uncontradicted ground that the shoe department was operated by an independent lessee. The defense was rejected on estoppel grounds since the actual relationship between the lessee and the corporation was inconsistent with the apparent fact that the shoe department was an integral part of the master's business.⁴⁶

IV. THE AGENCY RELATIONSHIP IN CONTRACT

A. *The General Rule of Contract Liability*

The general rule of the principal's liability for contracts made by his agent is as follows:

The principal will be liable for all contracts made in his behalf by his agent if:

- (1) the agent is authorized to enter into the transaction, and
- (2) the agency relationship between the principal and the agent is fully disclosed to the other party to the contract.

If the general rule applies, the agent will not be liable on the contract unless he manifests his consent to be bound in his individual capacity in addition to binding his principal in his representative capacity.⁴⁷ To illustrate, assume that George, the president of XYZ Corporation, is authorized by the XYZ board of directors to borrow a sum of money to be used for valid corporate purposes. After disclosing the agency relation between himself and XYZ (the principal) and exhibiting a copy of the corporate minutes containing the resolution authorizing him to borrow the money, George is informed by the Bank that the loan will be made only if he will agree to co-sign the note. George agrees and the money is lent. In such a case,

46. *Santise v. Martins, Inc.*, 258 App. Div. 663, 17 N.Y.S.2d 741 (1940).

47. See, e.g., *Hasbrouck v. Krsul*, 168 Mont. 270, 541 P.2d 1197 (1975).

the general rule binds the principal due to the full disclosure and express authorization. Had George not been required to co-sign, he would not have been liable; since he did manifest the intent to be bound in his individual capacity, he will be liable jointly with XYZ. Note that the manifestation to be bound in one's individual capacity need not be express as in this example, but can be implied from the conduct of the parties using normal contract principles.

As in tort cases, the initial consideration in determining whether an alleged principal is liable on the contract depends on the existence of an agency relationship. Obviously, no liability can be imputed to the principal if the putative agent has entered into the transaction solely in his individual capacity.⁴⁸ The remaining materials in this section assume that an agency relationship can be found using the analysis discussed previously, and having found the relationship, one must be able to determine the legal consequences if one or more of the requisites of the general rule are not present. As the consequences vary with the extent of deviation from the rule, several alternative situations must be considered.

B. *Application of the General Rule of Contract Liability*

1. *Was the Agency Relationship Disclosed?*

First, assume that an agent was authorized by his principal to enter into a contract with Mr. T, but the agent did not disclose to T the fact that this was an agency transaction. If the existence of the agency is completely undisclosed to T, the transaction when entered into obviously appeared to T to simply be a contract between himself and another person (the agent). The application of ordinary contract principles would seem to hold the agent personally liable since he had objectively manifested his intent to be bound to T. On the other hand, the unknown and undisclosed agency should have some bearing on the transaction. The courts have reconciled this problem by holding the principal and the agent liable alternatively, that is, that T can sue either the principal or the agent but not both.⁴⁹ Once the agency has been disclosed to T, an election by T is required and can be implied from T's conduct.⁵⁰

Since our principal is subject to alternative liability in the undisclosed agency case, it would follow that the principal should be able to enforce the contract against the other contracting party (T)

48. See, e.g., *Farmers Elevator Co. v. Pheister*, 153 Mont. 152, 455 P.2d 325 (1969).

49. See, e.g., *Old Ben Coal Co. v. Universal Coal Co.*, 248 Mich. 486, 227 N.W. 794 (1929).

50. See, e.g., *Klinger v. Modesto Fruit Co.*, 107 Cal. App. 97, 290 P. 127 (1930); RESTATEMENT § 210.

upon disclosure. While this is the nominal rule, it is subject to an important limitation in that enforcement by the principal cannot deprive T of any rights which have attached to the T-agent contract. At a minimum, this means that any defense good against the agent will also be good against his principal including the set-off of other debts owed to T by the agent in his individual capacity.⁵¹ In fact, the courts have been rather hostile to undisclosed principals who wish to enforce these contracts since T, by definition in this context, did not know he was entering into any relation with a principal. Thus courts have readily found defenses barring the principal's suit.

