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Relations between principal and third party

- Contractual liability
- Tortious liability

INTRODUCTION

As noted in Chapter 3, the primary purpose of many agency agreements is to create a contractual relationship between the principal and third party. However, whether such a relationship actually comes into existence can depend on a number of factors. Problems may arise in the agency relationship, or the agent may act in an unauthorized manner. It may even be the case that the third party believes the agent to be the principal. Where issues arise, it is important to be able to determine the legal nature of the relationship between the principal and third party.

Accordingly, this chapter examines the relationship that exists between principal and third party and focuses, in particular, on the liability that exists between principal and third party and those instances when they can sue, and be sued by, the other. Liability principally arises in contract and tort (as Figure 7.1 indicates), and so these two areas of liability will be discussed, beginning with the contractual liability of the principal and third party.

Contractual liability

The contractual relationship between the principal and third party, and the extent to which one party can be liable to the other, can be complex and

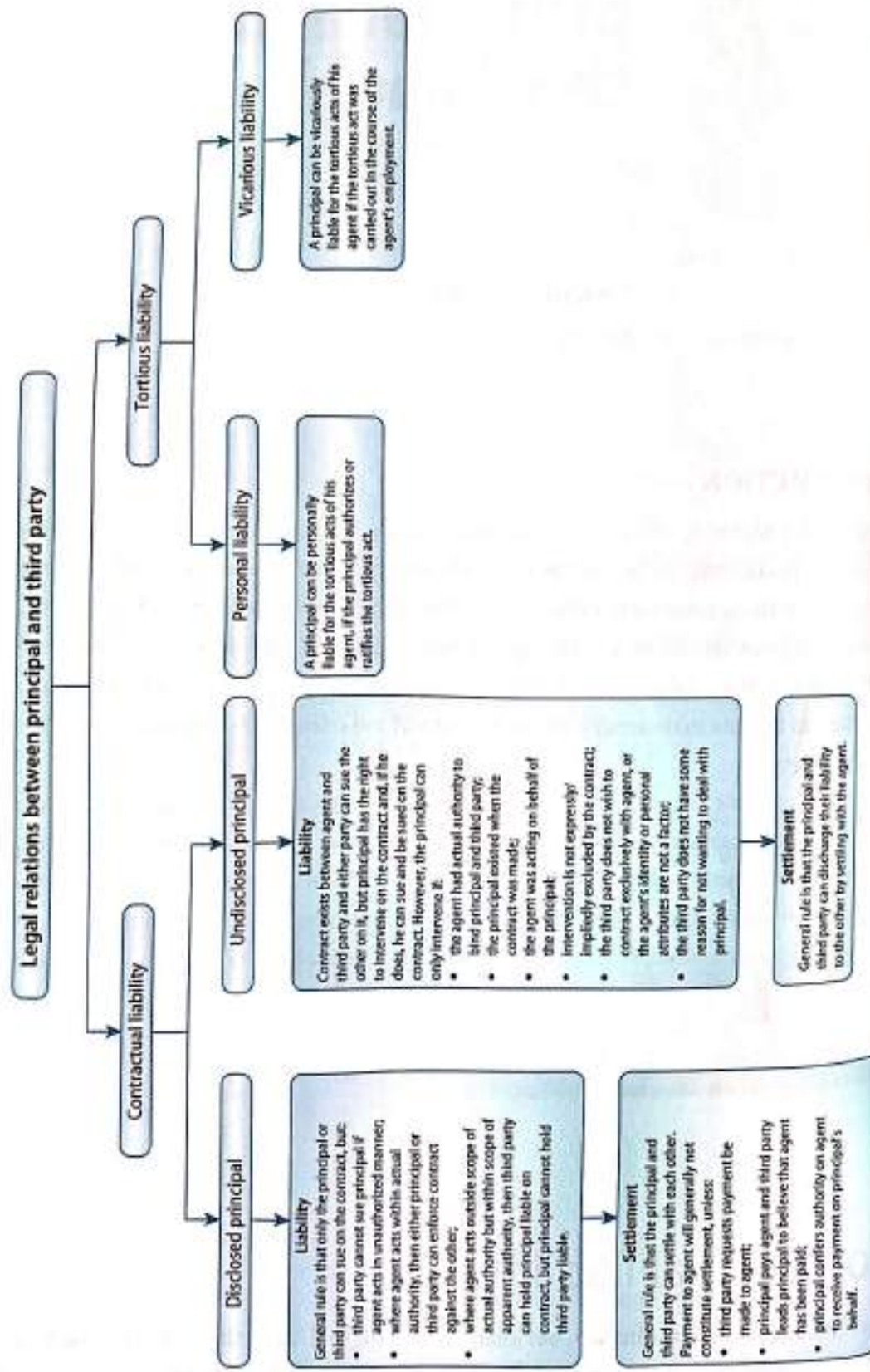



FIGURE 1.3 Legal relations between principal and third party

depends upon a number of variables, notably whether the principal is disclosed or undisclosed.

