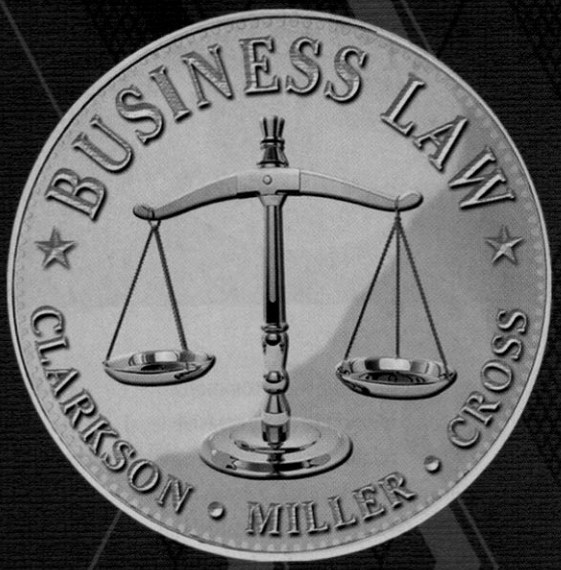
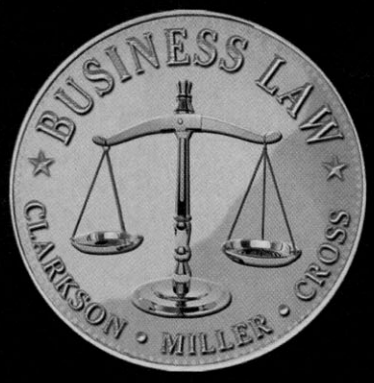
UNIT SEVEN

AGENCY AND EMPLOYMENT



CONTENTS



CHAPTER 32

Agency Formation and Duties

One of the most common, important, and pervasive legal relationships is that of agency. In an agency relationship involving two parties, one of the parties, called the *agent*, agrees to represent or act for the other, called the *principal*. The principal has the right to control the agent's conduct in matters entrusted to the agent. By using agents, a principal can conduct multiple business operations simultaneously in various locations. Thus, for example, contracts that bind the principal can be made at different places with different persons at the same time.

A familiar example of an agent is a corporate officer who serves in a representative capacity for the owners of the corporation. In this capacity, the officer has the authority to bind the principal (the corporation) to a contract. In fact, agency law is essential to the existence and operation of a corporate entity because only through its agents can a corporation function and enter into contracts.

Most employees are also considered to be agents of their employers. Thus, some of the concepts of employment law that you will learn about in Chapters 34 and 35 are based on agency law. Indeed, agency relationships permeate the business world. For that reason, an understanding of the law of agency is crucial to understanding business law.

SECTION 1
AGENCY RELATIONSHIPS

Section 1(1) of the *Restatement (Third) of Agency*[1] defines *agency* as "the fiduciary relation [that] results from the manifestation of consent by one person to another that the other shall act in his [or her] behalf and subject to his [or her] control, and consent by the other so to act." In other words, in a principal-agent relationship, the parties have agreed that the agent will act *on behalf and instead of* the principal in negotiating and transacting business with third parties.

The term **fiduciary** is at the heart of agency law. This term can be used both as a noun and as an adjective. When used as a noun, it refers to a person having a duty created by his or her undertaking to act primarily for another's benefit in matters connected with the undertaking. When used as an adjective, as in the phrase *fiduciary relationship*, it means that the relationship involves trust and confidence.

Agency relationships commonly exist between employers and employees. Agency relationships may sometimes also exist between employers and independent contractors who are hired to perform special tasks or services.

Employer-Employee Relationships

Normally, all employees who deal with third parties are deemed to be agents. A salesperson in a department store, for instance, is an agent of the store's owner (the principal) and acts on the owner's behalf. Any sale of goods made by the salesperson to a customer is binding on the principal. Similarly, most representations of fact made by the salesperson with respect to the goods sold are binding on the principal.

Because employees who deal with third parties generally are deemed to be agents of their employers, agency law and employment law overlap considerably. Agency relationships, though, as will become apparent, can exist outside an employer-employee

1. The *Restatement (Third) of Agency* is an authoritative summary of the law of agency and is often referred to by judges in their decisions and opinions.

relationship, and thus agency law has a broader reach than employment law does.

Employment laws (state and federal) apply only to the employer-employee relationship. Statutes governing Social Security, withholding taxes, workers' compensation, unemployment compensation, workplace safety, employment discrimination, and other aspects of employment (see Chapters 34 and 35) are applicable only when an employer-employee relationship exists. *These laws do not apply to an independent contractor.*

Employer–Independent Contractor Relationships

Independent contractors are not employees because, by definition, those who hire them have no control over the details of their work performance. Section 2 of the *Restatement (Third) of Agency* defines an **independent contractor** as follows:

> [An independent contractor is] a person who contracts with another to do something for him [or her] but who is not controlled by the other nor subject to the other's right to control with respect to his [or her] physical conduct in the performance of the undertaking. He [or she] may or may not be an agent.

Building contractors and subcontractors are independent contractors; a property owner who hires a contractor and subcontractors to complete a project does not control the details of the way they perform their work. Truck drivers who own their vehicles and hire out on a per-job basis are independent contractors, but truck drivers who drive company trucks on a regular basis usually are employees.

The relationship between a principal and an independent contractor may or may not involve an agency relationship. To illustrate: An owner of real estate who hires a real estate broker to negotiate the sale of her property not only has contracted with an independent contractor (the real estate broker) but also has established an agency relationship for the specific purpose of selling the property. Another example is an insurance agent, who is both an independent contractor and an agent of the insurance company for which he or she sells policies. (Note that an insurance *broker,* in contrast, normally is an agent of the person obtaining insurance and not of the insurance company.)

Determination of Employee Status

The courts are frequently asked to determine whether a particular worker is an employee or an independent contractor. How a court decides this issue can have a significant effect on the rights and liabilities of the parties. For example, employers are required to pay certain taxes, such as Social Security and unemployment taxes, for employees but not for independent contractors.

CRITERIA USED BY THE COURTS In deciding whether a worker is categorized as an employee or an independent contractor, courts often consider the following questions:

1. How much control does the employer exercise over the details of the work? (If the employer exercises considerable control over the details of the work and the day-to-day activities of the worker, this indicates employee status. This is perhaps the most important factor weighed by the courts in determining employee status.)
2. Is the worker engaged in an occupation or business distinct from that of the employer? (If so, this points to independent-contractor, not employee, status.)
3. Is the work usually done under the employer's direction or by a specialist without supervision? (If the work is usually done under the employer's direction, this indicates employee status.)
4. Does the employer supply the tools at the place of work? (If so, this indicates employee status.)
5. For how long is the person employed? (If the person is employed for a long period of time, this indicates employee status.)
6. What is the method of payment—by time period or at the completion of the job? (Payment by time period, such as once every two weeks or once a month, indicates employee status.)
7. What degree of skill is required of the worker? (If a great degree of skill is required, this may indicate that the person is an independent contractor hired for a specialized job and not an employee.)

Sometimes, workers may benefit from having employee status—for tax purposes and to be protected under certain employment laws, for example. As mentioned earlier, federal statutes governing employment discrimination apply only when an employer-employee relationship exists. Protection under employment-discrimination statutes provides a significant incentive for workers to claim that they are employees rather than independent contractors.

CASE IN POINT A Puerto Rican television station, WIPR, contracted with Victoria Lis Alberty-Vélez to co-host a television show. Alberty-Vélez signed a new contract for every new episode, each of which

required her to work a certain number of days. She was under no other commitment to work for WIPR and was free to pursue other opportunities during the weeks between filming. WIPR did not withhold any taxes from the lump-sum amount it paid her for each contract. When Alberty-Vélez became pregnant, WIPR stopped contracting with her. She filed a lawsuit claiming that WIPR was discriminating against her in violation of federal employment-discrimination laws, but the court found in favor of WIPR. Because the parties had structured their relationship through the use of repeated fixed-length contracts and had described the woman as an independent contractor on tax documents, she could not maintain an employment-discrimination suit.[2]

Whether a worker is an employee or an independent contractor can also affect the employer's liability for the worker's actions. In the following case, the court had to determine the status of a taxi driver whose passengers were injured in a collision.

2. *Alberty-Vélez v. Corporación de Puerto Rico para la Difusión Pública*, 361 F.3d 1 (1st Cir. 2004).

CASE 32.1

Lopez v. El Palmar Taxi, Inc.

Court of Appeals of Georgia, 297 Ga.App. 121, 676 S.E.2d 460 (2009).

BACKGROUND AND FACTS • El Palmar Taxi, Inc., requires its drivers to supply their own cabs, which must display El Palmar's logo. The drivers pay gas, maintenance, and insurance costs, as well as a fee to El Palmar. They are expected to follow certain rules—dress neatly, for example—and to comply with the law, including licensing regulations, but they can work when they want for as long as they want. El Palmar may dispatch a driver to pick up a fare, or the driver can look for a fare. Mario Julaju drove a taxi under a contract with El Palmar that described him as an independent contractor. El Palmar sent Julaju to pick up Maria Lopez and her children. During the ride, Julaju's cab collided with a truck. To recover for their injuries, the Lopezes filed a suit in a Georgia state court against El Palmar. The employer argued that it was not liable because Julaju was an independent contractor. The court ruled in El Palmar's favor. The plaintiffs appealed.

IN THE LANGUAGE OF THE COURT

PHIPPS, Judge.

* * * *

In the complaint, Lopez alleged that she, accompanied by her children, hired El Palmar to transport them safely to their destination. * * * In its * * * answer, El Palmar denied this allegation and stated that Lopez had hired an independent contractor for transportation, not El Palmar.

* * * *

As a general rule, an employer is not responsible for [the actions of] its employee when the employee exercises an independent business and is not subject to the immediate direction and control of the employer. *To determine whether the relationship of the parties is that of employer and servant or that of employer and independent contractor, the primary test is whether the employer retains the right to control the time, manner and method of executing the work.* [Emphasis added.]

Here, Julaju executed an agreement with * * * El Palmar Taxi that he would work for El Palmar as an independent contractor. The only restrictions the contract imposed on him were to comply with all federal, state and local laws requiring business permits, certificates and licenses and to refrain from operating under the company's name in any jurisdiction where the vehicle could not legally be operated.

The evidence does not show that El Palmar assumed control over the time, manner or method of Julaju's work. He was free to work when and for as long as he wanted, he was not required to accept fares from El Palmar, he could obtain his own fares and he could work anywhere the taxi could legally be operated. The fact that the cars he drove displayed the El Palmar logo and the fact that he received calls from El Palmar are not sufficient to create an employer-employee relationship.

* * * The car [Julaju] drove the day of the collision was not owned by El Palmar. Thus, El Palmar cannot be held liable for Julaju's [actions] under the theory that Julaju was El Palmar's employee.

