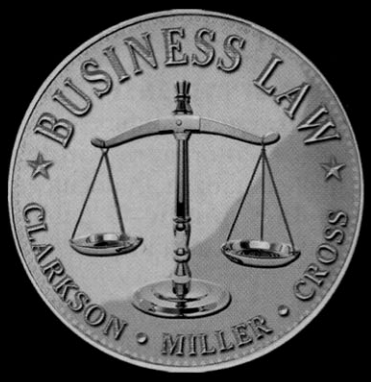
CHAPTER 33

Agency Liability and Termination



As discussed in the previous chapter, the law of agency focuses on the special relationship that exists between a principal and an agent–how the relationship is formed and the duties the principal and agent assume once the relationship is established. This chapter deals with another important aspect of agency law–the liability of principals and agents to third parties.

We look first at the liability of principals for contracts formed by agents with third parties. Generally, the liability of the principal will depend on whether the agent was authorized to form the contract. The second part of the chapter deals with an agent's liability to third parties in contract and tort, and the principal's liability to third parties because of an agent's torts. The chapter concludes with a discussion of how agency relationships are terminated.

SECTION 1
SCOPE OF AGENT'S AUTHORITY

The liability of a principal to third parties with whom an agent contracts depends on whether the agent had the authority to enter into legally binding contracts on the principal's behalf. An agent's authority can be either *actual* (express or implied) or *apparent*. If an agent contracts outside the scope of his or her authority, the principal may still become liable by ratifying the contract.

Express Authority

Express authority is authority declared in clear, direct, and definite terms. Express authority can be given orally or in writing.

THE EQUAL DIGNITY RULE In most states, the **equal dignity rule** requires that if the contract being executed is or must be in writing, then the agent's authority must also be in writing. Failure to comply with the equal dignity rule can make a contract voidable *at the option of the principal*. The law regards the contract at that point as a mere offer. If the principal decides to accept the offer, the acceptance must be ratified, or affirmed, in writing.

Assume that Paloma (the principal) orally asks Austin (the agent) to sell a ranch that Paloma owns. Austin finds a buyer and signs a sales contract (a contract for an interest in realty must be in writing) on behalf of Paloma to sell the ranch. The buyer cannot enforce the contract unless Paloma subsequently ratifies Austin's agency status in writing. Once the contract is ratified, either party can enforce rights under the contract.

Modern business practice allows an exception to the equal dignity rule. An executive officer of a corporation normally is not required to obtain written authority from the corporation to conduct *ordinary* business transactions. The equal dignity rule does not apply when the agent acts in the presence of the principal or when the agent's act of signing is merely perfunctory (token or customary). Thus, if Healy (the principal) negotiates a contract but is called out of town the day it is to be signed and orally authorizes Santini to sign, the oral authorization is sufficient.

POWER OF ATTORNEY Giving an agent a **power of attorney** confers express authority.[1] The power of attorney is a written document and is usually notarized. (A document is notarized when a **notary public**—a public official authorized to attest to the authenticity of signatures—signs and dates the document and imprints it with her or his seal of authority.) Most states have statutory provisions for creating a power of attorney. A power of attorney can be special (permitting the agent to perform specified acts only), or it can be general (permitting the agent to transact all business for the principal). Because of the extensive authority granted to an agent by a general power of attorney (see Exhibit 33–1 below), it should be used with great caution and usually only in exceptional circumstances. Ordinarily, a power of

1. An agent who holds a power of attorney is called an *attorney-in-fact* for the principal. The holder does not have to be an attorney-at-law (and often is not).

EXHIBIT 33–1 • A Sample General Power of Attorney

GENERAL POWER OF ATTORNEY

Know All Men by These Presents:

That I, _____, hereinafter referred to as PRINCIPAL, in the County of _____
State of _____, do(es) appoint _____ as my true and lawful attorney.