The alternative liability of an undisclosed principal is subject to two exceptions. First, if the contract involves a negotiable instrument, no liability can arise from the instrument itself unless the principal's signature appears on the document.⁵² This is consistent with normal negotiable instrument policy that limits rights and liabilities to those indicated on the face of the document. Note that this does not prevent ordinary liability arising from the underlying contract itself and thus is primarily applicable to holders and transferees of the original third party.⁵³

Secondly, if the T-agent contract is a sealed instrument, the common law rule limits liability to the agent who signed the document.⁵⁴ Note that this exception may be affected by the existence of statutes abolishing the use and effectiveness of seals, such as Montana Code Annotated § 1-4-205 (1978),⁵⁵ which states that "[a]ll instruments shall be as effectual without a seal as if the same had a seal attached thereto." Despite the apparent clarity of such a statute, the question is not resolved by adoption of such language. While the statute makes it clear that a document which needed a seal to be effective at common law now need not have a seal attached, the statutory language does not indicate whether this unsealed agreement is now to be construed as an unsealed common law contract, or whether the old rules which were peculiar to sealed agreements still apply. For instance, at common law a deed had to be sealed to be effective. Adoption of a statute such as Montana's clearly indicates that an unsealed document purporting to be a deed is effective, but it is not clear whether the unsealed agreement is enforceable as a common law contract or a common law deed. If the old dead rules still apply, including the inability to sue an undis-

51. See, e.g., *Hammer v. Paine*, 56 F.2d 19 (1st Cir. 1932).

52. See UNIFORM COMMERCIAL CODE, §§ 3-401 and 3-403; (MCA §§ 30-3-401 and 30-3-404 (1978) (formerly codified at R.C.M. 1947, §§ 87A-3-401 and 87A-3-404 (Supp. 1977))).

53. See, e.g., *Lady v. Thomas*, 38 Cal. App. 2d 688, 102 P.2d 396 (1940).

54. See, e.g., *McMullen v. McMullen*, 145 So.2d 568 (Fla. App. 1962).

55. Formerly codified at R.C.M. 1947, § 13-612.

closed principal, the statute does not change our agency rule which insulated the principal from liability. While most courts have applied the rules of unsealed contracts to these situations and permitted suit against the principal,⁵⁶ other courts have applied the old sealed contract rules.⁵⁷ An intermediate position is to permit T to sue our undisclosed principal on the ground of unjust enrichment.⁵⁸

A slightly different problem is presented when T knows he is dealing with an agent, but the principal is unnamed. For example, a note is signed, "John Jones, President." The signature on its face indicates an agency, but the failure to note the name of the principal (i.e., "John Jones, President of XYZ, Inc.") creates a new difficulty if the contract is in writing and the parol evidence rule applies. If the contract is oral or if the parol evidence rule does not apply to the particular written contract, the general rule will apply since the fact of the agency was disclosed and T intended to contract with the known but unnamed principal. The agent will not be liable. However, if the parol evidence rule does apply, the courts have been unwilling to allow the agent to deny his personal liability on the ground that to do so would be to contradict the integrated written document. The result in this case is alternative liability once more.⁵⁹

The following chart may help in remembering these distinctions:

General Rule:	Unknown/Undisclosed Principal:	Known but unnamed Principal:
Agent authorized and agency fully disclosed:	Third party does not know of existence of agency when contract made:	Third party knows of agency but does not know identity of principal:
1. Principal liable; agent not liable,	1. Principal and Agent T liable alternatively (requires election),	1. Principal and agent liable alternatively (requires election),
2. Same result regardless if contract written or oral.	2. Same result regardless if contract written or oral,	2. Only applies to contracts subject to parol evidence rule (contract written and integrated),
	3. Subject to negotiable instrument and sealed instrument exceptions.	3. Subject to negotiable instrument and sealed instrument exceptions.

56. See, e.g., *J. D. Streeter, Jr. Co. v. Jann*, 90 Minn. 393, 96 N.W. 1128 (1903).

57. See, e.g., *Sanger v. Warren*, 91 Tex. 472, 44 S.W. 477 (1898).

58. See, e.g., *Donner v. White Cotton*, 201 Mo. App. 443, 212 S.W. 378 (1919).

59. See, e.g., *Moore v. Spicer*, 249 Ky. 464, 61 S.W.2d 5 (1933).

2. *Was the Agent Authorized To Enter into the Transaction?*

The general rule regarding agent's contracts not only requires disclosure of the agency relationship, but in addition requires that the agent be fully authorized by the principal to enter into the agreement. If the agent did not have authority to enter into the contract in question, the principal will not be liable. In these cases, the agent will be liable to the third party, but the theory of the agent's liability varies with the facts. If the agent did not disclose the agency in addition to failing to have the requisite authority, ordinary contract principles tell us that the agent is simply liable on the contract.