CASE 32.1 CONTINUED ▶ **DECISION AND REMEDY** • *The state intermediate appellate court affirmed this part of the lower court's decision. A taxi driver who is not subject to the control of the taxi company is an independent contractor. But the appellate court reversed the judgment in El Palmar's favor on other grounds and remanded the case for trial.*

WHAT IF THE FACTS WERE DIFFERENT? • *Suppose that El Palmar had limited its driver to a set schedule in a specific area of the city and allowed him to pick up only certain passengers. Would these facts have established Julaju as an employee? Why or why not?*

MANAGERIAL IMPLICATIONS • *When an employment contract clearly designates one party as an independent contractor, the relationship between the parties is presumed to be that of employer and independent contractor. But this is only a presumption. Evidence can be introduced to show that the employer exercised sufficient control to establish the other party as an employee. The Internal Revenue Service is becoming increasingly aggressive in pursuing cases involving independent contractor versus employee status. Thus, from a tax perspective, business managers need to ensure that all independent contractors fully control their own work.*

CRITERIA USED BY THE IRS The Internal Revenue Service (IRS) has established its own criteria for determining whether a worker is an independent contractor or an employee. Although the IRS once considered twenty factors in determining a worker's status, guidelines today encourage IRS examiners to look closely at just one of those factors—the degree of control the business exercises over the worker.

The IRS tends to scrutinize closely a firm's classification of its workers, because, as mentioned, employers can avoid certain tax liabilities by hiring independent contractors instead of employees. Even when a firm has classified a worker as an independent contractor, the IRS may decide that the worker is actually an employee. In that situation, the employer will be responsible for paying any applicable Social Security, withholding, and unemployment taxes. Microsoft Corporation, for example, was once ordered to pay back payroll taxes for hundreds of temporary workers who had contractually agreed to work for Microsoft as independent contractors.[3]

EMPLOYEE STATUS AND "WORKS FOR HIRE" Under the Copyright Act of 1976, any copyrighted work created by an employee within the scope of her or his employment at the request of the employer is a "work for hire," and the employer owns the copyright to the work. In contrast, when an employer hires an independent contractor—a freelance artist, writer, or computer programmer, for example—the independent contractor normally owns the copyright. In this situation, the employer can own the copyright only if the parties agree in writing that the work is a "work for hire" and the work falls into one of nine specific categories, including audiovisual and other works.

CASE IN POINT Artisan House, Inc., hired a professional photographer, Steven H. Lindner, owner of SHL Imaging, Inc., to take pictures of its products for the creation of color slides to be used by Artisan's sales force. Lindner controlled his own work and carefully chose the lighting and angles used in the photographs. When Lindner later discovered that Artisan had published the photographs in a catalogue and brochures without his permission, he had SHL register the photographs with the copyright office and file a lawsuit for copyright infringement. Artisan claimed that its publication of the photographs was authorized because they were works for hire. The court, however, decided that SHL was an independent contractor and owned the copyright to the photographs. SHL had only given Artisan permission (a license) to provide the photographs to its sales reps, not to reproduce them in other publications. Because Artisan had used the photographs in an unauthorized manner, the court ruled that Artisan was liable for copyright infringement.[4]

SECTION 2

FORMATION OF THE AGENCY RELATIONSHIP

Agency relationships normally are *consensual*—that is, they come about by voluntary consent and agreement between the parties. Generally, the agreement

3. *Vizcaino v. U.S. District Court for the Western District of Washington*, 173 F.3d 713 (9th Cir. 1999).

4. *SHL Imaging, Inc. v. Artisan House, Inc.*, 117 F.Supp.2d 301 (S.D.N.Y. 2000).

need not be in writing,[5] and consideration is not required.

A person must have contractual capacity to be a principal.[6] Those who cannot legally enter into contracts directly should not be allowed to do so indirectly through an agent. Any person can be an agent, however, regardless of whether he or she has the capacity to contract (including minors).

An agency relationship can be created for any legal purpose. An agency relationship created for a purpose that is illegal or contrary to public policy is unenforceable. If Archer (as principal) contracts with Burke (as agent) to sell illegal narcotics, the agency relationship is unenforceable because selling illegal narcotics is a felony and is contrary to public policy. It is also illegal for physicians and other licensed professionals to employ unlicensed agents to perform professional actions.

An agency relationship can arise in four ways: by agreement of the parties, by ratification, by estoppel, and by operation of law. We look here at each of these possibilities.

Agency by Agreement

Most agency relationships are based on an express or implied agreement that the agent will act for the principal and that the principal agrees to have the agent so act. An agency agreement can take the form of an express written contract or be created by an oral agreement. For example, Henry asks Grace, a gardener, to contract with others for the care of his lawn on a regular basis. If Grace agrees, an agency relationship exists between Henry and Grace for the lawn care.

An agency agreement can also be implied by conduct. For example, a hotel expressly allows only Hans Cooper to park cars, but Hans has no employment contract there. The hotel's manager tells Hans when to work, as well as where and how to park the cars. The hotel's conduct manifests a willingness to have Hans park its customers' cars, and Hans can infer from the hotel's conduct that he has authority to act as a parking valet. Thus, there is an implied agreement that Hans is an agent of the hotel and provides valet parking services for hotel guests.

At issue in the following case was whether an agency relationship arose when a man, who was being hospitalized, asked his wife to sign the admissions papers for him.

5. There are two main exceptions to the statement that agency agreements need not be in writing. An agency agreement must be in writing (1) whenever agency authority empowers the agent to enter into a contract that the Statute of Frauds requires to be in writing (this is called the *equal dignity rule*, to be discussed in the next chapter) and (2) whenever an agent is given power of attorney.

6. Note that some states allow a minor to be a principal. When a minor is permitted to be a principal, any resulting contracts will be voidable by the minor principal but *not* by the adult third party.

CASE 32.2

Laurel Creek Health Care Center v. Bishop

Court of Appeals of Kentucky, ___ S.W.3d ___ (2010).
courts.ky.gov/courtofappeals[a]

BACKGROUND AND FACTS • Gilbert Bishop was admitted to Laurel Creek Health Care Center suffering from various physical ailments. During an examination, Bishop told Laurel Creek staff that he could not use his hands well enough to write or hold a pencil, but he was otherwise found to be mentally competent. Bishop's sister, Rachel Combs, testified that when she arrived at the facility, she offered to sign the admissions forms, but Laurel Creek employees told her that it was their policy to have the patient's spouse sign the admissions papers if the patient was unable to do so. Combs also testified that Bishop asked her to get his wife, Anna, so that she could sign his admissions papers. Combs then brought Anna to the hospital, and Anna signed the admissions paperwork, which contained a provision for mandatory arbitration. Subsequently, Bishop went into cardiopulmonary arrest and died. Following his death, Bishop's family brought an action in a Kentucky state court against Laurel Creek for negligence. Laurel Creek asked the trial court to order the parties to proceed to arbitration in accordance with the mandatory arbitration provision

a. Select "Searchable Opinions" from the "Related Content" list on the right side of the screen. On the page that opens, under "Select Search Category," choose "Court of Appeals Opinions (1996+)"; then enter "2009-CA-001055" in the "Enter Search Request" box and click on "Search." In the "Search Results" list, select the highlighted link to access the case. The Kentucky Court of Appeals maintains this Web site.

CASE 32.2 CONTINUED ➧ contained in the admissions paperwork signed by Anna. The trial court denied the request on the ground that Anna was not Bishop's agent and had no legal authority to make decisions for him. Laurel Creek appealed.

IN THE LANGUAGE OF THE COURT

LAMBERT, Judge.

* * * *

Laurel Creek first argues that this is a case of actual agency and that Anna Bishop had actual authority as Gilbert's agent to sign the admissions paperwork and is therefore bound by the arbitration agreement therein.

* * * *

We agree with Laurel Creek that Gilbert created an actual agency relationship between him and his wife. According to his sister, Rachel, Gilbert specifically asked that his wife be brought to the nursing home so that she could sign the admissions documents for him, and Anna acted upon that delegation of authority and signed the admissions papers. This is consistent with the creation of actual authority as described in the *Restatement (Third) of Agency*, [Section] 2.01, Comment c (2006). The Restatement explains the rationale for the creation of actual agency in three steps. *First, "the principal manifests assent to be affected by the agent's action."* In the instant case, Gilbert asked that Anna come to the hospital to sign the papers for him. *Second, "the agent's actions establish the agent's consent to act on the principal's behalf."* Here, Anna signed all the admissions papers per her husband's request and therefore consented to act on Gilbert's behalf. *Third, by acting within such authority, the agent affects the principal's legal relations with third parties.* Clearly here, Anna's actions affected Gilbert's relations with Laurel Creek, a third party. [Emphasis added.]

* * * *

* * * The evidence indicates that Gilbert indicated to Laurel Creek that he was physically incapable of signing the documents but was of sound mental capacity and wanted his wife to sign the documents on his behalf. When Gilbert communicated this to his sister, and the sister brought Anna in to sign the documents, Gilbert created an agency relationship upon which Laurel Creek relied.

DECISION AND REMEDY • *The Kentucky Court of Appeals reversed the trial court's judgment and remanded the case for further proceedings consistent with its opinion. An actual agency relationship between Bishop and his wife, Anna, had been formed, and the trial court had erred when it found otherwise.*

THE ECONOMIC DIMENSION • *Which party benefited from the court's ruling? Why?*

THE LEGAL ENVIRONMENT DIMENSION • *Laurel Creek argued that even if there was no actual agency relationship, an implied agency relationship existed. Is this argument valid? Why or why not?*

Agency by Ratification

On occasion, a person who is in fact not an agent (or who is an agent acting outside the scope of her or his authority) may make a contract on behalf of another (a principal). If the principal approves or affirms that contract by word or by action, an agency relationship is created by *ratification*. Ratification involves a question of intent, and intent can be expressed by either words or conduct. The basic requirements for ratification will be discussed in Chapter 33.

Agency by Estoppel

When a principal causes a third person to believe that another person is the principal's agent, and the third person acts to his or her detriment in reasonable reliance on that belief, the principal is "estopped to deny" (prevented from denying) the agency relationship. In such a situation, the principal's actions have created the *appearance* of an agency that does not in fact exist. The third person must prove that he or she *reasonably* believed that

an agency relationship existed, however.[7] Facts and circumstances must show that an ordinary, prudent person familiar with business practice and custom would have been justified in concluding that the agent had authority.