In principal's name, and for principal's use and benefit, said attorney is authorized hereby;

(1) To demand, sue for, collect, and receive all money, debts, accounts, legacies, bequests, interest, dividends, annuities, and demands as are now or shall hereafter become due, payable, or belonging to principal, and take all lawful means, for the recovery thereof and to compromise the same and give discharges for the same;
(2) To buy and sell land, make contracts of every kind relative to land, any interest therein or the possession thereof, and to take possession and exercise control over the use thereof;
(3) To buy, sell, mortgage, hypothecate, assign, transfer, and in any manner deal with goods, wares and merchandise, choses in action, certificates or shares of capital stock, and other property in possession or in action, and to make, do, and transact all and every kind of business of whatever nature;
(4) To execute, acknowledge, and deliver contracts of sale, escrow instructions, deeds, leases including leases for minerals and hydrocarbon substances and assignments of leases, covenants, agreements and assignments of agreements, mortgages and assignments of mortgages, conveyances in trust, to secure indebtedness or other obligations, and assign the beneficial interest thereunder, subordinations of liens or encumbrances, bills of lading, receipts, evidences of debt, releases, bonds, notes, bills, requests to reconvey deeds of trust, partial or full judgments, satisfactions of mortgages, and other debts, and other written instruments of whatever kind and nature, all upon such terms and conditions as said attorney shall approve.

GIVING AND GRANTING to said attorney full power and authority to do all and every act and thing whatsoever requisite and necessary to be done relative to any of the foregoing as fully to all intents and purposes as principal might or could do if personally present.

All that said attorney shall lawfully do or cause to be done under the authority of this power of attorney is expressly approved.

Dated: _____ /s/_____

State of _____ } SS.
County of _____
On _____, before me, the undersigned, a Notary Public in and for said State, personally appeared _____
_____
known to me to be the person _____ whose name _____ subscribed to the within instrument and acknowledged that _____ executed the same.

Witness my hand and official seal. (Seal) _____
Notary Public in and for said State.

attorney terminates on the incapacity or death of the person giving the power.[2]

Implied Authority

An agent has the **implied authority** to do what is reasonably necessary to carry out express authority and accomplish the objectives of the agency. Authority can also be implied by custom or inferred from the position the agent occupies. For example, Archer is employed by Packard Grocery to manage one of its stores. Packard has not expressly stated that Archer has authority to contract with third persons. Nevertheless, authority to manage a business implies authority to do what is reasonably required (as is customary or can be inferred from a manager's position) to operate the business. This includes forming contracts to hire employees, to buy merchandise and equipment, and to advertise the products sold in the store.

In general, implied authority is authority customarily associated with the position occupied by the agent or authority that can be inferred from the express authority given to the agent to perform fully his or her duties. For example, an agent has authority to solicit orders for goods sold by the principal. The agent, however, does not carry any goods with him when soliciting orders, and thus generally would not have the authority to collect payments for the goods. The test is whether it was reasonable for the agent to believe that she or he had the authority to enter into the contract in question.

Also note that an agent's implied authority cannot contradict his or her express authority. Thus, if a principal has limited an agent's authority—by forbidding a manager to enter into contracts to hire additional workers, for example—then the fact that managers customarily would have such authority is irrelevant.

2. A *durable* power of attorney, however, continues to be effective despite the principal's incapacity. An elderly person, for example, might grant a durable power of attorney to provide for the handling of property and investments or specific health-care needs should he or she become incompetent (see Chapter 52).

Apparent Authority

Actual authority (express or implied) arises from what the principal makes clear *to the agent*. Apparent authority, in contrast, arises from what the principal causes a third party to believe. An agent has **apparent authority** when the principal, by either word or action, causes a *third party* reasonably to believe that the agent has authority to act, even though the agent has no express or implied authority.

A PATTERN OF CONDUCT Apparent authority usually comes into existence through a principal's pattern of conduct over time. For example, Ashley is a traveling salesperson with the authority to solicit orders for a principal's goods. Because she does not carry any goods with her, she normally would not have the implied authority to collect payments from customers on behalf of the principal. Suppose that she does accept payments from Cabo Enterprises, however, and submits them to the principal's accounting department for processing. If the principal does nothing to stop Ashley from continuing this practice, a pattern develops over time, and the principal confers apparent authority on Ashley to accept payments from Cabo.

In the following case, an employee misappropriated more than $1 million from her employer by using his credit card without authorization over a number of years. The issue before the court was whether the employee had apparent authority to use the card.

CASE 33.1
Azur v. Chase Bank, USA

United States Court of Appeals, Third Circuit, 601 F.3d 212 (2010).
www.ca3.uscourts.gov[a]

BACKGROUND AND FACTS • ATM Corporation of America, Inc. (ATM), manages settlement services for large national lenders. Francis Azur, the founder of ATM, served as its president and chief executive officer until September 2007, when ATM was sold. In July 1997, ATM hired Michelle Vanek to be Azur's personal assistant. Vanek's responsibilities included opening Azur's personal bills, preparing and

a. Under "Opinions and Oral Arguments," select "Search for Opinions." When the search page appears, type "Azur" in the search box and click on "Go." When the case information appears at the bottom of the search page, click on the highlighted link to the PDF to access the case. The U.S. Court of Appeals for the Third Circuit maintains this Web site.

