CHAPTER 1

AGENCY

SECTION 1. WHO IS AN AGENT?

Gorton v. Doty

69 P.2d 136 (Idaho 1937).

In September, 1935, an action was commenced by R. S. Gorton, father of Richard Gorton, to recover expenses incurred by the father for hospitalization, physicians', surgeons', and nurses' fees, and another by the son, by his father as guardian ad litem, to recover damages for injuries sustained as a result of an accident. By stipulation the actions were consolidated for trial. Upon the trial of the cases so consolidated, the jury returned a verdict in favor of the father for $870 and another in favor of the son for $5,000. Separate judgments were then entered upon such verdicts. Thereafter a motion for a new trial was made and denied in each case. The cases come here upon an appeal from each judgment and order denying a new trial.

. . .

It appears that in September, 1934, Richard Gorton, a minor, was a junior in the Soda Springs High School and a member of the football team; that his high school team and the Paris High School team were scheduled to play a game of football at Paris on the 21st. Appellant was teaching at the Soda Springs High School and Russell Garst was coaching the Soda Springs team. On the day the game was played, the Soda Springs High School team was transported to and from Paris in privately owned automobiles. One of the automobiles used for that purpose was owned by appellant. Her car was driven by Mr. Garst, the coach of the Soda Springs High School team.

One of the most difficult questions, if not the most difficult, presented by the record, is, Was the coach, Russell Garst, the agent of appellant while and in driving her car from Soda Springs to Paris, and in returning to the point where the accident occurred?

Briefly stated, the facts bearing upon that question are as follows: That appellant knew the Soda Springs High School football team and the Paris High School football team were to play a game of football at Paris September 21, 1934; that she volunteered her car for use in transporting some of the members of the Soda Springs team to and from the game; that she asked the coach, Russell Garst, the day before the game, if he had all the cars necessary for the trip to Paris the next day; that he said he needed

one more; that she told him he might use her car if he drove it; that she was not promised compensation for the use of her car and did not receive any; that the school district paid for the gasoline used on the trip to and from the game; that she testified she loaned the car to Mr. Garst; that she had not employed Mr. Garst at any time and that she had not at any time ''directed his work or his services, or what he was doing.''

. . .

Broadly speaking, ''agency'' indicates the relation which exists where one person acts for another. It has these three principal forms: 1. The relation of principal and agent; 2. The relation of master and servant; and, 3. The relation of employer or proprietor and independent contractor. While all have points of similarity, there are, nevertheless, numerous differences. We are concerned here with the first form only.

Specifically, ''agency'' is the relationship which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act. [Restatement of Agency § 1.]

[In a subsequent passage, the court indicated that the principal is responsible for the acts of his or her agent: ''After having given the jury a correct definition of the term 'agency,' the [trial] court . . . instructed the jury that if they found from the evidence that Russell Garst was, at the time of the accident, the agent of appellant, then that she was chargeable with the acts of her agent as fully and to the same extent as though she had been driving the automobile herself . . . , which is unquestionably the law.'']

. . . [This court has not held] that the relationship of principal and agent must necessarily involve some matter of business, but only that where one undertakes to transact some business or manage some affair for another by authority and on account of the latter, the relationship of principal and agent arises.

To enable the Soda Springs football team to play football at Paris, it had to be transported to Paris. Automobiles were to be used and another car was needed. At that juncture, appellant volunteered the use of her car. For what purpose? Necessarily for the purpose of furnishing additional transportation. Appellant, of course, could have driven the car herself, but instead of doing that, she designated the driver (Russell Garst) and, in doing so, made it a condition precedent that the person she designated should drive her car. That appellant thereby at least consented that Russell Garst should act for her and in her behalf, in driving her car to and from the football game, is clear from her act in volunteering the use of her car upon the express condition that he should drive it, and, further, that Mr. Garst consented to so act for appellant is equally clear by his act in driving the car. It is not essential to the existence of authority that there be a contract between principal and agent or that the agent promise to act as such (Restatement Agency, §§ 15, 16, pp. 50–54), nor is it essential to the

relationship of principal and agent that they, or either, receive compensation (Restatement Agency, § 16, p. 53).

Furthermore, this court held in Willi v. Schaefer Hitchcock Co., 53 Idaho 367, 25 P.2d 167, in harmony with the clear weight of authority, that the fact of ownership alone (conceded here), regardless of the presence or absence of the owner in the car at the time of the accident, establishes a prima facie case against the owner for the reason that the presumption arises that the driver is the agent of the owner. . . .

It is vigorously contended, however, that the facts and circumstances bearing upon the question under discussion show appellant loaned her car to Mr. Garst. A determination of that question makes it necessary to quote appellant's testimony. She testified as follows:

"Q. On or about the 21st day of September, 1934, state whether or not you permitted Russell Garst to use that car?

"A. I did.

"Q. Under what circumstances?

"A. I loaned it to him.

"Q. When did you loan it to him? Was it that day, or the day before?

"A. On the day before I told him he might have it the next day.

"Q. Did you receive any compensation, or were you promised any compensation, for its use?

"A. No, sir.

"Q. What were the circumstances under which you permitted him to take it?

"A. Well,—"

After having so testified, appellant was then asked:

"Q. You may relate the conversation with him, if there was such conversation.

"A. I asked him if he had all the cars necessary for his trip to Paris the next day. He said he needed one more. I said that he might use mine if he drove it. That was the extent of it."