CASE IN POINT Marsha and Jerry Wiedmaier owned Wiedmaier, Inc., a corporation that operated a truck stop. Their son, Michael, did not own any interest in the corporation but had worked at the truck stop as a fuel operator. Michael decided to form his own business called Extreme Diecast, LLC. To obtain a line of credit with Motorsport Marketing, Inc., which sells racing memorabilia, Michael asked his mother to sign the credit application form. After Marsha had signed as "Secretary-Owner" of Wiedmaier, Inc., Michael added his name to the list of corporate owners and faxed the form to Motorsport. Later, when Michael stopped making payments on the merchandise he had ordered, Motorsport sued Wiedmaier, Inc., for the unpaid balance. The court ruled that Michael was an apparent agent of Wiedmaier, Inc., because the credit application had caused Motorsport to reasonably believe that Michael was acting as Wiedmaier's agent in ordering merchandise.[8]

7. These concepts also apply when a person who is in fact an agent undertakes an action that is beyond the scope of her or his authority, as will be discussed in Chapter 33.
8. *Motorsport Marketing, Inc. v. Wiedmaier, Inc.*, 195 S.W.3d 492 (Mo. App. 2006).

Note that the acts or declarations of a purported *agent* in and of themselves do not create an agency by estoppel. Rather, it is the deeds or statements of the *principal* that create an agency by estoppel. Thus, in the *Case in Point* feature just discussed, if Marsha Wiedmaier had not signed the credit application on behalf of the principal-corporation, then Motorsport would not have been justified in believing that Michael was Wiedmaier's agent.

Agency by Operation of Law

The courts may find an agency relationship in the absence of a formal agreement in other situations as well. This may occur in family relationships, such as when one spouse purchases certain basic necessaries and charges them to the other spouse's account. The courts often rule that a spouse is liable for payment for the necessaries because of either a social policy or a legal duty to supply necessaries to family members.

Agency by operation of law may also occur in emergency situations, when the agent is unable to contact the principal and the agent's failure to act outside the scope of her or his authority would cause the principal substantial loss. For example, a railroad engineer may contract on behalf of his or her employer for medical care for an injured motorist hit by the train.

Concept Summary 32.1 below reviews the various ways that agencies are formed.

CONCEPT SUMMARY 32.1
Formation of the Agency Relationship

Method of Formation	Description
By Agreement	The agency relationship is formed through express consent (oral or written) or implied by conduct.
By Ratification	The principal either by act or by agreement ratifies the conduct of a person who is not in fact an agent.
By Estoppel	The principal causes a third person to believe that another person is the principal's agent, and the third person acts to his or her detriment in reasonable reliance on that belief.
By Operation of Law	The agency relationship is based on a social or legal duty (such as the need to support family members) or formed in emergency situations when the agent is unable to contact the principal and failure to act outside the scope of the agent's authority would cause the principal substantial loss.

SECTION 3

DUTIES OF AGENTS AND PRINCIPALS

Once the principal-agent relationship has been created, both parties have duties that govern their conduct. As discussed previously, the principal-agent relationship is *fiduciary*—based on trust. In a fiduciary relationship, each party owes the other the duty to act with the utmost good faith. In this section, we examine the various duties of agents and principals.

Agent's Duties to the Principal

Generally, the agent owes the principal five duties—performance, notification, loyalty, obedience, and accounting.

PERFORMANCE An implied condition in every agency contract is the agent's agreement to use reasonable diligence and skill in performing the work. When an agent fails to perform his or her duties, liability for breach of contract may result. The degree of skill or care required of an agent is usually that expected of a reasonable person under similar circumstances. Generally, this is interpreted to mean ordinary care. If an agent has represented herself or himself as possessing special skills, however, the agent is expected to exercise the degree of skill claimed. Failure to do so constitutes a breach of the agent's duty.

Not all agency relationships are based on contract. In some situations, an agent acts gratuitously—that is, without payment. A gratuitous agent cannot be liable for breach of contract, as there is no contract; he or she is subject only to tort liability. Once a gratuitous agent has begun to act in an agency capacity, he or she has the duty to continue to perform in that capacity in an acceptable manner and is subject to the same standards of care and duty to perform as other agents.

For example, Bower's friend Alcott is a real estate broker. Alcott offers to sell Bower's farm at no charge. If Alcott never attempts to sell the farm, Bower has no legal cause of action to force her to do so. If Alcott does find a buyer, however, but negligently fails to follow through with the sales contract, causing the buyer to seek other property, then Bower can sue Alcott for negligence.

NOTIFICATION An agent is required to notify the principal of all matters that come to her or his attention concerning the subject matter of the agency. This is the *duty of notification,* or the duty to inform. Suppose that Perez, an artist, is about to negotiate a contract to sell a series of paintings to Barber's Art Gallery for $25,000. Perez's agent learns that Barber is insolvent and will be unable to pay for the paintings. The agent has a duty to inform Perez of Barber's insolvency because it is relevant to the subject matter of the agency, which is the sale of Perez's paintings. Generally, the law assumes that the principal is aware of any information acquired by the agent that is relevant to the agency—regardless of whether the agent actually passes on this information to the principal. It is a basic tenet of agency law that notice to the agent is notice to the principal.

LOYALTY Loyalty is one of the most fundamental duties in a fiduciary relationship. Basically, the agent has the duty to act *solely for the benefit of his or her principal* and not in the interest of the agent or a third party. For example, an agent cannot represent two principals in the same transaction unless both know of the dual capacity and consent to it. The duty of loyalty also means that any information or knowledge acquired through the agency relationship is confidential. It is a breach of loyalty to disclose such information either during the agency relationship or after its termination. Typical examples of confidential information are trade secrets and customer lists compiled by the principal.

In short, the agent's loyalty must be undivided. The agent's actions must be strictly for the benefit of the principal and must not result in any secret profit for the agent.

CASE IN POINT Don Cousins contracted with Leo Hodgins, a real estate agent, to negotiate the purchase of an office building. While working for Cousins, Hodgins discovered that the property owner would sell the building only as a package deal with another parcel. Hodgins then formed a company to buy the two properties and resell the building to Cousins. When Cousins discovered these actions, he filed a lawsuit alleging that Hodgins had breached his fiduciary duties. The court ruled in Cousins's favor. As a real estate agent, Hodgins had a duty to communicate all offers to his principal and not to secretly purchase the property and then resell it to his principal. Hodgins was required to act in Cousins's best interests and could only become the purchaser in this situation with Cousins's knowledge and approval.[9]

In the following case, an employer alleged that a former employee had breached his duty of loyalty by planning a competing business while still working for the employer.

9. *Cousins v. Realty Ventures, Inc.*, 844 So.2d 860 (La.App. 5 Cir. 2003).

EXTENDED CASE 32.3
Taser International, Inc. v. Ward

Court of Appeals of Arizona, Division 1, 224 Ariz. 389, 231 P.3d 921 (2010).
www.cofad1.state.az.us[a]

IN THE LANGUAGE OF THE COURT

PORTLEY, Judge.

* * * *

Taser International develops and manufactures electronic control devices, commonly called stun guns, and accessories for electronic control devices, including a personal video and audio recording device called TASER CAM. Taser sells its products to the military, law enforcement, corrections, private security, and the general public.

[Steve] Ward was employed full-time with Taser from January 1, 2004, to July 24, 2007, and served as Taser's vice president of marketing during the time relevant to this appeal. He was an at-will employee,[b] and he did not sign any employment contract, non-compete agreement, or non-disclosure agreement.

* * * *

In December 2006, Ward began exploring whether he could personally develop the concept of an eyeglass-mounted camera. He sought legal advice about whether he could permissibly develop such a camera independent of Taser, and hired patent counsel to conduct a patent search on the idea.

Between April 2007 and his resignation approximately four months later, Ward shifted his exploration to the concept of a clip-on camera device, after learning that the eyeglass-mounted concept was already patent protected. He directed patent counsel to conduct a patent search on the modified idea. He communicated with JAM-Proactive, a product development company, about the design and development of a clip-on camera device, and he received a detailed product development proposal from JAM-Proactive on June 12, 2007. Prior to his resignation, Ward planned to leave Taser to form a new business, and completed substantial work on a business plan to develop, market, and sell a clip-on camera device.

Ward resigned on July 24, 2007. * * * He formed Vievu LLC on August 23, 2007, and Vievu now markets a clip-on camera device to general consumers and law enforcement. Ten months after Ward resigned, Taser announced the AXON, a product that provides an audio-video record of an incident from the visual perspective of the person involved.

[Taser filed a suit against Ward in an Arizona state court alleging, among other things, that Ward had breached his duty of loyalty to Taser. Taser moved for summary judgment in its favor, which the court granted. Ward appealed.]

* * * *

"In Arizona, an employee/agent owes his or her employer/principal a fiduciary duty." *"It is too plain to need discussion that an agent is under the duty to act with entire good faith and loyalty for the furtherance of the interests of his principal in all matters concerning or affecting the subject of his agency, and if he fails to do so, he is responsible to his principal for any loss resulting therefrom."* [Emphasis added.]

One aspect of this broad principle is that an employee is precluded from actively competing with his or her employer during the period of employment.

Although an employee may not compete prior to termination, "[the employee] may take action [during employment], not otherwise wrongful, to prepare for competition following termination of the agency relationship." Preparation cannot take the form of "acts in direct competition with the employer's business."

The line separating mere preparation from active competition may be difficult to discern in some cases, and we must "focus on the nature of the defendant's preparations to compete." [Emphasis added.]

* * * *

It is undisputed that, prior to his resignation, Ward did not solicit or recruit any Taser employees, distributors, customers, or vendors; he did not buy, sell, or incorporate any business; he did not acquire office space or other general business services; he did not contact or enter into any agreements with suppliers or manufacturers for his proposed clip-on camera; and he did not sell any products. However, Ward did begin developing a business plan, counseled with several attorneys, explored and abandoned the concept of an eyeglass-mounted camera device, and engaged, to some extent, in the exploration and development of a clip-on camera device.

Ward argues that his pre-termination activities did not constitute active competition but were merely lawful preparation for a future business venture. Taser contends, however, that "this case is not about just investigating computer software, acquiring a line

---

a. On the page that opens, select "Opinions Div 1" from the list of topics in the left-hand column. Select "Civil" from the list of categories. Scroll down the resulting list to the case title, and click on the link to access the opinion. The Arizona Court of Appeals maintains this Web site.

b. *Employment at will* is a common law doctrine under which either party may terminate an employment relationship at any time for any reason, unless a contract specifies otherwise.

EXTENDED CASE 32.3 CONTINUED ◆

of credit, securing office space, or getting prices on telephones * * * [but] about developing a rival design during employment, knowing full well TASER has sold such a device and continues to develop a second-generation product."

Upon review, we agree with Ward that certain of his pre-termination activities are qualitatively different than "direct competition" and cannot form the basis for liability.

* * * *

However, assuming Taser was engaged in the research and development of a recording device during Ward's employment, assuming Ward knew or should have known of those efforts, and assuming Taser's device would compete with Ward's concept, substantial design and development efforts by Ward during his employment would constitute direct competition with the business activities of Taser and would violate his duty of loyalty. In the context of a business which engages in research, design, development, manufacture, and marketing of products, we cannot limit "competition" to just actual sales of competing products.

Summary judgment on this theory is nevertheless improper because a genuine issue of material fact exists as to the extent of Ward's pre-termination design and development efforts.