CASE CONTINUES

CASE 33.1 CONTINUED ➧ presenting checks for Azur to sign, balancing Azur's checking and savings accounts, and reviewing his credit-card and bank statements. Vanek also had access to Azur's credit-card number so that she could make purchases for him. Over a period of seven years, Vanek withdrew unauthorized cash advances of between $200 and $700, typically twice a day, from Azur's credit-card account with Chase Bank, USA. The fraudulent charges were reflected on at least sixty-five monthly billing statements sent by Chase to Azur, and Vanek paid the bills by either writing checks and forging Azur's signature or making online payments from Azur's checking account. In all, Vanek misappropriated more than $1 million from Azur. When Azur discovered Vanek's fraudulent scheme in 2006, he terminated her employment and closed the Chase account. Azur sued Chase, seeking reimbursement of the fraudulent charges under Section 1643 of the Truth-in-Lending Act, or TILA.[b] A magistrate judge concluded that Azur's claim failed because Vanek had apparent authority to use Azur's credit card. The trial court—a U.S. district court—agreed and granted Chase's motion for summary judgment on this issue. Azur appealed.

IN THE LANGUAGE OF THE COURT

FISHER, Circuit Judge.

* * * *

* * * [Section 1643 of the TILA] provides that "[a] cardholder shall be liable for the unauthorized use of a credit card" in certain circumstances. The term *"unauthorized use" is defined as the "use of a credit card by a person other than the cardholder who does not have actual, implied, or apparent authority for such use and from which the cardholder receives no benefit."* [Emphasis added.]

To determine whether apparent authority exists, we turn to applicable state agency law. * * * Citing the *Restatement (Second) of Agency*, the Pennsylvania Supreme Court has explained as follows:

> Apparent authority is power to bind a principal which the principal has not actually granted but which he leads persons with whom his agent deals to believe that he has granted. Persons with whom the agent deals can reasonably believe that the agent has power to bind his principal if, for instance, the principal knowingly permits the agent to exercise such power or if the principal holds the agent out as possessing such power.
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> * * * *
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> * * * A cardholder may, in certain circumstances, vest a fraudulent user with the apparent authority to use a credit card by enabling the continuous payment of the credit card charges over a period of time.

Here, Azur's negligent omissions led Chase to reasonably believe that the fraudulent charges were authorized. Although Azur may not have been aware that Vanek was using the Chase credit card, or even that the Chase credit card account existed, Azur knew that he had a Dollar Bank checking account, and he did not review his Dollar Bank statements or exercise any other oversight over Vanek, his employee. * * * Had Azur occasionally reviewed his statements, Azur would have likely noticed that checks had been written to Chase. Because Chase reasonably believed that a prudent business person would oversee his employees in such a manner, Chase reasonably relied on the continuous payment of the fraudulent charges.

DECISION AND REMEDY • *The U.S. Court of Appeals for the Third Circuit affirmed the trial court's judgment, holding that Azur had vested Vanek with apparent authority to use the Chase credit card.*

THE ETHICAL DIMENSION • *The TILA essentially is a consumer-protection law. How does allowing a credit-card company to avoid liability—if a card user has apparent authority to use the card—protect consumers?*

MANAGERIAL IMPLICATIONS • *Business owners and managers should take precautions to avoid being held liable, under a theory of apparent authority, for unauthorized credit-card charges made by their employees. Any employee who has access to the employer's credit-card number, credit-card statements, bank accounts, and other financial data should be carefully supervised. The employer should periodically review bank statements and credit-card payments to ensure that no checks have been forged and that all payments to credit-card companies are for authorized charges.*

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b. Among other things, the Truth-in-Lending Act (TILA) protects holders of credit cards from liability for the fraudulent use of their credit cards. (See Chapter 45 for a detailed discussion of this consumer-protection statute.)

APPARENT AUTHORITY AND ESTOPPEL The doctrine of agency by estoppel (introduced in Chapter 32) may be applied in situations in which a principal has given a third party reason to believe that an agent has authority to act. If the third party changes position to his or her detriment in good faith reliance on the principal's representations, the principal may be *estopped* (prevented) from denying that the agent had authority.