On the other hand, if the agent disclosed the agency, but did not have the requisite authority, his liability at common law can be based either on the tort theory of deceit or on the breach of an implied warranty of authority. In Montana, the rule is somewhat different in that ordinarily the unauthorized agent is liable only on breach of warranty unless: (1) the agent personally receives credit in the transaction with his consent; (2) the agent entered into a written contract without a good faith belief that he had authority; or (3) the agent's acts were "wrongful." In the three enumerated situations, the agent will be liable directly on the contract.⁶⁰ Another exception to the statement that A's liability will not be on the contract arises if the agent signs a negotiable instrument without authority. Section 3-404 of the Uniform Commercial Code⁶¹ restates the usual rule that the principal will not be liable for the unauthorized signature unless he ratifies it, but changes the common law rule as to the liability of the agent. Under the code, the unauthorized agent is liable on the note itself rather than on the breach of warranty or deceit theories.⁶²

Since the principal is not liable on the contract if the agent had no authority to enter into it, a determination of whether authority existed is crucial to analysis. While the distinctions are sometimes difficult to apply to specific facts, the theories are rather simple.

To begin with, there are only two kinds of authority: (1) actual, which can be either express or implied; or (2) apparent.⁶³ Further, as far as the principal's liability to the other contracting party is concerned, either type of authority will be sufficient.⁶⁴

60. See MCA §§ 28-10-701 and 28-10-702 (1978) (formerly codified at R.C.M. 1947, §§ 2-211 and 2-212).

61. See MCA § 30-3-404 (1978) (formerly codified at R.C.M. 1947, § 87A-3-404).

62. U.C.C. § 3-404, Comment 2.

63. See RESTATEMENT, *supra* note 16, §§ 26-27.

64. See, e.g., *Lind v. Schenley Indus. Inc.*, 278 F.2d 79, 85 (3d Cir. 1960).

Notwithstanding the simplicity of these precepts, one of the difficulties of studying agency law is the unfortunate use of several terms to represent the concept of "apparent authority." Courts, legislatures, and students have not only used the phrases "observable enterprise" and "ostensible authority" in lieu of the preferable phrase, but have on occasion blurred the distinction between "actual" and "apparent" authority completely by using the phrase "implied authority," (which is in fact merely a form of actual authority), to identify apparent authority.⁶⁵ While analysis would be improved if everyone used the Restatement's terminology, unfortunately the Montana agency statutes use the term "ostensible" rather than "apparent,"⁶⁶ although the Montana Supreme Court has implied that the two terms are synonymous.⁶⁷ With this caveat in mind, the phrase used hereinafter is "apparent authority."

The following summary will illustrate the different kinds of authority. It will be followed by more specific discussion.

Actual Authority (determined by an analysis of the relationship between the principal and the agent).

1. Express
 - a. oral
 - b. written
 - c. statutory (under the Uniform Partnership Act)

2. Implied (determined from conduct or status of the principal and the agent).

Apparent Authority (determined by an analysis of the manifestations by the principal to third parties regarding the agent's status).

As indicated above, actual authority is determined by analyzing the relationship between the principal and the agent. One must consider the given facts to determine if the principal in fact authorized the agent to enter into the transaction in question. In this regard, there are no really difficult conceptual problems involving express actual authority, either oral or in writing, as they simply turn on construction of the language used by the principal. While as a practical matter it may be difficult to prove what was said by the principal to the agent, or to determine the intent of the parties

65. *Id.*

66. See MCA § 28-10-103 (1978) (formerly codified at R.C.M. 1947, §§ 2-104 to 106).

67. See *Kraus v. Treasure Belt Mining Co.*, 146 Mont. 432, 435, 408 P.2d 151, 152 (1965). The court stated that an ostensible agent is one who has apparent authority to do the act in question if it is reasonable for a third person dealing with him to believe he is an authorized agent. Thus, the court, at least implicitly, does not distinguish apparent from ostensible authority.

from a poorly drafted instrument, the issue at least is clear. Common examples of written express authority include powers of attorney and resolutions by corporate boards of directors.