* * * *

For the foregoing reasons, we reverse the grant of summary judgment entered in favor of Taser * * * and remand for further proceedings.

QUESTIONS

1. Why was it unclear whether Ward's pretermination actions constituted direct competition with his employer or were mere planning activities?
2. Suppose that Ward's planning and development efforts were focused on a product that in no way would compete with Taser's products. Would such efforts have breached his duty of loyalty to Taser in any way? Explain fully.

OBEDIENCE When acting on behalf of the principal, an agent has a duty to follow all lawful and clearly stated instructions of the principal. Any deviation from such instructions is a violation of this duty. During emergency situations, however, when the principal cannot be consulted, the agent may deviate from the instructions without violating this duty. Whenever instructions are not clearly stated, the agent can fulfill the duty of obedience by acting in good faith and in a manner reasonable under the circumstances.

ACCOUNTING Unless an agent and a principal agree otherwise, the agent has a duty to keep and make available to the principal an account of all property and funds received and paid out on behalf of the principal. This includes gifts from third parties in connection with the agency. For example, a gift from a customer to a salesperson for prompt deliveries made by the salesperson's firm, in the absence of a company policy to the contrary, belongs to the firm. The agent has a duty to maintain separate accounts for the principal's funds and the agent's personal funds, and the agent must not intermingle the funds in these accounts. Whenever a licensed professional (such as an attorney) violates this duty to account, he or she may be subject to disciplinary proceedings carried out by the appropriate regulatory institution (such as the state bar association) in addition to being liable to the principal (the professional's client) for failure to account.

Principal's Duties to the Agent

The principal also has certain duties to the agent. These duties relate to compensation, reimbursement and indemnification, cooperation, and safe working conditions.

COMPENSATION In general, when a principal requests certain services from an agent, the agent reasonably expects payment. The principal therefore has a duty to pay the agent for services rendered. For example, when an accountant or an attorney is asked to act as an agent, an agreement to compensate the agent for this service is implied. The principal also has a duty to pay that compensation in a timely manner. Unless the agency relationship is gratuitous and the agent does not act in exchange for payment, the principal must pay the agreed-on value for the agent's services. If no amount has been expressly agreed on, then the principal owes the agent the customary compensation for such services.

REIMBURSEMENT AND INDEMNIFICATION Whenever an agent disburses funds to fulfill the request

of the principal or to pay for necessary expenses in the course of reasonable performance of her or his agency duties, the principal has the duty to reimburse the agent for these payments.[10] Agents cannot recover for expenses incurred by their own misconduct or negligence, though.

Subject to the terms of the agency agreement, the principal has the duty to *indemnify* (compensate) an agent for liabilities incurred because of authorized and lawful acts and transactions. For example, if the agent, on the principal's behalf, forms a contract with a third party, and the principal fails to perform the contract, the third party may sue the agent for damages. In this situation, the principal is obligated to compensate the agent for any costs incurred by the agent as a result of the principal's failure to perform the contract.

Additionally, the principal must indemnify the agent for the value of benefits that the agent confers on the principal. The amount of indemnification usually is specified in the agency contract. If it is not, the courts will look to the nature of the business and the type of loss to determine the amount. Note that this rule applies to acts by gratuitous agents as well.

COOPERATION A principal has a duty to cooperate with the agent and to assist the agent in performing his or her duties. The principal must do nothing to prevent that performance. For example, when a principal grants an agent an exclusive territory, it creates an *exclusive agency,* in which the principal cannot compete with the agent or appoint or allow another agent to compete. If the principal does so, it violates the exclusive agency, and the principal is exposed to liability for the agent's lost profits. Suppose that Akers (the principal) creates an exclusive agency by granting Johnson (the agent) a territory within which only Johnson may sell Akers's products. If Akers begins to sell the products himself within Johnson's territory or permits another agent to do so, Akers has violated the exclusive agency and can be held liable for Johnson's lost profits.

SAFE WORKING CONDITIONS The common law requires the principal to provide safe working premises, equipment, and conditions for all agents and employees. The principal has a duty to inspect working areas and to warn agents and employees about any unsafe situations. When the agent is an employee, the employer's liability is frequently covered by state workers' compensation insurance, and federal and state statutes often require the employer to meet certain safety standards (see Chapter 34).

10. This principle applies to acts by gratuitous agents as well. If a finder of a dog that becomes sick takes the dog to a veterinarian and pays the required fees for the veterinarian's services, the gratuitous agent is entitled to be reimbursed for those fees by the owner of the dog.

SECTION 4
RIGHTS AND REMEDIES OF AGENTS AND PRINCIPALS

In general, for every duty of the principal, the agent has a corresponding right, and vice versa. When one party to the agency relationship violates his or her duty to the other party, the remedies available to the nonbreaching party arise out of contract and tort law. These remedies include monetary damages, termination of the agency relationship, an injunction, and required accountings.

Agent's Rights and Remedies against the Principal

The agent has the right to be compensated, to be reimbursed and indemnified, and to have a safe working environment. An agent also has the right to perform agency duties without interference by the principal.

TORT AND CONTRACT REMEDIES Remedies of the agent for breach of duty by the principal follow normal contract and tort remedies. For example, Aaron Hart, a builder who has just constructed a new house, contracts with a real estate agent, Fran Boller, to sell the house. The contract calls for the agent to have an exclusive ninety-day listing and to receive 6 percent of the selling price when the home is sold. Boller holds several open houses and shows the home to a number of potential buyers. One month before the ninety-day listing terminates, Hart agrees to sell the house to another buyer—not one to whom Boller has shown the house—after the ninety-day listing expires. Hart and the buyer agree that Hart will reduce the price of the house by 3 percent because he will sell it directly and thus will not have to pay Boller's commission. In this situation, if Boller learns of Hart's actions, she can terminate the agency relationship and sue Hart for damages, including the 6 percent commission she should have earned on the sale of the house.

Liability for Agent's Intentional Torts

Most intentional torts that employees commit have no relation to their employment; thus, their employers will not be held liable. Nevertheless, under the doctrine of *respondeat superior,* the employer can be liable for intentional torts of the employee that are committed within the course and scope of employment, just as the employer is liable for negligence. For example, an employer is liable when an employee (such as a "bouncer" at a nightclub or a security guard at a department store) commits the tort of assault and battery or false imprisonment while acting within the scope of employment.

In addition, an employer who knows or should know that an employee has a propensity for committing tortious acts is liable for the employee's acts even if they would not ordinarily be considered within the scope of employment. For example, if an employer hires a bouncer knowing that he has a history of arrests for criminal assault and battery, the employer may be liable if the employee viciously attacks a patron in the parking lot after hours.

An employer is also liable for permitting an employee to engage in reckless actions that can injure others. For example, an employer observes an employee smoking while filling containerized trucks with highly flammable liquids. Failure to stop the employee will cause the employer to be liable for any injuries that result if a truck explodes. Needless to say, most employers purchase liability insurance to cover their potential liability for employee conduct in many situations (see Chapter 51).

Liability for Independent Contractor's Torts

Generally, an employer is not liable for physical harm caused to a third person by the negligent act of an independent contractor in the performance of the contract. This is because the employer does not have *the right to control* the details of an independent contractor's performance. Courts make an exception to this rule when the contract involves unusually hazardous activities, such as blasting operations, the transportation of highly volatile chemicals, or the use of poisonous gases. In these situations, an employer cannot be shielded from liability merely by using an independent contractor. Strict liability is imposed on the employer-principal as a matter of law. Also, in some states, strict liability may be imposed by statute.

Liability for Agent's Crimes

An agent is liable for his or her own crimes. A principal or employer is not liable for an agent's or employee's crime simply because the agent or employee committed the crime while otherwise acting within the scope of authority or employment. An exception to this rule is made when the principal or employer participated in the crime by conspiracy or other action. In some jurisdictions, under specific statutes, a principal may be liable if an agent, in the course and scope of employment, violates regulations such as those governing sanitation, prices, weights, and the sale of liquor.

SECTION 4

TERMINATION OF AN AGENCY

Agency law is similar to contract law in that both an agency and a contract may be terminated by an act of the parties or by operation of law. Once the relationship between the principal and the agent has ended, the agent no longer has the right (*actual* authority) to bind the principal. For an agent's *apparent* authority to be terminated, though, third persons may also need to be notified that the agency has been terminated.

Termination by Act of the Parties

An agency relationship may be terminated by act of the parties in any of the following ways:

1. *Lapse of time.* When an agency agreement specifies the time period during which the agency relationship will exist, the agency ends when that time period expires. For example, Akers signs an agreement of agency with Janz "beginning January 1, 2012, and ending December 31, 2014." The agency is automatically terminated on December 31, 2014. If no definite time is stated, then the agency continues for a reasonable time and can be terminated at will by either party. What constitutes a reasonable time depends on the circumstances and the nature of the agency relationship.
2. *Purpose achieved.* If an agent is employed to accomplish a particular objective, such as the purchase of breeding stock for a cattle rancher, the agency automatically ends after the cattle have been purchased. If more than one agent is employed to accomplish the same purpose, such as the sale of real estate, the first agent to complete the sale

automatically terminates the agency relationship for all the others.

3. *Occurrence of a specific event.* When an agency relationship is to terminate on the happening of a certain event, the agency automatically ends when the event occurs. For example, if Posner appoints Rubik to handle her business affairs while she is away, the agency automatically terminates when Posner returns.
4. *Mutual agreement.* The parties to an agency can cancel (rescind) their contract by mutually agreeing to terminate the agency relationship, whether the agency contract is in writing or whether it is for a specific duration.
5. *Termination by one party.* As a *general* rule, either party can terminate the agency relationship—because agency is a consensual relationship, and thus neither party can be compelled to continue in the relationship. The agent's act is said to be a *renunciation* of authority. The principal's act is a *revocation* of authority. Although both parties may have the *power* to terminate the agency, they may not possess the *right* to terminate and therefore may be liable for breach of contract, or *wrongful termination.*

WRONGFUL TERMINATION Wrongful termination can subject the canceling party to a lawsuit for breach of contract. For example, Rawlins has a one-year employment contract with Munro to act as agent in return for $65,000. Although Munro has the *power* to discharge Rawlins before the contract period expires, if he does so, he can be sued for breaching the contract because he had no *right* to terminate the agency.

Even in an agency at will—that is, an agency that either party may terminate at any time—the principal who wishes to terminate must give the agent *reasonable* notice. The notice must be at least sufficient to allow the agent to recoup his or her expenses and, in some situations, to make a normal profit.

AGENCY COUPLED WITH AN INTEREST A special rule applies in an *agency coupled with an interest.* This type of agency is not an agency in the usual sense because it is created for the agent's benefit instead of for the principal's benefit. For example, Julie borrows $5,000 from Rob, giving Rob some of her jewelry and signing a letter authorizing him to sell the jewelry as her agent if she fails to repay the loan. After Julie receives the $5,000 from Rob, she attempts to revoke his authority to sell the jewelry as her agent. Julie will not succeed in this attempt because a principal cannot revoke an agency created for the agent's benefit.