 The distinction between a disclosed and undisclosed principal is discussed at p 55

Disclosed principal

It will be remembered that, in a typical agency relationship, an agent will effect a contract between his principal and a third party, after which the agent will 'drop out' of the transaction. From this it follows that the general rule is that, where an agent makes a contract on behalf of a disclosed principal (named or unnamed), then the contract is between the principal and third party only, and either party can sue and be sued on it.

However, the ability of the principal and third party to sue on the contract will depend largely upon whether or not the agent has acted within the scope of his authority:

- Where the agent acts without authority, then the third party cannot sue the principal (or vice versa),¹ unless the principal ratifies the agent's unauthorized act.
- Where the agent acts within the scope of his actual authority (express or implied), then if either the principal or third party breaches the contract, the innocent party can sue the party in breach.²
- Where the agent acts outside the scope of his actual authority, but within the scope of his apparent authority, then the third party can hold the principal liable on the contract, but the principal cannot sue the third party on the contract unless he first ratifies the agent's actions.³ If, however, the third party knew that the agent lacked actual authority, then the principal will be able to rescind the contract, as the following case demonstrates.



Jordan v Norton (1838) 4 M&W 155

FACTS: Norton (the principal) wrote to Jordan (the third party) and agreed to purchase a horse. In a subsequent letter, Norton stated that his son (the agent) would collect the horse from Jordan, but only if Jordan provided a warranty stating that the horse was 'sound and quiet in harness'. The son collected the horse, but received no warranty from Jordan. Two days later, Norton returned the horse on the ground that it was unsound. Jordan sued for payment.

HELD: The claim failed. Jordan knew that the son was not authorized to collect the horse without the required warranty, and so Norton was entitled to repudiate the contract and return the horse to Jordan.

1. See e.g. *Comerford v Britannic Assurance Co Ltd* (1908) 24 TLR 593 (KB).


2. See e.g. *Camillo Tank Steamship Co Ltd v Alexandria Engineering Works* (1921) 38 TLR 134 (HL).

3. Peter G Watts, *Bowstead & Reynolds on Agency* (20th edn, Sweet & Maxwell 2014) [8-029].

In relation to deeds and negotiable instruments, the general rule does not apply and a disclosed principal will not be privy to a contract with a third party unless certain formalities are complied with:

- A principal cannot sue or be sued on a negotiable instrument (e.g. a bill of exchange or a cheque), unless he has signed it,⁴ or he has authorized another person to sign it and that person has signed it.⁵
- A principal cannot generally sue or be sued on a deed *inter partes* unless the deed describes him as being a party to it and it is executed in his name.⁶ There are, however, exceptions to this rule (e.g. if the agent executing the deed does so as a trustee of the principal, then the principal can sue and be sued on the deed).⁷

It used to be the case that where an agent acted on behalf of a foreign principal, then it would be presumed that the agent did not have the right to establish privity of contract between the principal and the third party, but this presumption was eventually abandoned.

 This presumption and the reasons behind its abolition are discussed at p 166

Settlement with the agent

Consider the following example:

Eg

COMCORP LTD

ComCorp Ltd (the principal) instructs Ben (the agent) to purchase a piece of machinery from Heavy Plant Ltd (the third party) for £5,000. Ben enters into a contract of sale with Heavy Plant on ComCorp's behalf and the machinery is delivered to ComCorp. ComCorp believes that Ben has already paid for the machinery, so it pays Ben £5,000 plus his commission. In fact, Ben has not paid Heavy Plant Ltd and he is subsequently declared bankrupt. Heavy Plant invoices ComCorp for payment, but ComCorp states that it is not liable to pay as it has already provided the payment to Ben. Heavy Plant commences proceedings against ComCorp.