More difficulty is encountered in cases involving implied actual authority. One must look to the conduct and manifestations of the principal to the agent in order to find implied actual authority. A common example would be the situation where a store manager, A, has been permitted by the principal to execute particular kinds of contracts over an extended period of time without objection. The principal's knowledge of A's activities without objection would be a manifestation to A that he was authorized to make such contracts. This is especially true where the activity is considered usual or customary for persons in this position to perform.⁶⁸ Related to these cases are those where an individual is appointed to a particular position such as store manager or corporate officer and no limitations on the usual activities connected with the position are communicated to the agent. The appointment without limitation would be a manifestation to the agent that he has the usual authority associated with the position.⁶⁹

Another source of confusion is that the facts that support implied actual authority also can support a conclusion that apparent authority exists.⁷⁰ As far as the third party is concerned, either form of authority will bind the principal to the contract and the differences between these two forms are not important. However, the existence of implied actual compared to apparent authority is very material with reference to the liability of the agent to the principal as the agent will not have breached his duty to the principal if actual authority existed. This problem will be discussed in greater detail below.

Apparent authority is found when the principal engaged in conduct that manifests to third parties that the agent has the authority to enter into the contract in question when in fact no authority exists.⁷¹ Obviously this requires an analysis of the principal's conduct (and not the agent's). It is also a conclusion that the principal has acted in such a way that the third party could have reasonably concluded that the agent was authorized notwithstanding limitations on the agent's authority that were known by the agent but unknown by the other contracting party.⁷²

68. See, e.g., *Southwestern Portland Cement v. Beavers*, 82 N.M. 218, 221, 478 P.2d 546, 549 (1970).

69. See, e.g., *Coover v. Davis*, 112 Mont. 605, 609, 121 P.2d 985, 987 (1941).

70. See, e.g., *Correa v. Quality Motor Co.*, 118 Cal. App. 2d 246, 257 P.2d 738 (1953).

71. See RESTATEMENT, *supra* note 16, § 27.

72. See, e.g., *Baker Nat'l Bank v. Lestar*, 153 Mont. 45, 54, 453 P.2d 774, 778 (1969);

The concept is similar to estoppel in that the principal will not be able to assert against the third party that no actual authority existed. The theory is not a true estoppel, however, as no reliance by the third party in response to the manifestation is required.⁷³ In fact the theory is similar to the objective theory of contracts — that is, that by manifesting the appearance of authority to third parties, such authority exists notwithstanding the principal's subjective or secret limitation on the agent's actual authority.⁷⁴

One should remember two important facets of apparent authority: (1) the third party need not rely on the principal's manifestations, and (2) apparent authority can be manifested to third parties even though the principal has communicated expressly to the agent that no actual authority exists. For example, principal tells his agent to buy Blackacre from Mr. T for \$5,000. This is obviously an example of express actual (oral) authority for the agent to make such a contract. The principal then writes a letter to T telling him that the agent has the authority to enter into this transaction. Before the agent actually deals with T, however, the principal revokes the agent's authority but fails to communicate this fact to T. The agent then enters into an executory contract to buy Blackacre for \$5,000. T can enforce the contract against the principal on the grounds of apparent authority. The letter from the principal to T regarding the agent's authority was clearly a sufficient manifestation to create such authority, even though T may not yet have relied on the manifestation since the contract was executory; and the agent in fact had no actual authority since the revocation was communicated to him.⁷⁵ Note that in this example there is authority as far as T is concerned, apparent authority, so the general rule applies and T cannot sue the agent. Since the agent proceeded against his principal's express wishes and did not have actual authority, he will be liable to the principal for breach of the duty owed by an agent to his principal, a concept that is discussed more fully below.

3. *Ratification of Agent's Acts by the Principal*

Even though the agent was not authorized at the time the contract was executed, the principal can ratify (or subsequently affirm) the agent's conduct, and if the principal does so the consequences are the same as if the agent had been authorized to enter into the agreement. To illustrate this concept, one should recognize that in

Ludwig v. Montana Bank and Trust Co., 109 Mont. 477, 496, 98 P.2d 379, 386 (1939).

73. See RESTATEMENT, *supra* note 16, § 8B, Comment b.

74. See RESTATEMENT, *supra* note 16, § 27, Comment d.

75. See RESTATEMENT, *supra* note 16, § 329, Illustration 6.

the normal agency case the sequence of events is that first, the principal authorizes the agent to act, and secondly, the agent deals with third parties. However, in the ratification cases the sequence is reversed. The agent deals with the third party followed by conduct by the principal that ratifies or affirms the agent's actions even though no authority existed initially.