An agency coupled with an interest should not be confused with a situation in which the agent merely derives proceeds or profits from the sale of the subject matter. For example, an agent who merely receives a commission from the sale of real property does not have a beneficial interest in the property itself.

NOTICE OF TERMINATION When an agency has been terminated by act of the parties, it is the principal's duty to inform any third parties who know of the existence of the agency that it has been terminated (notice of the termination may be given by others, however).

Although an agent's actual authority ends when the agency is terminated, an agent's *apparent authority* continues until the third party receives notice (from any source) that such authority has been terminated. If the principal knows that a third party has dealt with the agent, the principal is expected to notify that person *directly*. For third parties who have heard about the agency but have not yet dealt with the agent, *constructive notice* is sufficient.[14]

No particular form is required for notice of termination of the principal-agent relationship to be effective. The principal can personally notify the agent, or the agent can learn of the termination through some other means. For example, Manning bids on a shipment of steel, and Stone is hired as an agent to arrange transportation for the shipment. When Stone learns that Manning has lost the bid, Stone's authority to make the transportation arrangement terminates. If the agent's authority is written, however, normally it must be revoked in writing (unless the written document contained an expiration date).

Termination by Operation of Law

Certain events terminate agency authority automatically because their occurrence makes it impossible for the agent to perform or improbable that the principal would continue to want performance. We look at these events here. Note that when an agency terminates by operation of law, there is no duty to notify third persons—unless the agent's authority is coupled with an interest.

1. *Death or insanity.* The general rule is that the death or insanity of either the principal or the agent automatically and immediately terminates an ordinary agency relationship.[15] Knowledge of

---

14. With *constructive notice* of a fact, knowledge of the fact is imputed by law to a person if he or she could have discovered the fact by proper diligence. Constructive notice is often accomplished by publication in a newspaper.
15. An exception to this rule exists in the bank-customer relationship. A bank, as agent, can continue to exercise specific types of authority even after the customer's death or insanity, and can continue to pay checks drawn by the customer for ten days after death (see page 523 in Chapter 27).

the death or insanity is not required. For example, Grey sends Bosley to Japan to purchase a rare book. Before Bosley makes the purchase, Grey dies. Bosley's agent status is terminated at the moment of Grey's death, even though Bosley does not know that Grey has died. (Some states, however, have enacted statutes that change the common law rule to require an agent's knowledge of the principal's death before termination.)

An agent's transactions that occur after the death of the principal normally are not binding on the principal's estate. Assume that McCoy had an individual checking account and that he later authorized his live-in girlfriend, Kaye, to write checks on that account. The girlfriend is merely McCoy's agent and is not a joint account holder. If McCoy dies, Kaye's authority to write checks on the account is terminated. Thus, if Kaye writes checks on this account after McCoy's death, McCoy's estate is not bound by her acts. If the bank was aware of McCoy's death and paid the checks, it will be liable to the estate for the amount of the checks.[16]

2. *Impossibility.* When the specific subject matter of an agency is destroyed or lost, the agency terminates. For example, Gonzalez employs Arnez to sell Gonzalez's house. Prior to any sale, the house is destroyed by fire. Arnez's agency and authority to sell the house terminate. Similarly, when it is impossible for the agent to perform the agency lawfully because of a change in the law, the agency terminates.
3. *Changed circumstances.* When an event occurs that has such an unusual effect on the subject matter of the agency that the agent can reasonably infer that the principal will not want the agency to continue, the agency terminates. Suppose that Baird hires Joslen to sell a tract of land for $40,000. Subsequently, Joslen learns that there is oil under the land and that the land is therefore worth $1 million. The agency and Joslen's authority to sell the land for $40,000 are terminated.
4. *Bankruptcy.* If either the principal or the agent petitions for bankruptcy, the agency is *usually* terminated. In certain circumstances, such as when the agent's financial status is irrelevant to the purpose of the agency, the agency relationship may continue. *Insolvency* (the inability to pay debts when they come due or when liabilities exceed assets), as distinguished from bankruptcy, does not necessarily terminate the relationship.
5. *War.* When the principal's country and the agent's country are at war with each other, the agency is terminated. In this situation, the agency is automatically suspended or terminated because there is no way to enforce the legal rights and obligations of the parties.

See *Concept Summary 33.2* below and on the following page for a synopsis of the rules governing the termination of an agency.

16. See, for example, *Sturgill v. Virginia Citizens Bank*, 223 Va. 394, 291 S.E.2d 207 (1982).

CONCEPT SUMMARY 33.2
Termination of an Agency

Method of Termination	Rules	Termination of Agent's Authority
Act of the Parties		
1. Lapse of time.	Automatic at end of the stated time.	
2. Purpose achieved.	Automatic on the completion of the purpose.	**Notice to Third Parties Required–**
3. Occurrence of a specific event.	Normally automatic on the happening of the event.	1. Direct to those who have dealt with agency.
4. Mutual agreement.	Mutual consent required.	2. Constructive to all others.
5. At the option of one party (revocation, if by principal; renunciation, if by agent).	Either party normally has a right to terminate the agency but may lack the power to do so; wrongful termination can lead to liability for breach of contract.	

CONCEPT SUMMARY CONTINUES

CONCEPT SUMMARY 33.2
Termination of an Agency, Continued

Method of Termination	Rules	Termination of Agent's Authority
Operation of Law		
1. Death or insanity.	Automatic on the death or insanity of either the principal or the agent (except when the agency is coupled with an interest).	
2. Impossibility—destruction of the specific subject matter.	Applies any time the agency cannot be performed because of an event beyond the parties' control.	
3. Changed circumstances.	Events so unusual that it would be inequitable to allow the agency to continue to exist.	**No Notice Required–** Automatic on the happening of the event.
4. Bankruptcy.	Bankruptcy petition (not mere insolvency) usually terminates the agency.	
5. War between principal's country and agent's country.	Automatically suspends or terminates agency—no way to enforce legal rights.	

REVIEWING
Agency Liability and Termination

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

1. Under what doctrine discussed in this chapter might Buy-Mart be held liable for the tort committed by Watts?
2. What is the key factor in determining whether Buy-Mart is liable under this doctrine?
3. How is Buy-Mart's potential liability affected by whether Watts's behavior constituted an intentional tort or a tort of negligence?
4. Suppose that when Watts applied for the job at Buy-Mart, she disclosed in her application that she had previously been convicted of felony assault and battery. Nevertheless, Buy-Mart hired Watts as a cashier. How might this fact affect Buy-Mart's liability for Watts's actions?

DEBATE THIS: *The doctrine of* respondeat superior *should be modified to make agents solely liable for some of their tortious acts.*

EXTENDED CASE 33.3 CONTINUED

the building. After being informed of the situation, Hoggatt stopped spraying. Emergency services arrived as the building was being evacuated. Employees in the building complained of respiratory problems and itching and burning eyes.

Prior to and during the evacuation, [an Aegis employee, Catherine] Warner began having difficulty breathing, was coughing violently, and felt burning in her eyes, nose, and throat. As she exited the building, Warner began to feel faint and felt "extreme chest pain" and heart palpitations. Warner had had [two heart attacks in the past], and had undergone heart surgery in May 2003. * * * She was then transported by ambulance to the hospital, where she was treated and released after about four hours. * * * [It was later determined that Warner had suffered a heart attack on the day of the evacuation. She continued to experience health complications that she blamed on exposure to the spray.]

Warner sued SDI for negligence in September 2004, later amending her complaint to include * * * Hoggatt [and several others as defendants].

* * * *

The jury found SDI to be completely responsible for the injuries Warner suffered by inhaling the herbicide. * * * It awarded Warner $3,825 in compensatory damages and costs against SDI. [Warner appealed.]

On the last day of trial, the court entered a directed verdict in favor of Hoggatt because "the evidence [wa]s undisputed that Mr. Hoggatt [had] acted within the scope of his employment for [SDI]," and, thus, that SDI was "clearly liable in situation for whatever damages the jury does find in this matter." There was no dispute at trial that Hoggatt had been negligent * * *.

We agree with Warner that "there was no legal basis for the court's decision to dismiss Hoggatt from the action." *It is well-established law that an agent will not be excused from responsibility for tortious conduct merely because he is acting for his principal.* [Also, as stated in the *Restatement (Third) of Agency*], "An agent is subject to liability to a third party harmed by the agent's tortious conduct. Unless an applicable statute provides otherwise, an actor remains subject to liability although the actor acts * * * within the scope of employment." [Emphasis added.]

Hoggatt cites no authority suggesting this rule should not apply in this case. He does, however, argue the error was harmless. * * * Hoggatt asserts Warner was not prejudiced [injured] because "the jury apportioned one hundred percent of the fault to SDI. Adding other possible parties to the jury verdict form would not have changed the outcome of this case." We agree that including Hoggatt as a defendant throughout the trial could not have changed Warner's damage award, and Warner does not argue otherwise. Nor is there a need for the jury to apportion fault between Hoggatt and SDI—the liability of those parties is joint and several.

That the error does not warrant a new trial, however, does not mean it was not prejudicial to Warner. She has a right to recover her damages from Hoggatt, and his improper dismissal has deprived her of that right. Accordingly, we reverse the trial court's grant of a directed verdict in Hoggatt's favor and amend the judgment in Warner's favor to show it is against Hoggatt as well.

QUESTIONS

1. Why should Hoggatt be personally liable if he merely followed the instructions of his employer, SDI, given that the employer is better able financially to pay the judgment and may have insurance that covers the matter?
2. How could SDI reduce the likelihood of similar lawsuits occurring in the future?

RATIONALE UNDERLYING THE DOCTRINE OF *RESPONDEAT SUPERIOR* At early common law, a servant (employee) was viewed as the master's (employer's) property. The master was deemed to have absolute control over the servant's acts and was held strictly liable for them, no matter how carefully the master supervised the servant. The rationale for the doctrine of *respondeat superior* is based on the social duty that requires every person to manage his or her affairs, whether accomplished by the person or through agents, so as not to injure another. Liability is imposed on employers because they are deemed to be in a better financial position to bear the loss. The superior financial position carries with it the duty to be responsible for damages.

Generally, public policy requires that an injured person be afforded effective relief, and a business enterprise is usually better able to provide that relief than is an individual employee. Employers normally carry liability insurance to cover any damages awarded as a result of such lawsuits. They are also able to spread the cost of risk over the entire business enterprise.

The doctrine of *respondeat superior,* which the courts have applied for nearly two centuries, continues to have practical implications in all situations involving principal-agent (employer-employee) relationships. Today, the small-town grocer with one clerk and the multinational corporation with thousands of employees are equally subject to the

doctrinal demand of "let the master respond." (Keep this principle in mind when you read through Chapters 34 and 35.)