Is ComCorp liable to Heavy Plant or has ComCorp's payment to Ben settled the debt it owes to Heavy Plant? In many cases, it is possible for liability to be avoided if the parties reach a settlement. In the tri-partite agency relationship between principal, agent, and third party, it is important to determine who has the right to settle. Where the principal is disclosed, a binding contract will usually be created between the principal and the third party, to which the agent is not a party. From this, it follows that generally the principal can only be discharged from his obligation under the contract if he reaches a settlement with the third party, or vice versa. Consequently, a payment to the agent by the principal will not discharge the liability of the principal to the third party,⁸ so, in the example given, ComCorp will likely be liable to Heavy Plant for the cost of the machinery. This general rule is, however, subject to a number of exceptions:

- A principal can discharge his obligations to a third party if the third party requests that payment be made to the agent and such payment is made.⁹

4. Bills of Exchange Act 1882, s 23. In the case of a company, the corporate seal will act as a signature.

5. *ibid* s 91(1).

6. *Re International Contract Co, Pickering's Claim* (1871) 6 Ch App 525.

7. *Harmer v Armstrong* [1934] Ch 65 (CA).

8. *Irvine & Co v Watson & Sons* (1879–80) LR 5 QBD 414 (CA).

9. *Smyth v Anderson* (1949) 7 CB 21.

- Where the principal has paid the agent and the third party leads the principal to believe that the agent has paid, then the principal's obligations to the third party will be discharged.¹⁰
- If the principal has conferred authority on the agent to receive payment on the principal's behalf, then the third party's liability to the principal will be discharged if he provides payment to the agent,¹¹ providing that the agent is authorized to receive payment in the form provided.¹²

Undisclosed principal

Consider the following example:

Eg

COMCORP LTD

ComCorp (the principal) wishes to export goods overseas. It engages Jessica (the agent) to locate a suitable vessel and to charter it on ComCorp's behalf. She locates a vessel belonging to ShipHire Ltd (the third party), and charters it in her own name. At no point does she inform ShipHire that she is working on behalf of ComCorp. The chartermarket improves and ShipHire realizes that it could hire the ship to someone else for a higher rate. Accordingly, ShipHire contacts Jessica and tells her that it is cancelling the charterparty.

The question that arises is whether ComCorp can hold ShipHire liable on the charterparty. It could be argued that it would be most unfair to allow an undisclosed principal to hold a third party liable on a contract, as the third party will not know of the principal's existence; but in general, the law states that an undisclosed principal can sue and be sued on a contract made by his agent with a third party. What actually happens is that the law regards the contract as being between the agent and the third party,¹³ but grants the principal the right to intervene and sue, and be sued, by the third party. This rule is extremely controversial, with Stone noting:

The concept of the undisclosed principal clearly runs counter to the general contractual rule as to the necessity for privity of contract. The third party can find that they have rights against, and liabilities towards, a person with whom there was no intention to contract, and of whom the third party was in ignorance.¹⁴

Pollock notes that such a rule is rare amongst legal systems, stating that '[t]he right of one person to sue another on a contract not really made with the person suing is unknown to every other legal system except that of England and America'.¹⁵ Given the controversy, what is the justification for allowing an undisclosed principal to enforce

10. *Horsfall v Fautleroy* (1830) 10 B&C 755.

11. *Butwick v Grant* [1924] 2 KB 483 (KB) 489–90 (Sankey J). If the agent is not authorized to receive payment on behalf of the principal, but receives such payment and passes it on to the principal, then the agent's actions will be deemed to be ratified and the third party's liability to the principal will be discharged.

12. *Hine Bras v Steamship Insurance Syndicate Ltd* (1895) 72 LT 79 (payment to agent by bill of exchange did not discharge third party's liability where agent was only authorized to accept payment in cash).

13. *Sims v Bond* (1833) 5 B&A 389. The ability of the agent to sue, and be sued, when acting on behalf of an undisclosed principal is discussed on p 161.

