Agent's Personal Liability for Torts and Contracts

by Sophia

WHAT'S COVERED

In this lesson, you will learn about situations in which the agent can incur personal liability. Specifically, this lesson will cover:

1. Tort Liability

That a principal is held vicariously liable and must pay damages to an injured third person does not excuse the agent who actually committed the tortious acts. A person is always liable for his or her own torts (unless the person is insane, involuntarily intoxicated, or acting under extreme duress).

The agent is personally liable for his wrongful acts and must reimburse the principal for any damages the principal was forced to pay, as long as the principal did not authorize the wrongful conduct. The agent directed to commit a tort remains liable for his own conduct, but is not obliged to repay the principal.

Liability as an agent can be burdensome, sometimes perhaps more burdensome than as a principal. The latter normally purchases insurance to cover against wrongful acts of agents, but liability insurance policies frequently do not cover the employee's personal liability if the employee is named in a lawsuit individually.

> ↱ EXAMPLE Doctors' and hospitals' malpractice policies protect a doctor from both her own mistakes and those of nurses and others that the doctor would be responsible for; nurses, however, might need their own coverage.

In the absence of insurance, an agent is at serious risk in this lawsuit-conscious age. The risk is not total. The agent is not liable for torts of other agents unless he is personally at fault, such as by negligently supervising a minor or by giving faulty instructions.

> ↱ EXAMPLE An agent, the general manager for a principal, hires Brown as a subordinate. Brown is competent to do the job, but by failing to exercise proper control over a machine, negligently injures Ted, a visitor to the premises. The principal and Brown are liable to Ted, but the agent is not.

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2. Contract Liability

It makes sense that an agent should be liable for her own torts; it would be a bad social policy indeed if a

person could escape tort liability based on her own fault merely because she acted in an agency capacity.

It also makes sense that - as is the general rule - an agent is not liable on contracts she makes on the principal's behalf; the agent is not a party to a contract made by the agent on behalf of the principal.

No public policy would be served by imposing liability, and in many cases, it would not be reasonable.

> ↗ EXAMPLE Suppose an agent contracts to buy $25 million of rolled aluminum for a principal, an airplane manufacturer. The agent personally could not reasonably perform such a contract, and it is not intended by the parties that she should be liable.

DID YOU KNOW

The rule is different in England, where an agent residing outside the country is liable even if it is clear that he is signing in an agency capacity.

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3. Exceptions to Contract Liability

There are three exceptions to this rule:

- If the agent is undisclosed or partially disclosed
- If the agent lacks authority or exceeds it
- If the agent entered into the contract in a personal capacity

3a. Agent for Undisclosed or Partially Disclosed Principal

An agent need not, and frequently will not, inform the person with whom he is negotiating that he is acting on behalf of a principal. The secret principal is usually called an **undisclosed principal**.

Or the agent may tell the other person that he is acting as an agent but not disclose the principal's name, in which event the principal is referred to as a **partially disclosed principle**.

IN CONTEXT

To understand the difficulties that may occur, consider the following hypothetical but common example.

A real estate developer known for building amusement parks wants to acquire several parcels of land to construct a new park. He wants to keep his identity secret to hold down the land cost. If the landowners realized that a major building project was about to be launched, their asking price would be quite high. So the developer obtains two options to purchase land by using two secret agents—Betty and Clem.

Betty does not mention to sellers that she is an agent; therefore, to those sellers, the developer is an undisclosed principal and Betty is an **undisclosed agent**. Clem tells those with whom he is dealing that he is an agent, but refuses to divulge the developer's name or his business interest in the land. Thus the developer is, to the latter sellers, a partially disclosed principal. Suppose the sellers get

wind of the impending construction and want to back out of the deal. Who may enforce the contracts against them?

The developer and the agents may sue to compel transfer of title. The undisclosed or partially disclosed principal may act to enforce his rights unless the contract specifically prohibits it or there is a representation that the signatories are not signing for an undisclosed principal. The agents may also bring suit to enforce the principal's contract rights because, as agents for an undisclosed or partially disclosed principal, they are considered parties to their contracts.

Now suppose the developer attempts to call off the deal. Whom may the sellers sue? Both the developer and the agents are liable. That the sellers had no knowledge of the developer's identity - or even that there was a developer - does not invalidate the contract. If the sellers first sue agent Betty (or Clem), they may still recover the purchase price from the developer as long as they had no knowledge of his identity prior to winning the first lawsuit.

The developer is discharged from liability if, knowing his identity, the plaintiffs persist in a suit against the agents and recover a judgment against them anyway. Similarly, if the seller sues the principal and recovers a judgment, the agents are relieved of liability. The seller thus has a "right of election" to sue either the agent or the undisclosed principal, a right that in many states may be exercised any time before the seller collects on the judgment.

TERMS TO KNOW

Undisclosed Principal

A principal unknown to a third party at the time that a transaction is conducted by the principal through an agent.

Partially Disclosed Principal

A principal whose identity is not disclosed, but whose existence is disclosed by the agent to a third party.