THE SCOPE OF EMPLOYMENT The key to determining whether a principal may be liable for the torts of an agent under the doctrine of *respondeat superior* is whether the torts are committed within the scope of the agency or employment. Courts may consider the following factors in determining whether a particular act occurred within the course and scope of employment:

1. Whether the employee's act was authorized by the employer.
2. The time, place, and purpose of the act.
3. Whether the act was one commonly performed by employees on behalf of their employers.
4. The extent to which the employer's interest was advanced by the act.
5. The extent to which the private interests of the employee were involved.
6. Whether the employer furnished the means or instrumentality (for example, a truck or a machine) by which an injury was inflicted.
7. Whether the employer had reason to know that the employee would perform the act in question and whether the employee had done it before.
8. Whether the act involved the commission of a serious crime.

THE DISTINCTION BETWEEN A "DETOUR" AND A "FROLIC" A useful insight into the concept of "scope of employment" may be gained from Judge Baron Parke's classic distinction between a "detour" and a "frolic" in the case of *Joel v. Morison* (1834).[13] In this case, the English court held that if a servant merely took a detour from his master's business, the master will be responsible. If, however, the servant was on a "frolic of his own" and not in any way "on his master's business," the master will not be liable.

Consider an example. Mandel, a traveling salesperson, while driving his employer's vehicle to call on a customer, decides to stop at the post office—which is one block off his route—to mail a personal letter. As Mandel approaches the post office, he negligently runs into a parked vehicle owned by Chan. In this situation, because Mandel's detour from the employer's business is not substantial, he is still acting within the scope of employment, and the employer is liable. The result would be different, though, if Mandel had decided to pick up a few friends for cocktails in another city and in the process had negligently run his vehicle into Chan's. In that circumstance, the departure from the employer's business would be substantial, and the employer normally would not be liable to Chan for damages. Mandel would be considered to have been on a "frolic" of his own.

EMPLOYEE TRAVEL TIME An employee going to and from work or to and from meals usually is considered to be outside the scope of employment. In contrast, all travel time of traveling salespersons or others whose jobs require them to travel normally is considered to be within the scope of employment for the duration of the business trip, including the return trip home, unless there is a significant departure from the employer's business.

NOTICE OF DANGEROUS CONDITIONS The employer is charged with knowledge of any dangerous conditions discovered by an employee and pertinent to the employment situation. Suppose that Brad, a maintenance employee in an apartment building, notices a lead pipe protruding from the ground in the building's courtyard. Brad neglects either to fix the pipe or to inform his employer of the danger. John trips on the pipe and is injured. The employer is charged with knowledge of the dangerous condition regardless of whether Brad actually informed the employer. That knowledge is imputed to the employer by virtue of the employment relationship.

BORROWED SERVANTS Employers sometimes lend the services of their employees to other employers. Suppose that an employer leases ground-moving equipment to another employer and sends along an employee to operate the machinery. Who is liable for injuries caused by the employee's negligent actions on the job site?

Liability turns on *which employer had the primary right to control* the employee at the time the injuries occurred. Generally, the employer who rents out the equipment is presumed to retain control over her or his employee. If the rental is for a relatively long period of time, however, control may be deemed to pass to the employer who is renting the equipment and presumably controlling and directing the employee.

13. 6 Car. & P. 501, 172 Eng.Rep. 1338 (1834).

fully and effectively as I could do as part of my normal, everyday business affairs if acting personally." A few days later, at Davis's direction, Ansell prepared, and Davis signed, a will that gave Brandt the right to occupy, rent-free, the house in which she and Davis lived "so long as she lives in the premises." The will's other chief beneficiaries were Davis's daughters, Sharon Jones and Jody Clark. According to Ansell, Davis intended to "take care of [Brandt] outside of this will" and asked Ansell to designate Brandt the beneficiary "payable on death" (POD) of Davis's $250,000 certificate of deposit (CD). The CD had no other named beneficiary. Less than two months later, Davis died. A suit between Brandt and Davis's daughters ensued in a Virginia state court. [Jones v. Brandt, *274 Va. 131, 645 S.E.2d 312 (2007)*]

(a) Should the language in a power of attorney be interpreted broadly or strictly? Why?

(b) In this case, did Ansell have the authority under the power of attorney to change the beneficiary of Davis's CD? Explain.

(c) Ansell advised Davis by letter that he had complied with the instruction to designate Brandt the beneficiary of the CD. Davis made no objection. Based on these facts, what theory might apply to validate the designation?

LEGAL RESEARCH EXERCISES ON THE WEB

Go to this text's Web site at **www.cengage.com/blaw/clarkson**, select "Chapter 33," and click on "Practical Internet Exercises." There you will find the following Internet research exercises that you can perform to learn more about the topics covered in this chapter.

Practical Internet Exercise 33–1: **Legal Perspective**
Power of Attorney

Practical Internet Exercise 33–2: **Management Perspective**
Liability in Agency Relationships

CHAPTER 34

Employment, Immigration, and Labor Law

Until the early 1900s, most employer-employee relationships were governed by the common law. Even today, under the common law *employment-at-will doctrine*, private employers are generally free to hire and fire workers at will, unless doing so violates an employee's contractual or statutory rights. Now, however, there are numerous statutes and administrative agency regulations that regulate the workplace. Thus, to a large extent, statutory law has displaced common law doctrines.

In this chapter, we look at the most significant laws regulating employment relationships. We deal with other important laws regulating the workplace—those that prohibit employment discrimination—in the next chapter.

SECTION 1
EMPLOYMENT AT WILL

Traditionally, employment relationships have generally been governed by the common law doctrine of **employment at will.** Under this doctrine, either party may terminate the employment relationship at any time and for any reason, unless doing so would violate the provisions of an employment contract or a statute. The majority of U.S. workers continue to have the legal status of "employees at will." In other words, this common law doctrine is still in widespread use, and only one state (Montana) does not apply the doctrine.

Nonetheless, as mentioned in the chapter introduction, federal and state statutes governing employment relationships prevent the doctrine from being applied in a number of circumstances. Today, an employer is not permitted to fire an employee if doing so would violate a federal or state employment statute, such as one prohibiting employment termination for discriminatory reasons (see Chapter 35). Note that the distinction made under agency law (discussed in Chapter 32) between employee status and independent-contractor status is important here. The employment laws that will be discussed in this chapter and in Chapter 35 apply only to the employer-employee relationship. They do not apply to independent contractors.

Exceptions to the Employment-at-Will Doctrine

Under the employment-at-will doctrine, as mentioned, an employer may hire and fire employees at will (regardless of the employees' performance) without liability, unless the decision violates the terms of an employment contract or statutory law. Because of the harsh effects of the employment-at-will doctrine for employees, courts have carved out various exceptions to this doctrine. These exceptions are based on contract theory, tort theory, and public policy.

EXCEPTIONS BASED ON CONTRACT THEORY Some courts have held that an *implied* employment contract exists between the employer and the employee. If the employee is fired outside the terms of the implied contract, he or she may succeed in an action for breach of contract even though no written employment contract exists.

For example, an employer's manual or personnel bulletin may state that, as a matter of policy, workers will be dismissed only for good cause. If the employee is aware of this policy and continues to

TERMS AND CONCEPTS

apparent authority 641
disclosed principal 645
e-agent 647
equal dignity rule 639
express authority 639
implied authority 641
notary public 640
partially disclosed principal 645
power of attorney 640
ratification 644
***respondeat superior* 648**
undisclosed principal 645
vicarious liability 648

QUESTIONS AND CASE PROBLEMS

33–1. Agent's Authority Adam is a traveling salesperson for Peter Petri Plumbing Supply Corp. Adam has express authority to solicit orders from customers and to offer a 5 percent discount if payment is made within thirty days of delivery. Petri has said nothing to Adam about extending credit. Adam calls on a new prospective customer, John's Plumbing Firm. John tells Adam that he will place a large order for Petri products if Adam will give him a 10 percent discount with payment due in equal installments thirty, sixty, and ninety days from delivery. Adam says he has authority to make such a contract. John calls Petri and asks if Adam is authorized to make contracts giving a discount. No mention is made of payment terms. Petri replies that Adam has authority to give discounts on purchase orders. On the basis of this information, John orders $10,000 worth of plumbing supplies and fixtures. The goods are delivered and are being sold. One week later, John receives a bill for $9,500, due in thirty days. John insists he owes only $9,000 and can pay it in three equal installments, at thirty, sixty, and ninety days from delivery. Discuss the liability of Petri and John only.

33–2. QUESTION WITH SAMPLE ANSWER: Unauthorized Acts.

Janell Arden is a purchasing agent–employee for the A&B Coal Supply partnership. Arden has authority to purchase the coal needed by A&B to satisfy the needs of its customers. While Arden is leaving a coal mine from which she has just purchased a large quantity of coal, her car breaks down. She walks into a small roadside grocery store for help. While there, she encounters Will Wilson, who owns 360 acres back in the mountains with all mineral rights. Wilson, in need of cash, offers to sell Arden the property for $1,500 per acre. On inspection of the property, Arden forms the opinion that the subsurface contains valuable coal deposits. Arden contracts to purchase the property for A&B Coal Supply, signing the contract "A&B Coal Supply, Janell Arden, agent." The closing date is August 1. Arden takes the contract to the partnership. The managing partner is furious, as A&B is not in the property business. Later, just before closing, both Wilson and the partnership learn that the value of the land is at least $15,000 per acre. Discuss the rights of A&B and Wilson concerning the land contract.

- **For a sample answer to Question 33–2, go to Appendix I at the end of this text.**

33–3. Ratification by Principal Springer was a political candidate running for Congress. He was operating on a tight budget and instructed his campaign staff not to purchase any campaign materials without his explicit authorization. In spite of these instructions, one of his campaign workers ordered Dubychek Printing Co. to print some promotional materials for Springer's campaign. When the printed materials arrived, Springer did not return them but instead used them during his campaign. When Springer failed to pay for the materials, Dubychek sued for recovery of the price. Springer contended that he was not liable on the sales contract because he had not authorized his agent to purchase the printing services. Dubychek argued that the campaign worker was Springer's agent and that the worker had authority to make the printing contract. Additionally, Dubychek claimed that even if the purchase was unauthorized, Springer's use of the materials constituted ratification of his agent's unauthorized purchase. Is Dubychek correct? Explain.

33–4. *Respondeat Superior* ABC Tire Corp. hires Arnez as a traveling salesperson and assigns him a geographic area and time schedule in which to solicit orders and service customers. Arnez is given a company car to use in covering the territory. One day, Arnez decides to take his personal car to cover part of his territory. It is 11:00 A.M., and Arnez has just finished calling on all customers in the city of Tarrytown. His next appointment is at 2:00 P.M. in the city of Austex, twenty miles down the road. Arnez starts out for Austex, but halfway there he decides to visit a former college roommate who runs a farm ten miles off the main highway. Arnez is enjoying his visit with his former roommate when he realizes that it is 1:45 P.M. and that he will be late for the appointment in Austex. Driving at a high speed down the country road to reach the main highway, Arnez crashes his car into a tractor, severely injuring Thomas, the driver of the tractor. Thomas claims that he can hold ABC Tire

Corp. liable for his injuries. Discuss fully ABC's liability in this situation.

