

Duties between Agent and Principal

by Sophia



WHAT'S COVERED

In this lesson, you will learn about the responsibilities that exist between an agent and a principal according to agency law. Specifically, this lesson will cover:

1. Agent's Fiduciary Duty

The agent owes the principal duties in two categories: the **fiduciary** duty and a set of general duties imposed by agency law. However, these general duties are not unique to agency law; they are duties owed by any employee to the employer.

But the agency relationship is more than a contractual one, and the agent's responsibilities go beyond the border of the contract. Agency imposes a higher duty than simply abiding by the contract terms— it imposes a fiduciary duty. The law infiltrates the contract creating the agency relationship and reverses the general principle that the parties are free to act in the absence of agreement.

As a fiduciary of the principal, the agent stands in a position of special trust. His responsibility is to subordinate his self-interest to that of his principal, meaning that he has absolute loyalty to the interests of the principal.

The fiduciary responsibility is imposed by law. The absence of any clause in the contract detailing the agent's fiduciary duty does not relieve him of it. The duty contains several aspects.



TERM TO KNOW

Fiduciary

An individual who is given a high degree of authority and of whom is demanded a very high level of loyalty and trust. Examples include officers and directors of corporations, bank officers who handle money that is not their own, and trustees of funded organizations.

1a. Duty to Avoid Self-Dealing

A fiduciary may not lawfully profit from a conflict between his personal interest in a transaction and his principal's interest in that same transaction. When this occurs, it is known as **self-dealing**.

➞ **EXAMPLE** A broker hired as a purchasing agent may not sell to his principal through a company in which he or his family has a financial interest.

The penalty for breach of fiduciary duty is loss of compensation and profit and possible damages for breach of trust.



Self-Dealing

In business, a departure from a duty of loyalty to another in favor of oneself. For example, an officer of a corporation who is a fiduciary with a duty of loyalty to the corporation would be guilty of self-dealing if he or she set up a side business that competed with the corporation.

1b. Duty to Preserve Confidential Information

To further his objectives, a principal will usually need to reveal a number of secrets to his agent— how much he is willing to sell or pay for property, marketing strategies, and the like. Such information could easily be turned to the disadvantage of the principal if the agent were to compete with the principal or were to sell the information to those who do.

The law therefore prohibits an agent from using for his own purposes or in ways that would injure the interests of the principal, information confidentially given or acquired. This prohibition extends to information gleaned from the principal though unrelated to the agent's assignment, per the Restatement (Third) of Agency, Section 1.01, Comment e:

"Unless the principal consents...an agent may not use the principal's property, the agent's position, or nonpublic information the agent acquires while acting within the scope of the relationship, for the agent's own purposes or for the benefit of another."

Nor may the agent use confidential information after resigning his agency. Though he is free, in the absence of contract, to compete with his former principal, he may not use information learned in the course of his agency, such as trade secrets and customer lists.

2. Agent's General Duties

In addition to fiduciary responsibility (and whatever special duties may be contained in the specific contract), the law of agency imposes other duties on an agent.

These duties are not necessarily unique to agents; a non-fiduciary employee could also be bound to these duties on the right facts.

2a. Duty of Skill and Care

An agent is usually taken on because he has special knowledge or skills that the principal wishes to tap.

The agent is under a legal duty to perform his work with the care and skill that is standard in the locality for the kind of work which he is employed to perform and to exercise any special skills, if these are greater or more refined than those prevalent among those normally employed in the community.

2b. Duty of Good Conduct

In the absence of an agreement, a principal may not ordinarily dictate how an agent must live his private life.

➞ **EXAMPLE** An overly fastidious florist may not instruct her truck driver to steer clear of the local bar on his way home from delivering flowers at the end of the day.

But there are some jobs on which the personal habits of an employee may have an effect. The employee is

not at liberty to act with impropriety or notoriety, so as to bring disrepute on the business in which the principal is engaged.

➞ **EXAMPLE** A lecturer at an alcohol treatment center may be directed to refrain from frequenting bars. A bank cashier who becomes known as a gambler may be fired.

2c. Duty to Keep and Render Accounts

The agent must keep accurate financial records, take receipts, and otherwise act in conformity to standard business practices.

2d. Duty to Act Only as Authorized

This duty states a truism, but is one for which there are limits. A principal's wishes may have been stated ambiguously or may be broad enough to confer discretion on the agent.

As long as the agent acts reasonably under the circumstances, he will not be liable for damages later if the principal ultimately repudiates what the agent has done, per the Restatement (Third) of Agency, Section 1.01, Comment e:

"An agent's fiduciary position requires the agent to interpret the principal's statement of authority, as well as any interim instructions by the principal, in a reasonable manner to further purposes of the principal that the agent knows or should know...."

2e. Duty Not to Attempt the Impossible or Impracticable

If the principal says to the agent, "Keep working until the job is done," the agent is not obligated to go without food or sleep because the principal misjudged how long it would take to complete the job.

Nor should the agent continue to expend the principal's funds in an impractical attempt to gain business, sign up customers, or produce inventory when it is reasonably clear that such efforts would be in vain.

2f. Duty to Obey

As a general rule, the agent must obey reasonable directions concerning the manner of performance. What is reasonable depends on the customs of the industry or trade, prior dealings between agent and principal, and the nature of the agreement creating the agency.