In the following case, the court applied the doctrine of estoppel to a situation involving a question of apparent authority or, as the court referred to it, "ostensible authority."

CASE 33.2
Ermoian v. Desert Hospital

Court of Appeal of California, Fourth District, 152 Cal.App.4th 475, 61 Cal.Rptr.3d 754 (2007).

BACKGROUND AND FACTS • In 1990, Desert Hospital in California established a comprehensive perinatal services program (CPSP) to provide obstetrical care to women who were uninsured (*perinatal* is often defined as relating to the period from about the twenty-eighth week of pregnancy to around one month after birth). The CPSP was set up in an office suite across from the hospital and named "Desert Hospital Outpatient Maternity Services Clinic." The hospital contracted with a corporation controlled by Dr. Morton Gubin, which employed Dr. Masami Ogata, to provide obstetrical services. In January 1994, Jackie Shahan went to the hospital's emergency room because of cramping and other symptoms. The emergency room physician told Shahan that she was pregnant and referred her to the clinic. Shahan visited the clinic throughout her pregnancy. On May 15, Shahan's baby, Amanda Ermoian, was born with brain abnormalities that left her severely mentally retarded and unable to care for herself. Her conditions could not have been prevented, treated, or cured *in utero*. Through a guardian, Amanda filed a suit in a California state court against the hospital and others, alleging "wrongful life." She claimed that the defendants negligently failed to inform her mother of her abnormalities before her birth, depriving her mother of the opportunity to make an informed choice to terminate the pregnancy. The court ruled in the defendants' favor, holding, among other things, that the hospital was not liable because Drs. Gubin and Ogata were not its employees. Amanda appealed to a state intermediate appellate court, contending that the physicians were the hospital's "ostensible agents."

IN THE LANGUAGE OF THE COURT

KING, J. [Judge]

* * * *

Agency may be either actual or ostensible [apparent]. Actual agency exists when the agent is really employed by the principal. Here, there was evidence that the physicians were not employees of the Hospital, but were physicians with a private practice who contracted with the Hospital to perform obstetric services at the clinic. The written contract between the Hospital and Dr. Gubin's corporation (which employed Dr. Ogata) describes Dr. Gubin and his corporation as "independent contractors with, and not as employees of, [the] Hospital." [Maria Sterling, a registered nurse at the clinic and Shahan's CPSP case coordinator] testified that Drs. Gubin and Ogata, not the Hospital, provided the obstetric services to the clinic's patients. Donna McCloudy, a director of nursing [who set up the CPSP] at the Hospital, testified that while the Hospital provided some aspects of the CPSP services, "independent physicians * * * provided the obstetrical care * * *." Based upon such evidence, the [trial] court reasonably concluded that the physicians were not the employees or actual agents of the Hospital for purposes of vicarious [indirect] liability.

Ostensible [apparent] agency on the other hand, may be implied from the facts of a particular case, and if a principal by his acts has led others to believe that he has conferred authority upon an agent, he cannot be heard to assert, as against third parties who have relied thereon in good faith, that he did not intend to confer such power * * *. The doctrine establishing the principles of liability for the acts of an ostensible agent rests on the doctrine of estoppel. *The essential elements are representations by the principal, justifiable reliance thereon by a third party,*

CASE CONTINUES ➧

CASE 33.2 CONTINUED ➧ *and change of position or injury resulting from such reliance.* Before recovery can be had against the principal for the acts of an ostensible agent, the person dealing with an agent must do so with belief in the agent's authority and this belief must be a reasonable one. Such belief must be generated by some act or neglect by the principal sought to be charged and the person relying on the agent's apparent authority must not be guilty of neglect. [Emphasis added.]

* * * *

Here, the Hospital held out the clinic and the personnel in the clinic as part of the Hospital. Furthermore, it was objectively reasonable for Shahan to believe that Drs. Gubin and Ogata were employees of the Hospital. The clinic was located across the street from the Hospital. It used the same name as the Hospital and labeled itself as an outpatient clinic. Numerous professionals at the clinic were employees of the Hospital. [Carol Cribbs, a comprehensive perinatal health worker at the clinic] and Sterling indicated to Shahan that they were employees of the Hospital and that the program was run by the Hospital. Sterling personally set up all of Shahan's appointments at the main Hospital rather than giving Shahan a referral for the various tests. Shahan was referred by individuals in the emergency room specifically to Dr. Gubin. When she called for an appointment she was told by the receptionist that she was calling the Hospital outpatient clinic which was the clinic of Dr. Gubin. On days when Shahan would see either Dr. Gubin or Dr. Ogata at the clinic, she would also see either Cribbs or Sterling, whom she knew were employed by the Hospital.