14. Richard Stone, *Law of Agency* (Cavendish 1996) 94.

15. Sir Frederick Pollock (1887) 3 LQR 358, 359.

the contract? Numerous theories have been advanced by academics, the majority of which have been rejected by the courts. It has been argued that the undisclosed principal acquires the right to sue on the contract because the contract between the agent and third party is automatically assigned to the principal,¹⁶ but the Privy Council has emphatically rejected this theory.¹⁷ Diplock LJ stated, *obiter*, that:

it matters not whether [the agent] discloses to the other party the identity of his principal, or even if he is contracting on behalf of a principal at all, if the other party is willing or leads the agent to believe that he is willing to treat as a party to the contract anyone on whose behalf the agent may have been authorised to contract.¹⁸

One commentator has used this *dictum* to contend that when a third party contracts with an agent, he is implicitly agreeing to contract with the agent and the agent's principal, should there be one.¹⁹ However, it could be argued that the mere possibility that a principal might exist is not a sufficiently strong ground for implying a contract between the undisclosed principal and the third party. Munday²⁰ contends that, ultimately, the rule may simply be one of commercial convenience, citing the following passage of Lord Lindley:

The explanation of the doctrine that an undisclosed principal can sue and be sued on a contract made in the name of another person with his authority is, that the contract is in truth, although not in form, that of the undisclosed principal himself. Both the principal and the authority exist when the contract is made; and the person who makes it for him is only the instrument by which the principal acts. In allowing him to sue and be sued upon it, effect is given, so far as he is concerned, to what is true in fact, although that truth may not have been known to the other contracting party.²¹

Intervention of the principal

Irrespective of the justification (or lack thereof) behind the rule, it has been upheld and applied numerous times by the courts, and so the task is now to discuss the application of the rule. As noted, where an agent contracts with a third party on behalf of an undisclosed principal, a contract will exist between the agent and third party. The principal can intervene on this contract and consequently sue, and be sued by, the third party. The courts have recognized that the principal's intervention can cause unfairness to the third party, and so the principal's ability to intervene is subject to a number of limitations. The position has been neatly summarized by Lord Lloyd, who established five points, namely:

(1) An undisclosed principal may sue and be sued on a contract made by an agent on his behalf, acting within the scope of his actual authority. (2) In entering into the contract, the agent must intend to act on the principal's behalf. (3) The agent of an undisclosed principal may also sue and be sued on the contract. (4) Any defence which the third party may have against the agent is available against his principal. (5) The terms of the contract may, expressly or by implication, exclude the principal's right to sue, and his liability to be sued. The contract itself, or the circumstances surrounding the contract, may show that the agent is the true and only principal.²²

16. Al. Goodhart and C.J. Hamson, 'Undisclosed Principals in Contract' (1932) 4 CLJ 320.

17. *Siu Yin Kwan v Eastern Insurance Co Ltd* [1994] 2 AC 199 (PC) 210 (Lord Lloyd).

18. *Teheran-Europe Co Ltd v ST Belton (Tractors) Ltd* [1968] 2 QB 545 (CA) 555.

19. Tan Cheng-Han, 'Undisclosed Principals and Contract' (2004) 120 LQR 480, 502.

20. Roderick Munday, *Agency: Law and Principles* (2nd edn, OUP 2013) 250.

21. *Keighley, Maxsted & Co v Durant* [1901] AC 240 (HL) 261.

22. *Siu Yin Kwan v Eastern Insurance Co Ltd* [1994] 2 AC 199 (PC) 207.

Each of these limitations will now be discussed, along with several limitations that have been subsequently established. First, the principal can only intervene if the agent had actual authority to bind the principal to the third party.²³ Ratification of the agent's unauthorized acts will not subsequently permit the principal to intervene, because an undisclosed principal is incapable of ratifying the unauthorized actions of his agent. Second, the principal can only intervene if it existed at the time it was entered into—clearly, this requirement is primarily aimed at bodies corporate (such as companies and limited liability partnerships). Third, the principal can only intervene if the agent was acting on behalf of the undisclosed principal—this will be determined subjectively. Accordingly, if the agent was acting to benefit himself and not his principal, then the principal cannot intervene or be sued by the third party.²⁴ Fourth, a principal will not be permitted to intervene where such intervention is expressly excluded by the terms of the contract. This exclusion may be obvious (e.g. where the contract expressly states that the agent is the only party to it),²⁵ or it may be deduced from the facts, as in the following case.



***UK Mutual Steamship Assurance Association Ltd v Nevill*
(1887) 19 QBD 110 (CA)**

FACTS: Tully (the agent) was the manager and part-owner of a ship. He became a member of the UK Mutual Steamship Assurance Association (the third party) and took out an insurance policy under the Association's rules. The Association's articles of association gave it the power to require that members pay contributions, and Tully owed such contributions. Tully was declared bankrupt, and so the Association sought to recover the contributions from Nevill, another part-owner of the ship. The Association alleged that Nevill was an undisclosed principal and so could be liable. Nevill denied liability on the ground that he was not a member of the Association.