Although express ratification is possible, as where a corporate board of directors ratifies by resolution an act by an officer after the fact, the doctrine is frequently implied by courts to simply make the principal liable because justice seems to require it. The kind of conduct most likely to be classified as an implied ratification is where (1) the principal acquired knowledge of the agent's act, and (2) retained the benefit of the contract with the third party for a period without immediately disclaiming authority as soon as he became aware of the agent's actions. The courts have not been receptive to technical arguments by principals that no authority existed when the contract later soured and the principal desires to rescind. In one case,⁷⁶ for example, Mrs. P, an owner of race horses, wrote a letter to her agent informing him that her financial circumstances were such that he should sell a particular filly for \$300. The agent wrote back immediately stating that he had sold a different horse for \$2,000, paid a pressing debt for Mrs. P, and would forward the balance of the proceeds to her. During the following two months, the horse that had been sold won several races and earned substantial sums for its new owner, who paid the \$2,000 to the agent. Mrs. P then attempted to rescind the contract on the grounds that her agent had no authority to enter this transaction. As the initial letter from Mrs. P to the agent did not express actual authority to sell the horse in question and since she had not manifested any indication to the buyer that the agent was authorized, no apparent authority existed either. The Louisiana Supreme Court had no problem concluding that Mrs. P had ratified the sale by failing to complain after knowledge of the act in a case similar to these facts. Silence and retention of the benefits of the sale were equivalent to express ratification.⁷⁷

A note of caution must be added regarding the use of the ratification doctrine in Montana. It can be used to "cure" a lack of authority only; it cannot compensate for the fact that no agency relationship existed at the time the contract was entered into. While

76. *Watson v. Schmidt*, 173 La. 92, 136 So. 99 (1931).

77. *Id.* at 95, 136 So. at 100.

one might contend that such a distinction is without merit, the Montana Supreme Court has taken this position.⁷⁸

V. RIGHTS AND DUTIES BETWEEN PRINCIPAL AND AGENT

A. *The Agent's Fiduciary Duty*

An agent is a fiduciary, and as such owes a duty to his principal that exceeds that owed to the world at large. As Cardozo stated in *Meinhard v. Salmon*:⁷⁹

Many forms of conduct permissible in a workaday world for those acting at arms length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior.⁸⁰

While courts do not always hold agents to the rigid standard suggested by Cardozo, one should remember that every agency situation creates a duty that is different from that owed between strangers. Further, while the precise extent of this duty will vary with the circumstances, in general an agent owes a duty to act loyally for his principal's benefit. At a minimum, this means that the agent cannot take advantage of a situation created by the agency to benefit himself at the expense of the principal. For example, a principal employed an agent, a real estate broker, to sell a particular parcel of property. During his negotiations with a potential buyer, the agent learned that this individual would be willing to pay \$3,300 for the property. Later, the agent discovered that his principal would accept as little as \$3,000 and informed the principal that a buyer was available who would pay that price, but refused to identify the individual. The agent then purchased the property himself through a "straw man" for \$3,000 and promptly sold it to the interested buyer for \$3,300. The court found a clear breach of the agent's duty to the principal.⁸¹

In addition, an agent cannot assist one whose position is adverse to his principal. To illustrate, assume that an owner hires an agent to negotiate the rental of commercial property. Unknown to the owner, the agent has also been hired by a potential lessee to attempt to rent the same property. The agent would be in breach

78. Compare *Federal Land Bank v. Myhre*, 110 Mont. 416, 421, 101 P.2d 1017, 1020 (1940) with *United States Nat'l Bank v. Chappel*, 71 Mont. 553, 568-69, 230 P. 1084, 1088 (1924) (dictum).

79. 249 N.Y. 458, 164 N.E. 545 (1928).

80. *Id.* at 464, 164 N.E. at 546.