➞ **EXAMPLE** A principal may prescribe uniforms for various classes of employees, and a manufacturing company may tell its sales force what sales pitch to use on customers.

On the other hand, certain tasks entrusted to agents are not subject to the principal's control.

➞ **EXAMPLE** A lawyer may refuse to permit a client to dictate courtroom tactics.

2g. Duty to Give Information

Because the principal cannot be every place at once - that is why agents are hired, after all - much that is vital to the principal's business first comes to the attention of agents. If the agent has actual notice or reason to know of information that is relevant to matters entrusted to him, he has a duty to inform the principal.

This duty is especially critical because information in the hands of an agent is, under most circumstances, imputed to the principal, whose legal liabilities to third persons may hinge on receiving information in a timely fashion.

➔ **EXAMPLE** Service of process requires a defendant to answer within a certain number of days; an agent's failure to communicate to the principal that a summons has been served may bar the principal's right to defend a lawsuit.

The imputation to the principal of knowledge possessed by the agent is strict: Even where the agent is acting adversely to the principal's interests, such as by trying to defraud his employer, a third party may still rely on notification to the agent, unless the third party knows the agent is acting adversely.

2h. Shop Rights Doctrine

To understand this duty, consider the following case.

CASE STUDY: *Grip Nut Co. v. Sharp*

In this case, Sharp made a deal with Grip Nut Company that in return for a salary and bonuses as company president, he would assign to the company any inventions he made. When the five-year employment contract expired, Sharp continued to serve as chief executive officer, but no new contract was negotiated concerning either pay or rights to inventions. During the next ten years, Sharp invented a number of new products and developed new machinery to manufacture them; patent rights went to the company. However, he made one invention with two other employees and they assigned the patent to him. A third employee invented a safety device and also assigned the patent to Sharp. At one time, Sharp's son invented a leakproof bolt and a process to manufacture it; these, too, were assigned to Sharp. These inventions were developed in the company's plants at its expense.

When Sharp died, his family claimed the rights to the inventions on which Sharp held assignments and sued the company, which used the inventions, for patent infringement. The family reasoned that after the expiration of the employment contract, Sharp was employed only in a managerial capacity, not as an inventor. The court disagreed and invoked the **shop rights doctrine**, under which an invention "developed and perfected in [a] plant with its time, materials, and appliances, and wholly at its expense" may be used by the company without payment of royalties: "Because the servant uses his master's time, facilities and materials to attain a concrete result, the employer is entitled to use that which embodies his own property and to duplicate it as often as he may find occasion to employ similar appliances in his business." The company would have been given complete ownership of the patents had there been an express or implied (e.g., the employee is hired to make inventions) contract to this effect between Sharp and the company.

Grip Nut Co. v. Sharp, 150 F.2d 192 (7th Cir. 1945).



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The right of an employer to the invention of its employee created during the term of the employment using employer's materials, equipment, etc.

3. Principal's Duties

The principal owes the agent duties in contract, tort, and - statutorily - workers' compensation law.

The fiduciary relationship of agent to principal does not run in reverse— that is, the principal is not the agent's fiduciary. Nevertheless, the principal has a number of contractually related obligations toward his agent.

3a. General Contract Duties

In general, the principal has the right to control the agent's actions even where the principal has agreed not to interfere with the agent's work, although if this breaches the agency contract, the agent may have remedies available for the breach, per the Restatement (Third) of Agency, Section 1.01, Comment f, 1. The principal is allowed, however, to compete with the agent unless the agreement specifically prohibits it.

The principal has a duty to inform his agent of risks of physical harm or pecuniary loss that inhere in the agent's performance of assigned tasks.

➞ **EXAMPLE** Failure to warn an agent that travel in a particular neighborhood required by the job may be dangerous (a fact unknown to the agent but known to the principal) could under common law subject the principal to a suit for damages if the agent is injured while in the neighborhood performing her job.

A principal is obliged to render accounts of monies due to agents; a principal's obligation to do so depends on a variety of factors, including the degree of independence of the agent, the method of compensation, and the customs of the particular business.

An agent's reputation is no less valuable than a principal's, and an agent is under no obligation to continue working for one who sullies it.



SUMMARY

In this lesson, you learned that an agent owes a principal two categories of duties: fiduciary and general. The **agent's fiduciary duty** is the duty to act always in the interest of the principal; this includes the **duty to avoid self-dealing** and **to preserve confidential information**. The **agent's general duties** encompass the sorts of obligations any employee might have: the **duty of skill and care, of good conduct, to keep and render accounts, to act only as authorized, to not attempt the impossible or impracticable, to obey, and to give information**. The **shop rights doctrine** provides that inventions made by an employee using the employer's resources and on the employer's time belong to the employer.

You also learned that the principal owes the agent duties, although not fiduciary ones. The **principal's duties** may be categorized as contract and tort duties. **General contract duties** are to warn the agent of hazards associated with the job, to avoid interfering with the agent's performance of his job, and to render accounts of money due the agent.

Best of luck in your learning!

Source: THIS TUTORIAL HAS BEEN ADAPTED FROM (1) "BUSINESS LAW AND THE LEGAL ENVIRONMENT" VERSION 1.0 BY DON MAYER, DANIEL WARNER, GEORGE SIEDEL, AND JETHRO K. LIEBERMAN.



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