HELD: The Association's claim failed. It was a term of the articles of association that only members were liable to pay contributions and, as Nevill was not a member, making him liable to the Association would be inconsistent with the express terms of the articles.

Fifth, a principal will not be liable where, by implication, the contract excludes the intervention of the principal. The following case provides an example of such an exclusion.



***Humble v Hunter* (1848) 12 QB 310**

FACTS: Mrs Humble (the purported principal) owned a ship called *The Ann*. Her son, CJ Humble (the purported agent), chartered the ship to Hunter (the third party). The son signed the charterparty 'CJ Humble Esq, owner of the good ship or vessel called the Ann'. Mrs Humble sought to take over the contract from her son as an undisclosed principal.

HELD: She was not permitted to intervene and the court held that she was not in fact the principal. The description of the son as the 'owner' of the ship indicated that he was in fact the principal, which excluded the possibility of her intervening as principal.

23. *Keighley, Maxsted & Co v Durant* [1901] AC 240 (HL).

24. *Rolls-Royce Power Engineering plc v Ricardo Consulting Engineers Ltd* [2003] EWHC 2871 (TCC), [2004] 2 All ER (Comm) 129.

25. *JH Rayner (Mincing Lane) Ltd v Department of Trade and Industry* [1990] 2 AC 418 (HL).

However, in the following case, the effects of *Humble* were noticeably restricted, with Scott LJ in *Epps v Rothnie* contending that *Humble* 'can no longer be regarded as good law'.²⁶



Fred Drughorn Ltd v Rederiaktiebolaget Transatlantic **[1919] AC 203 (HL)**

FACTS: Fred Drughorn Ltd ('FD', the third party) chartered a steamship to Lundgren (the purported agent), with the charterparty describing Lundgren as the 'charterer'. It transpired that Lundgren had in fact chartered the ship on behalf of Rederiaktiebolaget Transatlantic ('RT', the undisclosed principal), but FD did not know this. FD withdrew the services of the ship from Lundgren, on the ground that Lundgren had performed voyages not permitted under the charterparty. Lundgren commenced proceedings against FD, but before the case reached trial, Lundgren died. RT sought to intervene and substitute itself as claimant, on the ground that Lundgren was acting as its agent. The issue the House had to determine was whether evidence indicating that Lundgren was acting on behalf of RT was admissible.

HELD: The House held that the evidence indicating that Lundgren was acting on behalf of RT was admissible. In comparing *Humble* to the present case, Viscount Haldane stated that:

the term 'charterer' is a very different term from the term 'owner' or the term 'proprietor.' A charterer may be and prima facie is merely entering into a contract. A charterparty is not a lease—it is a chattel that is being dealt with, a chattel that is essentially a mere subject of contract; and although rights of ownership or rights akin to ownership may be given under it prima facie it is a contract for the hiring or use of the vessel. Under these circumstances it is in accordance with ordinary business common-sense and custom that charterers should be able to contract as agents for undisclosed principals who may come in and take the benefit of the charterparty.²⁷

COMMENT: Whilst Scott LJ's contention that *Fred Drughorn* has overruled *Humble v Hunter* cannot be regarded as correct, there is no doubt that the case has significantly restricted those instances where the intervention of a principal will be regarded as inconsistent with the contract. Munday suggests that, following this case, intervention of the principal may only be regarded as inconsistent with the contract 'where the agent has affected the clear role of owner of property which is the subject matter of the contract'.²⁸

Sixth, the principal will not be permitted to intervene where the third party wishes to contract exclusively with the agent,²⁹ or where the identity or personal attributes of the agent are an important factor for the third party.



Collins v Associated Greyhound Racecourses Ltd **[1930] 1 Ch 1 (CA)**

FACTS: Associated Greyhound Racecourses Ltd ('AGR', the third party) circulated a draft prospectus to a group of underwriters shortly before it was incorporated. An investment company agreed to purchase 1.16 million shares in AGR, or find persons who would subscribe for

26. [1945] KB 562 (CA) 565.

27. [1919] AC 203 (HL) 207.