* * * At her first appointment she signed a document titled "patient rights and responsibilities," which would unambiguously lead a patient to the conclusion that the clinic "was a one-stop shop for the patient," and that all individuals at the clinic were connected with the Hospital. All of Shahan's contacts with the physicians were at the Hospital-run clinic. Most, if not all, of the physician contacts occurred in conjunction with the provision of other services by either Sterling or Cribbs. The entire appearance created by the Hospital, and those associated with it, was that the Hospital was the provider of the obstetrical care to Shahan.

DECISION AND REMEDY • *The state intermediate appellate court decided that, contrary to the lower court's finding, Drs. Gubin and Ogata were "ostensible agents of the Hospital." The appellate court affirmed the lower court's ruling, however, on Amanda's "wrongful life" claim, concluding that the physicians were not negligent in failing to advise Shahan to have an elective abortion.*

THE ETHICAL DIMENSION • *Does a principal have an ethical responsibility to inform an unaware third party that an apparent (ostensible) agent does not in fact have authority to act on the principal's behalf?*

THE E-COMMERCE DIMENSION • *Could Amanda have established Drs. Gubin and Ogata's apparent authority if Desert Hospital had maintained a Web site that advertised the services of the CPSP clinic and stated clearly that the physicians were not its employees? Explain.*

Emergency Powers

When an unforeseen emergency demands action by the agent to protect or preserve the property and rights of the principal, but the agent is unable to communicate with the principal, the agent has emergency power. For example, Fulsom is an engineer for Pacific Drilling Company. While Fulsom is acting within the scope of his employment, he is severely injured in an accident at an oil rig many miles from home. Acosta, the rig supervisor, directs Thompson, a physician, to give medical aid to Fulsom and to charge Pacific for the medical services. Acosta, an agent, has no express or implied authority to bind the principal, Pacific Drilling, for Thompson's medical services. Because of the emergency situation, however, the law recognizes Acosta as having authority to act appropriately under the circumstances.

Ratification

Ratification occurs when the principal affirms, or accepts responsibility for, an agent's *unauthorized* act. When ratification occurs, the principal is bound to the agent's act, and the act is treated as if it had been authorized by the principal *from the outset.* Ratification can be either express or implied.

If the principal does not ratify the contract, the principal is not bound, and the third party's agreement with the agent is viewed as merely an unaccepted offer. Because the third party's agreement is

an unaccepted offer, the third party can revoke it at any time, without liability, before the principal ratifies the contract. The agent, however, may be liable to the third party for misrepresenting her or his authority.

The requirements for ratification can be summarized as follows:

1. The agent must have acted on behalf of an identified principal who subsequently ratifies the action.
2. The principal must know all of the material facts involved in the transaction. If a principal ratifies a contract without knowing all of the facts, the principal can rescind (cancel) the contract.[3]
3. The principal must affirm the agent's act in its entirety.
4. The principal must have the legal capacity to authorize the transaction at the time the agent engages in the act and at the time the principal ratifies. The third party must also have the legal capacity to engage in the transaction.
5. The principal's affirmation (ratification) must occur before the third party withdraws from the transaction.
6. The principal must observe the same formalities when ratifying the act as would have been required to authorize it initially.

Concept Summary 33.1 below summarizes the rules concerning an agent's authority to bind the principal and a third party.

3. If the third party has changed position in reliance on the apparent contract, however, the principal can rescind but must reimburse the third party for any costs.

SECTION 2
LIABILITY FOR CONTRACTS

Liability for contracts formed by an agent depends on how the principal is classified and on whether the actions of the agent were authorized or unauthorized. Principals are classified as disclosed, partially disclosed, or undisclosed.[4]

A **disclosed principal** is a principal whose identity is known by the third party at the time the contract is made by the agent. A **partially disclosed principal** is a principal whose identity is not known by the third party, but the third party knows that the agent is or may be acting for a principal at the time the contract is made. An **undisclosed principal** is a principal whose identity is totally unknown by the third party, and the third party has no knowledge that the agent is acting in an agency capacity at the time the contract is made.