81. *Jansen v. Williams*, 36 Neb. 869, 55 N.W. 279 (1893); see also, *First Nat'l Bank v. Sant*, 161 Mont. 376, 384, 506 P.2d 835, 840 (1973).

of duty to the owner to accept the agency under these circumstances.⁸² Note that this is an agency problem that frequently arises in commercial real estate transactions when both sides to a transaction deal with real estate brokers. In these cases the broker must make full disclosure to all parties of his arrangements in order to avoid a conflict of interest or breach of duty claim.⁸³

Courts traditionally impose rather strict penalties upon finding a breach of duty by an agent. These include not only holding the agent liable for the principal's actual damages but also require the agent to disgorge his ill-gotten gains so that he cannot retain any profit realized as a result of his breach, even though the principal suffered no actual damages.⁸⁴

As indicated in the preceding discussion on authority, the consequence of the agent having actual authority, as opposed to apparent authority, is very significant in analyzing the principal-agent set of rights and duties. If actual authority existed, the agent has not breached his duty to his principal even though the principal was not aware such authority existed. On the other hand, if no actual authority was present, a finding that apparent authority existed will make the principal liable to third parties, but he will have an action over against the agent based on the breach of duty.⁸⁵

B. Duties Owed by Principal to Agent

In contrast to the duty of loyalty and fidelity owed by agents to their principals, an agent holds certain rights against his principal. These include: (1) a right to reasonable compensation for services rendered either by the terms of the contract creating the agency or in *quantum meruit* for the reasonable value of the services if the agency was not contractually based; (2) the right to be reimbursed for expenses made by the agent in its principal's behalf; and (3) the right to be indemnified for losses suffered while acting within the scope of the agency.⁸⁶

VI. TERMINATION OF THE RELATIONSHIP

Since the agency relationship is basically consensual, any manifestation that either the principal or the agent no longer desire to

82. See, e.g., *Weinhagen v. Hayes*, 174 Wis. 233, 178 N.W. 780 (1921).

83. See, e.g., *Seigel v. Cambridge-Wendell Realty Co.*, 323 Mass. 598, 83 N.E.2d 262 (1949).

84. See, e.g., *First Nat'l Bank v. Sant*, 161 Mont. at 384, 506 P.2d at 570; *United States v. Drisko*, 303 F. Supp. 858 (E.D. Va. 1969).

85. See RESTATEMENT, *supra* note 16, § 329, Comment f.

86. See W. SELL, AGENCY §§ 165-66, 170 (1975).

maintain the relationship will cause it to be terminated.⁸⁷ In addition to renunciation or revocation of the agency by either party, the Montana statutes also specify that the agency is terminated by (1) the death of either party; (2) the incapacity of either the agent to act as such or the principal to make a contract; (3) the extinction of the subject matter of the agency; and (4) the expiration of the agreed term.⁸⁸ Further, even if the agency is based on a contract, the usual contract rule applies in that either party has the power to cause termination even though the right to terminate does not exist.⁸⁹

In general, the facts manifesting the termination must be communicated to the other party to the agency and third parties who had knowledge of the relationship.⁹⁰ Although either the agent or the principal can terminate, the problems that cause most difficulty are those where it is the principal's act that terminates, since the agent is the one who is dealing with third parties and thus may create situations that would otherwise bind the principal, but for the termination. This is particularly true when the termination is caused by the death of the principal.

Obviously, death rescinds prior consent and the common law rule was that death terminated the agency automatically.⁹¹ Since the agent may not in fact learn of the death of the principal immediately, he may enter into transactions with third parties in good faith without knowledge that his authority has been revoked by operation of law. Notwithstanding the injustice that can result to both the agent and the third parties under these circumstances, the common law rule has been enforced on the tenuous grounds that the fact of death is so notorious that all should know of it even though the parties in fact had no reasonable chance to discover it. This result has been modified in a few states by statute, including Montana,⁹² but the common law rule is still followed in many states.

VII. CONCLUSION

A short summary of agency thought and analysis obviously omits a number of topics that can be found in the standard reference

87. See, e.g., *Morgan v. Harper*, 236 S.W. 71, 72 (Tex. App. 1922).

88. See MCA §§ 28-10-801 to 802 (1978) (formerly codified at R.C.M. 1947, §§ 2-304 to 305).

89. See *W. SELL, AGENCY*, §§ 164, 168 (1975).

90. See MCA §§ 28-10-801 to 802 (1978) (formerly codified at R.C.M. 1947, §§ 2-304 to 305).

91. See, e.g., *Weber v. Bridgman*, 113 N.Y. 600, 21 N.E. 985 (1889).

92. See MCA §§ 28-10-801 to 802 (1978) (formerly codified at R.C.M. 1947, §§ 2-304 to 305).

works. As indicated at the outset, however, the purpose here is to simplify the main principles and suggest an analytical framework to which the subtleties can be added as needed. Without such an understanding, the existing opinions are bound to continue to reflect confusion. If this article assists in the goal of reducing that confusion, it has met the author's expectations.