28. Roderick Munday, *Agency: Law and Principles* (2nd edn, OUP 2013) 259.

29. *Greer v Downs Supply Co* [1927] 2 KB 28 (CA).

the shares. Two underwriters, Mason and Ovington (the agents), agreed to underwrite 12,000 shares addressed to the investment company, but they did not disclose that they were in fact acting on behalf of Collins (the undisclosed principal). Upon AGR's incorporation, the prospectus was issued to the public, where it was found to contain an innocent misrepresentation. Collins sought to intervene and rescind the underwriting agreement entered into by Mason and Ovington on his behalf.

HELD: Collins was not permitted to intervene. Lord Hanworth MR stated:

[T]he contract between the company and Mason and Ovington was one in which importance attached to the personality of the persons with whom the company were contracting. In such a case it is not right to treat the agents as necessarily interchangeable with their principal so as to enable the principal to come forward and seek to disaffirm the contract on the ground of a misrepresentation on which he alone had relied.³⁰

See AL Goodhart and CJ Hamson, 'Undisclosed Principals in Contract' (1932) 4 CLJ 320

Finally, the courts have held that the principal will not be able to intervene where the third party has some reason for not wanting to deal with the undisclosed principal, but, as will be seen, the validity of this rule is open to question.



Said v Butt [1920] 3 KB 497 (KB)

FACTS: Said (the undisclosed principal) was a theatre critic who wished to attend the first night performance of a play in the Palace Theatre (the third party). Said had made a number of serious and unfounded allegations against a number of the theatre staff, and therefore knew that his application for a ticket would be refused. Said therefore asked Pollock (the agent), a friend of his, to purchase a ticket for him. When Said turned up on the first night, Butt (the theatre manager) refused him admission. Said commenced proceedings against Butt.

HELD: Said's action failed. McCardie J stated:

The personal element was here strikingly present. The plaintiff knew that the Palace Theatre would not contract with him for the sale of a seat ... They had expressly refused to do so. He was well aware of their reasons. I hold that by the mere device of utilizing the name and services of Mr. Pollock, the plaintiff could not constitute himself a contractor with the Palace Theatre against their knowledge, and contrary to their express refusal. He is disabled from asserting that he was the undisclosed principal of Mr. Pollock.³¹

COMMENT: The decision was ultimately based on the contention that there was a contract between Said and the theatre, and this contract was void on the ground of mistake as to identity. This reasoning has been strongly criticized, with Sealy and Hooley branding the case as 'wrongly decided'.³² The criticism stems from the fact that, in cases involving an undisclosed principal, the contract is not between the principal and the third party, but is actually between the agent and the third party, with the principal acquiring a right to intervene in the contract. The subsequent case of *Dyster v Randall & Sons*,³³ the facts of which were very similar to *Said*, appears to have sought to limit the scope of *Said* by stating, *obiter*, that the principal will only be prevented from interfering if his identity was a 'material ingredient'.³⁴

30. [1930] 1 Ch 1 (CA) 33.

31. [1920] 3 KB 497 (KB) 503.

32. Len S Sealy and Richard JA Hooley, *Commercial Law: Text, Cases and Materials* (4th edn, OUP 2009) 190.

33. [1926] Ch 932 (Ch).

34. *ibid* 938 (Lawrence J).

Settlement with the agent

A third party who deals with an agent acting for an undisclosed principal can discharge his liability if he reaches a settlement with the agent. If the principal subsequently seeks to enforce the contract against the third party, the settlement will provide the third party with a complete defence, as the following case demonstrates.

**Coates v Lewes (1808) 1 Camp 444**

FACTS: Coates (the undisclosed principal) instructed an agent to sell a quantity of linseed oil. The agent, with the principal's authority, sold the linseed oil in his own name to Lewes (the third party). Lewes had no idea that the agent was acting on behalf of Coates, as Lewes paid the agent, who then paid Coates. Coates then sought to recover the purchase price from Lewes, and Lewes contended that the oil had already been paid for.

HELD: Coates' claim failed. The agent, with Coates' authority, acted as if he was principal, and therefore a third party who settles with such an agent will discharge his liability to the undisclosed principal.

Accordingly, a third party can discharge his obligations to an undisclosed principal if, prior to discovering the existence of the principal, he settles with the agent. The question that arises is whether the opposite is also true—can an undisclosed principal discharge his obligations to a third party by settling with the agent? As the following controversial case demonstrates, the answer appears to be yes.