4. *Restatement (Third) of Agency*, Section 1.04 (2).

CONCEPT SUMMARY 33.1
Authority of an Agent to Bind the Principal and a Third Party

Authority of Agent	Definition	Effect on Principal and Third Party
Express Authority	Authority expressly given by the principal to the agent.	Principal and third party are bound in contract.
Implied Authority	Authority implied (1) by custom, (2) from the position in which the principal has placed the agent, or (3) because such authority is necessary if the agent is to carry out expressly authorized duties and responsibilities.	Principal and third party are bound in contract.
Apparent Authority	Authority created when the conduct of the principal leads a third party to believe that the principal's agent has authority.	Principal and third party are bound in contract.
Unauthorized Acts	Acts committed by an agent that are outside the scope of his or her express, implied, or apparent authority.	Principal and third party are not bound in contract—*unless* the principal ratifies prior to the third party's withdrawal.

Authorized Acts

If an agent acts within the scope of her or his authority, normally the principal is obligated to perform the contract regardless of whether the principal was disclosed, partially disclosed, or undisclosed. Whether the agent may also be held liable under the contract, however, depends on the disclosed, partially disclosed, or undisclosed status of the principal.

DISCLOSED OR PARTIALLY DISCLOSED PRINCIPAL A disclosed or partially disclosed principal is liable to a third party for a contract made by the agent. If the principal is disclosed, the agent has no contractual liability for the nonperformance of the principal or the third party. If the principal is partially disclosed, in most states the agent is also treated as a party to the contract, and the third party can hold the agent liable for contractual nonperformance.[5]

CASE IN POINT Walgreens leased commercial property at a mall owned by Kedzie Plaza Associates to operate a drugstore. A property management company, Taxman Corporation, signed the lease on behalf of the principal, Kedzie. The lease required the landlord to keep the sidewalks free of snow and ice, so Taxman, on behalf of Kedzie, contracted with another company to remove ice and snow from the sidewalks surrounding the Walgreens store. When a Walgreens employee slipped on ice outside the store and was injured, she sued Taxman, among others, for negligence. Because the principal's identity (Kedzie) was fully disclosed in the snow-removal contract, however, the court ruled that the agent, Taxman, could not be held liable. Taxman did not assume a contractual obligation to remove the snow but merely retained a contractor to do so on behalf of the owner.[6]

UNDISCLOSED PRINCIPAL When neither the fact of an agency relationship nor the identity of the principal is disclosed, the undisclosed principal is bound to perform just as if the principal had been fully disclosed at the time the contract was made.

When a principal's identity is undisclosed and the agent is forced to pay the third party, the agent is entitled to be *indemnified* (compensated) by the principal. The principal had a duty to perform, even though his or her identity was undisclosed,[7] and failure to do so will make the principal ultimately liable. Once the undisclosed principal's identity is revealed, the third party generally can elect to hold either the principal or the agent liable on the contract.

Conversely, the undisclosed principal can require the third party to fulfill the contract, *unless* (1) the undisclosed principal was expressly excluded as a party in the written contract; (2) the contract is a negotiable instrument signed by the agent with no indication of signing in a representative capacity;[8] or (3) the performance of the agent is personal to the contract, allowing the third party to refuse the principal's performance.

Unauthorized Acts

If an agent has no authority but nevertheless contracts with a third party, the principal cannot be held liable on the contract. It does not matter whether the principal was disclosed, partially disclosed, or undisclosed. The person who acted as an agent is liable, however. For example, Updike signs a contract for the purchase of a truck, purportedly acting as an agent under authority granted by Parker. In fact, Parker has not given Updike any such authority. Parker refuses to pay for the truck, claiming that Updike had no authority to purchase it. The seller of the truck is entitled to hold Updike liable for payment.

If an agent for a disclosed or partially disclosed principal contracts with a third party without authorization, the third party who relied on the agency status can also hold the agent liable for breaching the *implied warranty of authority*. The agent's liability here is based on the third party's reliance on the agent's purported authority, not on the breach of the contract itself.[9] For example, Pinnell, a reclusive artist, hires Auber to solicit offers for particular paintings from various galleries, but does not authorize her to enter into sales agreements. Olaf, a gallery owner, offers to buy two of Pinnell's paintings for an upcoming show. If Auber draws up a sales contract with Olaf, she impliedly warrants that she has the authority to enter into sales contracts on behalf of Pinnell. If Pinnell does not agree to ratify Auber's sales contract, Olaf cannot hold Pinnell liable, but he can hold Auber liable for breaching the implied warranty of authority.