33–5. Liability for Independent Contractor's Torts Dean Brothers Corp. owns and operates a steel drum manufacturing plant. Lowell Wyden, the plant superintendent, hired Best Security Patrol, Inc. (BSP), a security company, to guard Dean property and "deter thieves and vandals." Some BSP security guards, as Wyden knew, carried firearms. Pete Sidell, a BSP security guard, was not certified as an armed guard but nevertheless brought his gun, in a briefcase, to work. While working at the Dean plant on October 31, 2010, Sidell fired his gun at Tyrone Gaines, in the belief that Gaines was an intruder. The bullet struck and killed Gaines. Gaines's mother filed a lawsuit claiming that her son's death was the result of BSP's negligence, for which Dean was responsible. What is the plaintiff's best argument that Dean is responsible for BSP's actions? What is Dean's best defense? Explain.

33–6. Principal's Liability for Contracts In 1998, William Larry Smith signed a lease for certain land in Chilton County, Alabama, owned by Sweet Smitherman. The lease stated that it was between "Smitherman, and WLS, Inc., d/b/a [doing business as] S&H Mobile Homes," and the signature line identified the lessee as "WLS, Inc. d/b/a S&H Mobile Homes . . . By: William Larry Smith, President." The amount of the rent was $5,000, payable by the tenth of each month. All of the checks that Smitherman received for the rent identified the owner of the account as "WLS Corporation d/b/a S&H Mobile Homes." Nearly four years later, Smitherman filed a suit in an Alabama state court against William Larry Smith, alleging that he owed $26,000 in unpaid rent. Smith responded, in part, that WLS was the lessee and that he was not personally responsible for the obligation to pay the rent. Is Smith a principal, an agent, both a principal and an agent, or neither? In any event, in the lease, is the principal disclosed, partially disclosed, or undisclosed? With the answers to these questions in mind, who is liable for the unpaid rent, and why? Discuss. [*Smith v. Smitherman*, 887 So.2d 285 (Ala.Civ.App. 2004)]

33–7. CASE PROBLEM WITH SAMPLE ANSWER: Apparent Authority.

Lee Dennegar and Mark Knutson lived in Dennegar's house in Raritan, New Jersey. Dennegar paid the mortgage and other household expenses. With Dennegar's consent, Knutson managed their household's financial affairs and the "general office functions concerned with maintaining the house." Dennegar allowed Knutson to handle the mail and "to do with it as he chose." Knutson wrote checks for Dennegar to sign, although Knutson signed Dennegar's name to many of the checks with Dennegar's consent. AT&T Universal issued a credit card in Dennegar's name in February 2001. Monthly statements were mailed to Dennegar's house, and payments were sometimes made on those statements. Knutson died in June 2003. The unpaid charges on the card of $14,752.93 were assigned to New Century Financial Services, Inc. New Century filed a suit in a New Jersey state court against Dennegar to collect the unpaid amount. Dennegar claimed that he never applied for or used the card and knew nothing about it. Under what theory could Dennegar be liable for the charges? Explain. [New Century Financial Services, Inc. v. Dennegar, *394 N.J.Super. 595, 928 A.2d 48 (A.D. 2007)*]

- **To view a sample answer for Problem 33–7, go to this book's Web site at www.cengage.com/blaw/clarkson, select "Chapter 33," and click on "Case Problem with Sample Answer."**

33–8. Undisclosed Principal Homeowners Jim and Lisa Criss hired Kevin and Cathie Pappas, doing business as Outside Creations, to undertake a landscaping project. Kevin signed the parties' contract as "Outside Creations Rep." The Crisses made payments on the contract with checks payable to Kevin, who deposited them in his personal account—there was no Outside Creations account. Later, alleging breach of contract, the Crisses filed a suit in a Georgia state court against the Pappases. The defendants contended that they could not be liable because the contract was not with them personally. They claimed that they were the agents of Forever Green Landscaping and Irrigation, Inc., which had been operating under the name "Outside Creations" at the time of the contract and had since filed for bankruptcy. The Crisses pointed out that the name "Forever Green" was not in the contract. Can the Pappases be liable on this contract? Why or why not? [*Pappas v. Criss*, 296 Ga.App. 803, 676 S.E.2d 21 (2009)]

33–9. Liability Based on Actual or Apparent Authority Summerall Electric Co. and other subcontractors were hired by National Church Services, Inc. (NCS), which was the general contractor on a construction project for the Church of God at Southaven. As work progressed, payments from NCS to the subcontractors were late and eventually stopped altogether. The church had paid NCS in full for the entire project beforehand, but apparently NCS had mismanaged the project. When payments from NCS stopped, the subcontractors filed *mechanic's liens* (see page 546 in Chapter 28) for the value of the work they had performed but for which they had not been paid. The subcontractors sued the church, contending that it was liable for the payments because NCS was its agent on the basis of either actual or apparent authority. Was NCS an agent for the church, thereby making the church liable to the subcontractors? Explain your reasoning. [*Summerall Electric Co. v. Church of God at Southaven*, 25 So.3d 1090 (App.Miss. 2010)]

33–10. A QUESTION OF ETHICS: Power of Attorney.

Warren Davis lived with Renee Brandt in a house that Davis owned in Virginia Beach, Virginia. At Davis's request, attorney Leigh Ansell prepared, and Davis acknowledged, a durable power of attorney appointing Ansell to act as Davis's attorney-in-fact. Ansell was authorized to sign "any . . . instrument of . . . deposit" and "any contract . . . relating to . . . personal property." Ansell could act "in any circumstances as

DEMAND FOR AN ACCOUNTING An agent can also withhold further performance and demand that the principal give an accounting. For example, a sales agent may demand an accounting if the agent and principal disagree on the amount of commissions the agent should have received for sales made during a specific period of time.

NO RIGHT TO SPECIFIC PERFORMANCE When the principal-agent relationship is not contractual, the agent has no right to specific performance. An agent can recover for past services and future damages but cannot force the principal to allow him or her to continue acting as an agent.

Principal's Rights and Remedies against the Agent

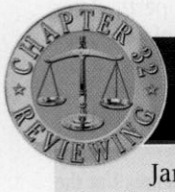
In general, a principal has contract remedies for an agent's breach of fiduciary duties. The principal also has tort remedies if the agent engages in misrepresentation, negligence, deceit, libel, slander, or trespass. In addition, any breach of a fiduciary duty by an agent may justify the principal's termination of the agency. The main actions available to the principal are constructive trust, avoidance, and indemnification.

CONSTRUCTIVE TRUST Anything that an agent obtains by virtue of the employment or agency relationship belongs to the principal. An agent commits a breach of fiduciary duty if he or she secretly retains benefits or profits that, by right, belong to the principal. For example, Lee, a purchasing agent for Metcalf, receives cash rebates from a customer. If Lee keeps the rebates for himself, he violates his fiduciary duty to his principal, Metcalf. On finding out about the cash rebates, Metcalf can sue Lee and recover them.

AVOIDANCE When an agent breaches the agency agreement or agency duties under a contract, the principal has a right to avoid any contract entered into with the agent. This right of avoidance is at the election of the principal.

INDEMNIFICATION In certain situations, when a principal is sued by a third party for an agent's negligent conduct, the principal can sue the agent for indemnification—that is, for an equal amount of damages. The same holds true if the agent violates the principal's instructions. For example, Parker (the principal) owns a used-car lot where Moore (the agent) works as a salesperson. Parker tells Moore to make no warranties for the used cars. Moore is eager to make a sale to Walters, a customer, and adds a 50,000-mile warranty for the car's engine. Parker may still be liable to Walters for engine failure, but if Walters sues Parker, Parker normally can then sue Moore for indemnification for violating his instructions.

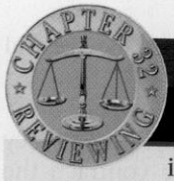
Sometimes, it is difficult to distinguish between instructions of the principal that limit an agent's authority and those that are merely advice. For example, Gutierrez (the principal) owns an office supply company, and Logan (the agent) is the manager. Gutierrez tells Logan, "Don't purchase any more inventory this month." Gutierrez goes on vacation. A large order comes in from a local business, and the inventory on hand is insufficient to meet it. What is Logan to do? In this situation, Logan probably has the inherent authority to purchase more inventory despite Gutierrez's command. It is unlikely that Logan would be required to indemnify Gutierrez in the event that the local business subsequently canceled the order.



REVIEWING
Agency Formation and Duties

James Blatt hired Marilyn Scott to sell insurance for the Massachusetts Mutual Life Insurance Co. Their contract stated, "Nothing in this contract shall be construed as creating the relationship of employer and employee." The contract was terminable at will by either party. Scott financed her own office and staff, was paid according to performance, had no taxes withheld from her checks, and could legally sell products of Massachusetts Mutual's competitors. But when Blatt learned that Scott was simultaneously selling insurance for Perpetual Life Insurance Corp., one of Massachusetts Mutual's fiercest competitors, Blatt withheld client contact information from Scott that would have assisted her

REVIEWING CONTINUES ➧



REVIEWING
Agency Formation and Duties, Continued

insurance sales for Massachusetts Mutual. Scott complained to Blatt that he was inhibiting her ability to sell insurance for Massachusetts Mutual. Blatt subsequently terminated their contract. Scott filed a suit in a New York state court against Blatt and Massachusetts Mutual. Scott claimed that she had lost sales for Massachusetts Mutual—and her commissions—as a result of Blatt's withholding contact information from her. Using the information presented in the chapter, answer the following questions.

1. Who is the principal and who is the agent in this scenario? By which method was an agency relationship formed between Scott and Blatt?
2. What facts would the court consider most important in determining whether Scott was an employee or an independent contractor?
3. How would the court most likely rule on Scott's employee status? Why?
4. Which of the four duties that Blatt owed Scott in their agency relationship has probably been breached?

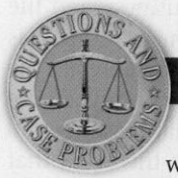
DEBATE THIS: *All works created by independent contractors should be considered works for hire under copyright law.*

TERMS AND CONCEPTS

agency 624

fiduciary 624

independent contractor 625



QUESTIONS AND CASE PROBLEMS

32–1. Agency Formation Paul Gett is a well-known, wealthy financial expert living in the city of Torris. Adam Wade, Gett's friend, tells Timothy Brown that he is Gett's agent for the purchase of rare coins. Wade even shows Brown a local newspaper clipping mentioning Gett's interest in coin collecting. Brown, knowing of Wade's friendship with Gett, contracts with Wade to sell a rare coin valued at $25,000 to Gett. Wade takes the coin and disappears with it. On the payment due date, Brown seeks to collect from Gett, claiming that Wade's agency made Gett liable. Gett does not deny that Wade was a friend, but he claims that Wade was never his agent. Discuss fully whether an agency was in existence at the time the contract for the rare coin was made.