**Armstrong v Stokes (1872) LR 7 QB 598 (QB)**

FACTS: J&O Ryder & Co ('Ryder', the agent) was a commission agent that sometimes acted as agent on behalf of others, and sometimes acted on its own behalf. Armstrong (the third party) had dealt with Ryder on numerous occasions, but never enquired whether it was acting as an agent or on its own behalf. Ryder, acting on behalf of Stokes (the principal), purchased a number of shirts from Armstrong, but did not disclose that it was acting as Stokes's agent. Armstrong delivered the shirts to Ryder, which then passed them on to Stokes. Stokes paid Ryder for the shirts, but Ryder could not afford to pay Armstrong. Armstrong discovered that Ryder was acting on behalf of Stokes and so sued Stokes for the purchase price.

HELD: Armstrong's claim failed and the Court held that the payment that Stokes made to Ryder discharged his liability to Armstrong. Blackburn J stated that to require an undisclosed principal to pay 'after they had fairly paid the price to those whom the vendor believed to be the principals, and to whom alone the vendor gave credit ... would produce intolerable hardship'.³⁵

COMMENT: As discussed on p 144, the general rule is that a disclosed principal cannot discharge his obligations to a third party by settling with the agent. However, *Armstrong* states that an undisclosed principal can settle with an agent. The correctness of *Armstrong* has split academic commentators. Munday states:

Given that the principal has either created this situation by choosing to remain concealed from the third party behind the cloak of the agent or has been aware that the agent

35. (1872) LR 7 QB 598 (QB) 610.

proposed to act on his behalf in this way, it is . . . difficult to see why . . . the third party should suffer if the principal takes it into his head to settle with the agent.³⁶

However, Reynolds argues in favour of *Armstrong*, stating:

The principal has utilized the services of an intermediary who in the transaction into which he has entered has raised no expectation of the accountability of a principal. Surely the principal's duty is performed by keeping the intermediary in funds: if the third party loses, it is because of his misplaced trust in the intermediary. There is no need to make the principal the insurer.³⁷

Tortious liability

Consider the following example:

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COMCORP LTD

ComCorp (the principal) wishes to expand its manufacturing capacity and so it instructs HomeBuild Ltd (the agent) to build two new factories. HomeBuild builds the factories as requested, but several months later, the roof falls in, injuring Rebecca, one of ComCorp's employees. It transpires that the roof was fitted in a negligent manner, but Rebecca cannot commence proceedings against HomeBuild as it has since been dissolved.

The question that arises is can Rebecca sue ComCorp or, in other words, can the principal be held liable for the tortious acts of its agent? There is little doubt that where a principal authorizes his agent to engage in, or ratifies, a tortious act, then the principal can be liable to persons who sustain loss due to the agent's tort.



Monaghan v Taylor (1886) 2 TLR 685 (DC)

FACTS: Taylor (the principal) was the proprietor of a music hall. He engaged a singer (the agent) who, on numerous occasions, sang a song that infringed the copyright of Monaghan (the third party). Monaghan sued Taylor on the ground that Taylor authorized the singer to sing the song. Taylor denied this.

HELD: The singer was hired to sing whatever songs she liked, and Taylor exercised no supervision or control over her. This was enough to establish that a relationship of agency existed and that Taylor had authorized the singer to sing the song complained of. Accordingly, Taylor was held liable for the copyright infringement and ordered to pay £2 for each occasion the song was sung.

Certain torts require the alleged **tortfeasor** to be in a certain state of mind before liability can be imposed. For example, the tort of deceit requires a false statement to be made knowingly, or without belief in its truth, or recklessly careless whether it be

→ **tortfeasor:** a person who commits a tort

36. Roderick Munday, *Agency: Law and Principles* (2nd edn, OUP 2013) 275.

37. FMB Reynolds, 'Practical Problems of the Undisclosed Principal Doctrine' (1983) 36 CLP 119, 134.

true or false.³⁸ Where the principal has the required state of mind, but the agent does not, then liability can be imposed on the principal, as the following case demonstrates.



Cornfoot v Fowke (1840) 6 M&W 358

FACTS: Fowke (the third party) was looking for a house to rent for himself and his children to live in. He approached Clarke (the agent) and asked him if he knew of any houses to rent. Clarke stated that he knew of a suitable house, namely one that belonged to Cornfoot (the principal). Fowke asked Clarke whether there was anything objectionable about the house, to which Clarke answered no. Fowke agreed to rent the house and signed a lease agreement. A day later, Fowke discovered that the house was next door to a brothel. It transpired that Cornfoot knew of this, but Clarke did not. Fowke wrote to Cornfoot, informing him that he would not be taking up the lease. Cornfoot sued.