Note that if the third party knows at the time the contract is made that the agent does not have authority, then the agent is not liable. Similarly, if the agent expressed to the third party *uncertainty* as to the extent of her or his authority, the agent is not personally liable.

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5. *Restatement (Third) of Agency,* Section 6.02.
6. *McBride v. Taxman Corp.*, 327 Ill.App.3d 992, 765 N.E.2d 51 (2002).
7. If the agent is a gratuitous agent, and the principal accepts the benefits of the agent's contract with a third party, then the principal will be liable to the agent on the theory of quasi contract (see Chapter 10).
8. Under the Uniform Commercial Code (UCC), only the agent is liable if the instrument neither names the principal nor shows that the agent signed in a representative capacity [UCC 3–402(b)(2)].
9. The agent is not liable on the contract, because the agent was never intended personally to be a party to the contract.

Actions by E-Agents

Although in the past standard agency principles applied only to *human* agents, today these same agency principles also apply to e-agents. An electronic agent, or **e-agent,** is a semiautonomous computer program that is capable of executing specific tasks. E-agents used in e-commerce include software that can search through many databases and retrieve only relevant information for the user.

The Uniform Electronic Transactions Act (UETA), which was discussed on pages 233 to 239 in Chapter 11, sets forth provisions relating to the principal's liability for the actions of e-agents. According to Section 15 of the UETA, e-agents can enter into binding agreements on behalf of their principals—at least, in those states that have adopted the act. Thus, if consumers place an order over the Internet, and the company (principal) takes the order via an e-agent, the company cannot later claim that it did not receive the order.

The UETA also stipulates that if an e-agent does not provide an opportunity to prevent errors at the time of the transaction, the other party to the transaction can avoid the transaction. Therefore, if an e-agent fails to provide an on-screen confirmation of a purchase or sale, the other party can avoid the effect of any errors. For example, Bigelow wants to purchase three copies of three different books (a total of nine items). The e-agent mistakenly records an order for thirty-three of a single book and does not provide an on-screen verification of the order. If thirty-three books are then sent to Bigelow, he can avoid the contract to purchase them.

SECTION 3

LIABILITY FOR TORTS AND CRIMES

Obviously, any person, including an agent, is liable for his or her own torts and crimes. Whether a principal can also be held liable for an agent's torts and crimes depends on several factors, which we examine here. In some situations, a principal may be held liable not only for the torts of an agent, but also for torts committed by an independent contractor.

Principal's Tortious Conduct

A principal who acts through an agent may be liable for harm resulting from the principal's own negligence or recklessness. Therefore, a principal may be liable if he or she gives improper instructions, authorizes the use of improper materials or tools, or establishes improper rules that result in the agent's committing a tort. For instance, Peter knows that Audrey's driver's license has been suspended but nevertheless tells her to use the company truck to deliver some equipment to a customer. If someone is injured as a result, Peter will be liable for his own negligence in instructing Audrey to drive without a valid license.

Principal's Authorization of Agent's Tortious Conduct

Similarly, a principal who authorizes an agent to commit a tort may be liable to persons or property injured thereby, because the act is considered to be the principal's. For example, Pagani directs his agent, Atkin, to cut the corn on specific acreage, which neither of them has the right to do. The harvest is therefore a trespass (a tort), and Pagani is liable to the owner of the corn.

Note that an agent acting at the principal's direction can be liable as a *tortfeasor* (one who commits a wrong, or tort), along with the principal, for committing the tortious act even if the agent was unaware that the act was wrong. Assume in the above example that Atkin, the agent, did not know that Pagani lacked the right to harvest the corn. Atkin can still be held liable to the owner of the field for damages, along with Pagani, the principal.

Liability for Agent's Misrepresentation

A principal is exposed to tort liability whenever a third person sustains a loss due to the agent's misrepresentation. The principal's liability depends on whether the agent was actually or apparently authorized to make representations and whether the representations were made within the scope of the agency. The principal is always directly responsible for an agent's misrepresentation made within the scope of the agent's authority.