32–2. QUESTION WITH SAMPLE ANSWER: Duty of Loyalty.

Peter hires Alice as an agent to sell a piece of property he owns. The price is to be at least $30,000. Alice discovers that the fair market value of Peter's property is actually at least $45,000 and could be higher because a shopping mall is going to be built nearby. Alice forms a real estate partnership with her cousin Carl, and she prepares for Peter's signature a contract for the sale of the property to Carl for $32,000. Peter signs the contract. Just before closing and passage of title, Peter learns about the shopping mall and the increased fair market value of his property. Peter refuses to deed the property to Carl. Carl claims that Alice, as agent, solicited a price above that agreed on when the agency was created and that the contract is therefore binding and enforceable. Discuss fully whether Peter is bound to this contract.

- **For a sample answer to Question 32–2, go to Appendix I at the end of this text.**

32–3. Principal's Remedies against Agent Ankir is hired by Jamison as a traveling salesperson. Ankir not only solicits orders but also delivers the goods and collects payments from his customers. Ankir deposits all payments in his private checking account and at the end of each month draws sufficient cash from his bank to cover the payments made. Jamison is totally unaware of this procedure. Because of a slowdown in the economy, Jamison

tells all his salespeople to offer 20 percent discounts on orders. Ankir solicits orders, but he offers only 15 percent discounts, pocketing the extra 5 percent paid by customers. Ankir has not lost any orders by this practice, and he is rated as one of Jamison's top salespersons. Jamison learns of Ankir's actions. Discuss fully Jamison's rights in this matter.

32–4. Agency Formation Ford Motor Credit Co. is a subsidiary of Ford Motor Co. with its own offices, officers, and directors. Ford Credit buys contracts and leases of automobiles entered into by dealers and consumers. Ford Credit also provides inventory financing for dealers' purchases of Ford and non-Ford vehicles and makes loans to Ford and non-Ford dealers. Dealers and consumers are not required to finance their purchases or leases of Ford vehicles through Ford Credit. Ford Motor is not a party to the agreements between Ford Credit and its customers and does not directly receive any payments under those agreements. Also, Ford Credit is not subject to any agreement with Ford Motor "restricting or conditioning" its ability to finance the dealers' inventories or the consumers' purchases or leases of vehicles. A number of plaintiffs filed a product liability suit in a Missouri state court against Ford Motor. Ford Motor claimed that the court did not have venue. The plaintiffs asserted that Ford Credit, which had an office in the jurisdiction, acted as Ford's "agent for the transaction of its usual and customary business" there. Is Ford Credit an agent of Ford Motor? Discuss. [*State ex rel. Ford Motor Co. v. Bacon*, 63 S.W.3d 641 (Mo. 2002)]

32–5. Agent's Duties to Principal Sam and Theresa Daigle decided to build a home in Cameron Parish, Louisiana. To obtain financing, they contacted Trinity United Mortgage Co. At a meeting with Joe Diez on Trinity's behalf, on July 18, 2001, the Daigles signed a temporary loan agreement with Union Planters Bank. Diez assured them that they did not need to make payments on this loan until their house was built and permanent financing had been secured. Because the Daigles did not make payments on the Union loan, Trinity declined to make the permanent loan. Meanwhile, Diez left Trinity's employ. On November 1, the Daigles moved into their new house. They tried to contact Diez at Trinity but were told that he was unavailable and would get back to them. Three weeks later, Diez came to the Daigles' home and had them sign documents that they believed were to secure a permanent loan but that were actually an application with Diez's new employer. Union filed a suit in a Louisiana state court against the Daigles for failing to pay on its loan. The Daigles paid Union, obtained permanent financing through another source, and filed a suit against Trinity to recover the cost. Who should have told the Daigles that Diez was no longer Trinity's agent? Could Trinity be liable to the Daigles on this basis? Explain. [*Daigle v. Trinity United Mortgage, L.L.C.*, 890 So.2d 583 (La.App. 3 Cir. 2004)]

32–6. Principal's Duties to Agent Josef Boehm was an officer and the majority shareholder of Alaska Industrial Hardware, Inc. (AIH), in Anchorage, Alaska. In August 2001, Lincolnshire Management, Inc., in New York, created AIH Acquisition Corp. to buy AIH. The three firms signed a "commitment letter" to negotiate "a definitive stock purchase agreement" (SPA). In September, Harold Snow and Ronald Braley began to work, on Boehm's behalf, with Vincent Coyle, an agent for AIH Acquisition, to produce an SPA. They exchanged many drafts and dozens of e-mails. Finally, in February 2002, Braley told Coyle that Boehm would sign the SPA "early next week." That did not occur, however, and at the end of March, after more negotiations and drafts, Boehm demanded a larger payment. AIH Acquisition agreed, and, following more work by the agents, another SPA was drafted. In April, the parties met in Anchorage. Boehm still refused to sign. AIH Acquisition and others filed a suit in a federal district court against AIH. Did Boehm violate any of the duties that principals owe to their agents? If so, which duty, and how was it violated? Explain. [*AIH Acquisition Corp., LLC v. Alaska Industrial Hardware, Inc.*, __ F.Supp.2d __ (S.D.N.Y. 2004)]

32–7. CASE PROBLEM WITH SAMPLE ANSWER: Agent's Duties to Principal.

In July 2001, John Warren viewed a condominium in Woodland Hills, California, as a potential buyer. Hildegard Merrill was the agent for the seller. Because Warren's credit rating was poor, Merrill told him he needed a co-borrower to obtain a mortgage at a reasonable rate. Merrill said that her daughter Charmaine would "go on title" until the loan and sale were complete if Warren would pay her $10,000. Merrill also offered to defer her commission on the sale as a loan to Warren so that he could make a 20 percent down payment on the property. He agreed to both plans. Merrill applied for and secured the mortgage in Charmaine's name alone by misrepresenting her daughter's address, business, and income. To close the sale, Merrill had Warren remove his name from the title to the property. In October, Warren moved into the condominium, repaid Merrill the amount of her deferred commission, and began paying the mortgage. Within a few months, Merrill had Warren evicted. Warren filed a suit in a California state court against Merrill and Charmaine. Who among these parties was in an agency relationship? What is the basic duty that an agent owes a principal? Was the duty breached here? Explain. [Warren v. Merrill, *143 Cal.App.4th 96, 49 Cal. Rptr.3d 122 (2 Dist. 2006)]*

- **To view a sample answer for Problem 32–7, go to this book's Web site at www.cengage.com/blaw/clarkson, select "Chapter 32," and click on "Case Problem with Sample Answer."**

32–8. Agent's Duties to Principal Su Ru Chen owned the Lucky Duck Fortune Cookie Factory in Everett, Massachusetts, which made Chinese-style fortune cookies for restaurants. In November 2001, Chen listed the business for sale with Bob Sun, a real estate broker, for $35,000. Sun's daughter Frances and her fiancé, Chiu Chung Chan, decided that Chan would buy the business. Acting as a broker on Chen's (the seller's) behalf, Frances asked about the Lucky Duck's finances. Chen said that each

month the business sold at least 1,000 boxes of cookies at a $2,000 profit. Frances negotiated a price of $23,000, which Chan (her fiancé) paid. When Chan began to operate the Lucky Duck, it became clear that the demand for the cookies was actually about 500 boxes per month—a rate at which the business would suffer losses. Less than two months later, the factory closed. Chan filed a suit in a Massachusetts state court against Chen, alleging fraud, among other things. Chan's proof included Frances's testimony as to what Chen had said to her. Chen objected to the admission of this testimony. What is the basis for this objection? Should the court admit the testimony? Why or why not? [*Chan v. Chen*, 70 Mass.App.Ct. 79, 872 N.E.2d 1153 (2007)]

32–9. Agency by Ratification Wesley Hall, an independent contractor managing property for Acree Investments, Ltd., lost control of a fire he had set to clear ten acres of Acree land. The runaway fire burned seventy-eight acres of Earl Barrs's property. Russell Acree, one of the owners of Acree Investments, had previously owned the ten acres, but he had put it into the company and was no longer the principal owner. Hall had worked for Russell Acree in the past and had told the state forestry department that he was burning the land for Acree. Barrs sued Russell Acree for the acts of his agent, Hall. In his suit, Barrs noted that Hall had been an employee of Russell Acree, Hall had talked about burning the land "for Acree," Russell Acree had apologized to Barrs for the fire, and Acree Investments had not been identified as the principal property owner until Barrs had filed his lawsuit. Barrs argued that those facts were sufficient to create an agency by ratification to impose liability on Russell Acree. Was Barrs's agency by ratification claim valid? Why or why not? [*Barrs v. Acree*, 691 S.E.2d 575 (Ga.App. 2010)]

32–10. A QUESTION OF ETHICS: Agency Formation and Duties. *Emergency One, Inc. (EO), makes fire and rescue vehicles. Western Fire Truck, Inc., contracted with EO to be its exclusive dealer in Colorado and Wyoming through December 2003. James Costello, a Western salesperson, was authorized to order EO vehicles for his customers. Without informing Western, Costello e-mailed EO about Western's difficulties in obtaining cash to fund its operations. He asked about the viability of Western's contract and his possible employment with EO. On EO's request, and in disregard of Western's instructions, Costello sent some payments for EO vehicles directly to EO. In addition, Costello, with EO's help, sent a competing bid to a potential Western customer. EO's representative e-mailed Costello, "You have my permission to kick [Western's] ass." In April 2002, EO terminated its contract with Western, which, after reviewing Costello's e-mail, fired Costello. Western filed a suit in a Colorado state court against Costello and EO, alleging, among other things, that Costello breached his duty as an agent and that EO aided and abetted the breach.* [Western Fire Truck, Inc. v. Emergency One, Inc., *134 P.3d 570 (Colo.App. 2006)]*

(a) Was there an agency relationship between Western and Costello? Western required monthly reports from its sales staff, but Costello did not report regularly. Does this indicate that Costello was *not* Western's agent? In determining whether an agency relationship exists, is the *right* to control or the *fact* of control more important? Explain.

(b) Did Costello owe Western a duty? If so, what was the duty? Did Costello breach it? If so, how?

(c) A Colorado state statute allows a court to award punitive damages in "circumstances of fraud, malice, or willful and wanton conduct." Did any of these circumstances exist in this case? Should punitive damages be assessed against either defendant? Why or why not?

LEGAL RESEARCH EXERCISES ON THE WEB

Go to this text's Web site at **www.cengage.com/blaw/clarkson**, select "Chapter 32," and click on "Practical Internet Exercises." There you will find the following Internet research exercises that you can perform to learn more about the topics covered in this chapter.

Practical Internet Exercise 32–1: Legal Perspective
Employees or Independent Contractors?

Practical Internet Exercise 32–2: Management Perspective
Problems with Using Independent Contractors