HELD: Rolfe B stated that:

(i) if the plaintiff, knowing of the nuisance, expressly authorized Clarke to state that it did not exist, or to make any statement of similar import; or if he purposely employed an agent, ignorant of the truth, in order that such agent might innocently make a false statement believing it to be true, and might so deceive the party with whom he was dealing, in either of these cases he would be guilty of a fraud.³⁹

COMMENT: In *Cornfoot*, liability was imposed upon a principal who knew that the statement made by his innocent agent was false. However, liability for deceit will not be imposed on a principal who innocently makes a false statement, which is repeated by the agent, even if the agent knew the statement to be false.⁴⁰

Vicarious liability

If the agent of a principal is also his employee, then the principal can be vicariously liable for the tortious acts of his agent, providing that the acts were carried out in the course of the agent's employment.⁴¹ The question that arises is whether an agent who acts in an unauthorized manner is acting within the scope of his employment. In other words, within the agency relationship, are the scope of employment and authority synonymous? In the following case, the House clearly stated that a principal will not be vicariously liable for the acts of an agent who is acting in an unauthorized manner.



Armagas Ltd v Mundogas SA (The Ocean Frost) [1986] AC 717 (HL)

FACTS: Magelssen (the agent) was the vice-president and manager of Mundogas SA (the principal). Mundogas was trying to sell the ship *The Ocean Frost*. Armagas Ltd (the third party) was interested in purchasing the ship, but only if it could then charter it back to Mundogas for at least three years. Magelssen did not have the authority to agree such a deal, but told Armagas

38. *Derry v Peek* (1889) 14 App Cas 337 (HL).

39. (1840) 6 M&W 358, 370.

40. *Armstrong v Strain* (1952) 1 KB 232 (CA).

41. A discussion of what constitutes 'in the course of employment' is beyond the scope of this text, but will be covered by most tort textbooks.

that he did. Armagas purchased the ship and Mundogas entered into a three-year charterparty. Magelssen's fraud came to light and Armagas sued Mundogas.

HELD: The claim failed. Lord Keith stated:

At the end of the day the question is whether the circumstances under which a servant has made the fraudulent misrepresentation which has caused loss to an innocent party contracting with him are such as to make it just for the employer to bear the loss. Such circumstances exist where the employer by words or conduct has induced the injured party to believe that the servant was acting in the lawful course of the employer's business. They do not exist where such belief, although it is present, has been brought about through misguided reliance on the servant himself, when the servant is not authorised to do what he is purporting to do, when what he is purporting to do is not within the class of acts that an employee in his position is usually authorised to do, and when the employer has done nothing to represent that he is authorised to do it.⁴²

Accordingly, given that Magelssen was not acting within the scope of his actual or apparent authority, the House held that he was not acting within the scope of his employment and so Mundogas was not liable.

COMMENT: The House of Lords affirmed the decision of the Court of Appeal, but it is unclear as to the scope of the decision. The Court of Appeal decision was clearly stated as referring to all torts of representation, but, as Lord Keith's statement indicates, the decision of the House of Lords was couched solely in terms of fraudulent misrepresentation. As a result, Reynolds states that '[t]he question of how far this reasoning applies to other torts of representation remains therefore open to argument'.⁴³

See David G Powles, 'Ship Sales and Frauds by Intermediaries' [1987] JBL 337

CONCLUSION

This chapter demonstrates that complications can arise which can prevent a contractual relationship being created between the principal and third party. Given that the primary purpose of many agency relationships is to effect contractual relations between a principal and a third party, it is of vital importance to be aware of those instances where this purpose might be prevented from coming to fruition.

Having discussed the relationship between the principal and agent, and between the principal and third party, Chapter 8 moves on to discuss the relationship between the agent and the third party. The chapter also discusses those instances where the third party will acquire a right to sue the principal and third party. Accordingly, there is a significant overlap between the discussion in this chapter and in Chapter 8.

PRACTICE QUESTIONS

1. 'The legal rules relating to a third party's liability to an undisclosed principal lack a sufficiently clear justification and, as a result, the law in this area is confused and lacks fairness.'
Discuss the validity of this statement.

42. [1986] AC 717 (HL) 782–3.

43. FMB Reynolds, 'Apparent Authority: Principal's Liability for Fraud of Agent; Bribery of Agent' [1986] JBL 396, 397.