Undisclosed Agent

An agent who deals with a third party without disclosing that he or she is an agent.

3b. Lack of Authority in Agent

An agent who purports to make a contract on behalf of a principal, but who in fact has no authority to do so, is liable to the other party. The theory is that the agent has warranted to the third party that he has the requisite authority.

The principal is not liable in the absence of apparent authority or ratification, but the agent does not warrant that the principal has capacity.

↱ EXAMPLE An agent for a minor is not liable on a contract that the minor later disavows, unless the agent expressly warranted that the principal had attained his majority.

In short, the implied warranty is that the agent has authority to make a deal, not that the principal will necessarily comply with the contract once the deal is made.

3c. Agent Acting on Own Account

An agent will be liable on contracts made in a personal capacity, such as when the agent personally guarantees repayment of a debt. The agent's intention to be personally liable is often difficult to determine on the basis of his signature on a contract.

Generally, a person signing a contract can avoid personal liability only by showing that he was in fact signing as an agent.

> ↗ EXAMPLE If the contract is signed "Jones, Agent," Jones can introduce evidence to show that there was never an intention to hold him personally liable. But if he signed "Jones" and neither his agency nor the principal's name is included, he will be personally liable.

This can be troublesome to agents who routinely indorse checks and notes. There are special rules governing these situations.

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4. Termination of Agency by Act of the Parties

The agency relationship is not permanent, and the parties to an agency contract can certainly terminate the agreement. As with the creation of the relationship, the agreement may be terminated either expressly or impliedly.

4a. Express Termination

Many agreements contain specified circumstances whose occurrence signals the end of the agency. The most obvious of these circumstances is the expiration of a fixed period of time ("agency to terminate at the end of three months" or "on midnight, December 31").

An agreement may also terminate on the accomplishment of a specified act ("on the sale of the house") or following a specific event ("at the conclusion of the last horse race").

Mutual consent between the parties will end the agency. Moreover, the principal may revoke the agency or the agent may renounce it; such a revocation or renunciation of agency would be an express termination. Even a contract that states the agreement is irrevocable will not be binding, although it can be the basis for a damage suit against the one who breached the agreement by revoking or renouncing it.

As with any contract, a person has the power to breach, even in absence of the right to do so. If the agency is coupled with an interest, however, so that the authority to act is given to secure an interest that the agent has in the subject matter of the agency, then the principal lacks the power to revoke the agreement.

4b. Implied Termination

There are a number of other circumstances that will spell the end of the relationship by implication. Unspecified events or changes in business conditions or the value of the subject matter of the agency might lead to a reasonable inference that the agency should be terminated or suspended.

> ↗ EXAMPLE The principal desires the agent to buy silver, but the silver market unexpectedly rises and silver doubles in price overnight.

Other circumstances that end the agency include disloyalty of the agent (e.g., he accepts an appointment that is adverse to his first principal or embezzles from the principal), bankruptcy of the agent or of the principal, the outbreak of war (if it is reasonable to infer that the principal, knowing of the war, would not want the agent to continue to exercise authority), and a change in the law that makes a continued carrying out of the task illegal or seriously interferes with it.

5. Termination of Agency by Operation of Law

Aside from the express termination (by agreement of both or upon the insistence of one), or the necessary or reasonable inferences that can be drawn from their agreements, the law voids agencies under certain circumstances.

The most frequent termination by **operation of law** is the death of a principal or an agent. The death of an agent also terminates the authority of subagents he has appointed, unless the principal has expressly consented to the continuing validity of their appointment. Similarly, if the agent or principal loses capacity to enter into an agency relationship, it is suspended or terminated. The agency terminates if its purpose becomes illegal.

Even though authority has terminated, whether by action of the parties or operation of law, the principal may still be subject to liability. Apparent authority in many instances will still exist; this is called lingering authority. It is imperative for a principal on termination of authority to notify all those who may still be in a position to deal with the agent.

The only exceptions to this requirement are when termination is effected by death, loss of the principal's capacity, or an event that would make it impossible to carry out the object of the agency.

TERM TO KNOW

Operation of Law

The manner in which something happens without intentional actions by parties to a transaction, but occurs as the result of application of law.

SUMMARY

In this lesson, you learned that agents hold **tort liability** for their own actions. An agent does not generally hold **contract liability**. However, there are **exceptions** to this general rule of contract liability, such as if the **agent is for an undisclosed or partially disclosed principal**, if the agent **lacks authority** or exceeds it, or if the **agent acted on his or her own account** by entering into the contract in a personal capacity.

Parties to an agency contract can terminate the agency expressly or impliedly, or it can terminate by operation of law. An agency **terminates expressly** by the terms of the agreement or by mutual consent. It **terminates impliedly** by any number of circumstances in which it is reasonable to assume one or both of the parties would not want the relationship to continue. An agency will **terminate by operation of law** when a party dies or becomes incompetent, or if the object of the agency becomes illegal. However, an agent may have apparent lingering authority, so the principal should notify those who might deal with the agent when the relationship is severed.

Best of luck in your learning!

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