Suppose that Ainsley is a demonstrator for Pavlovich's products. Pavlovich sends Ainsley to a home show to demonstrate the products and to answer questions from consumers. Pavlovich has given Ainsley authority to make statements about the products. If Ainsley makes only true representations, all is fine. But if he makes false claims, Pavlovich will be liable for any injuries or damages sustained by third parties in reliance on Ainsley's false representations.

APPARENT IMPLIED AUTHORITY When a principal has placed an agent in a position of apparent authority—making it possible for the agent to

defraud a third party—the principal may also be liable for the agent's fraudulent acts. For example, Joan Ableman is a loan officer at First Security Bank. In the ordinary course of her job, Ableman approves and services loans and has access to the credit records of all customers. Ableman falsely represents to a borrower, McMillan, that the bank feels insecure about McMillan's loan and intends to call it in unless McMillan provides additional collateral, such as stocks and bonds. McMillan gives Ableman numerous stock certificates, which Ableman keeps in her own possession and later uses as collateral to take out a personal loan. The bank is liable to McMillan for any losses sustained on the stocks even though the bank was unaware of the fraudulent scheme.

If, in contrast, Ableman had been a recently hired junior bank teller rather than a loan officer when she told McMillan that the bank required additional security for the loan, McMillan would not have been justified in relying on her representation. In that situation, the bank normally would not be liable to McMillan for any the losses sustained.

As will be discussed in Chapter 37, partners in a partnership generally have the apparent implied authority to act as agents on behalf of the firm. Thus, if one of the partners commits a tort or a crime, the partnership itself—and often the other partners personally—can be held liable for the loss.

CASE IN POINT Selheimer & Company, a securities broker-dealer that operated as a partnership, provided various financial services. The managing partner, Perry Selheimer, embezzled funds that clients had turned over to the firm for investment. After Selheimer was convicted, other partners in the firm claimed that they were not liable for losses resulting from his illegal activities. The court, however, held that Selheimer had apparent implied authority to act in the ordinary course of the partnership's business. Thus, the firm, as principal, was liable, and under the law of partnerships, the personal assets of the individual partners could be used to cover the firm's liability.[10]

INNOCENT MISREPRESENTATION Tort liability based on fraud requires proof that a material misstatement was made knowingly and with the intent to deceive. An agent's *innocent* mistakes occurring in a contract transaction or involving a warranty contained in the contract can provide grounds for the third party's rescission of the contract and the award of damages. Moreover, justice dictates that when a principal knows that an agent is not accurately advised of facts but does not correct either the agent's or the third party's impressions, the principal is directly responsible to the third party for resulting damages. The point is that the principal is always directly responsible for an agent's misrepresentation made within the scope of authority.

Liability for Agent's Negligence

Under the doctrine of ***respondeat superior,***[11] the principal-employer is liable for any harm caused to a third party by an agent-employee within the scope of employment. This doctrine imposes **vicarious liability,** or indirect liability, on the employer—that is, liability without regard to the personal fault of the employer for torts committed by an employee in the course or scope of employment.[12] Third parties injured through the negligence of an employee can sue either that employee or the employer, if the employee's negligent conduct occurred while the employee was acting within the scope of employment.

When an agent commits a negligent act, can the agent, as well as the principal, be held liable? That was the issue in the following case.

10. *In re Selheimer & Co.*, 319 Bankr. 395 (E.D.Pa. 2005).
11. Pronounced ree-*spahn*-dee-uht soo-*peer*-ee-your. The doctrine of *respondeat superior* applies not only to employer-employee relationships but also to other principal-agent relationships in which the principal has the right of control over the agent.
12. The theory of *respondeat superior* is similar to the theory of strict liability covered in Chapter 7.

EXTENDED CASE 33.3
Warner v. Southwest Desert Images, LLC

Court of Appeals of Arizona, 218 Ariz. 121, 180 P.3d 986 (2008).

IN THE LANGUAGE OF THE COURT

J. William *BRAMMER,* Jr., Judge.

* * * Southwest Desert Images, LLC (SDI) was hired by Warner's employer, Aegis Communications (Aegis), to perform landscaping and weed control. On September 29, 2003, SDI employee [David] Hoggatt began spraying an herbicide on weeds on the property around Aegis's building. * * * After approximately an hour and a half of spraying, Hoggatt was informed that people inside Aegis's building were complaining. The herbicide spray had entered the building through its air conditioning system and had circulated throughout