While it appears that appellant first testified that she permitted Russell Garst to use her car and also that she loaned it to him, it further appears that when she was immediately afterward asked to state the conversation she had with the coach about the matter, she stated that she asked him if he had all the cars necessary for the trip to Paris the next day, that he said he needed one more, that she said he might use her car if he drove it, and, finally, she said that that was the extent of it. It is clear, then, that appellant intended, in relating the conversation she had with the coach, to state the circumstances fully, because, after having testified to the conversation, she concluded by saying, "That was the extent of it." Thus she gave the jury to understand that those were the circumstances, and all of the circumstances, under which Russell Garst drove her car to the

football game. If the appellant fully and correctly related the conversation she had with the coach and the circumstances under which he drove her car, as she unquestionably undertook to, and did, do, it follows that, as a matter of fact, she did not say anything whatever to him about loaning her car and he said nothing whatever to her about borrowing it.

We therefore conclude the evidence sufficiently supports the finding of the jury that the relationship of principal and agent existed between appellant and Russell Garst.

. . .

During the course of the closing argument of counsel for respondent, an objection was made by counsel for appellant to certain remarks addressed to the jury. Thereupon the trial court ordered a brief recess and took up such objection in chambers with counsel for the respective parties, whereupon the following proceedings took place outside of the presence of the jury:

> ''Mr. GLENNON: What I said, your Honor, was in response to counsel's repeated charges that the plaintiff was attempting to mulch [mulct] the defendant in damages, and I stated to the jury in substance, 'That you have a right to draw on your experience as business men in determining the facts in this case, and that you know from your experience as business men that prudent automobile owners usually protect themselves against just such contingencies as are involved in this case.' ''

Following that statement by Senator Glennon, counsel for appellant agreed it was substantially correct. Upon returning to the courtroom, the trial judge denied appellant's motion for a mistrial and then instructed the reporter to read the above quoted remarks to the jury, after which the court instructed the jury to disregard the remarks.

Appellant contends that the trial court erred in denying her motion for a mistrial.

Funk & Wagnalls New Standard Dictionary defines the word mulct: ''1. To sentence to a pecuniary penalty or forfeiture as a punishment; fine; hence, to fine unjustly, as, to mulct the prisoner in $100. 2. To punish.'' Appellant had testified during the trial that she volunteered the use of her car. To charge, then, that respondent was attempting to ''mulct'' her in damages carried the inference that respondent was attempting to punish her in damages for having volunteered the use of her car for the commendable purpose of supplying additional transportation for the home town football team.

And it will be noted that Mr. Glennon stated, and the record shows no denial, that the above-quoted remarks were made by him only in response to repeated charges by appellant's counsel that respondent was attempting to mulct appellant in damages. There is no evidence whatever in the record justifying such charges. They were made during the course of the argument of counsel for appellant, and were as fully and clearly outside the record as

the remarks of counsel for respondent. It was a case of meeting improper argument with improper argument. The remarks complained of were provoked by the conduct of counsel for appellant. Hence, we conclude that appellant has no just cause for complaint. Having reached that conclusion, we find it unnecessary to review the cases cited by counsel for the respective parties.

. . .

The judgments and orders are affirmed with costs to respondents.

■ BUDGE, J., Dissenting.—I am unable to concur in the majority opinion.

As I read the entire record there is a total lack of evidence to support the allegation in the complaint that Garst was the agent of appellant Doty at or prior to the time of the accident in which respondent Richard Gorton was injured and as such agent was acting within the scope of his authority. An agent is one who acts for another by authority from him, one who undertakes to transact business or manage some affair for another by authority and on account of the latter. (Moreland v. Mason, 45 Idaho 143, 260 P. 1035.) Agency means more than mere passive permission. It involves request, instruction or command. (Klee v. United States, 53 F.2d 58.) . . . As I read the record [Ms. Doty] simply loaned her car to Garst to enable him to furnish means of transportation for the team from Soda Springs to Paris. It was nothing more or less than a kindly gesture on her part to be helpful to Garst, the athletic coach, in arranging transportation for the team. The mere fact that she stated to Garst that he should drive the car was a mere precaution upon her part that the car should not be driven by any one of the young boys, a perfectly natural thing for her to do. It is principally and particularly upon this statement of fact that the majority opinion holds that the relationship of principal and agent was created and that Garst became the agent of Miss Doty, authorized by her to undertake the transportation of the boys from Soda Springs to Paris for her and on her behalf. In other words, Miss Doty is held legally liable for each and every act done or performed by Garst as though she had been personally present and personally performed each and every act that was done or performed by Garst, this in the absence of any contractual relationship between her and Garst or between her and the school district. The rule would seem to be that one who borrows a car for his own use is a gratuitous bailee and not an agent of the owner. (Gochee v. Wagner, 257 N.Y. 344, 178 N.E. 553.) . . . .

I am also of the opinion the judgment should be reversed because of the prejudicial remarks of one of counsel for respondent while making his closing argument to the jury as follows:

> "That you have a right to draw on your experience as business men in determining the facts in this case and what you know from your experience as business men that prudent automobile owners usually protect themselves against just such contingencies as are involved in this case."

Upon the making of the above-quoted remarks by respondent's counsel appellant moved for a mistrial basing his motion upon the theory that they suggested that the appellant was carrying insurance and would not have to pay any judgment the jury might render, and, that there was no evidence to support such a theory. The court refused to declare a mistrial but directed counsel for respondent not to argue the point further and directed the jury to disregard that part of counsel's argument. However, the prejudicial effect of the remarks was not cured by the court instructing the jury to disregard that part of counsel's argument. Nothing can be gleaned from the remarks made by learned counsel other than that he, intentionally or otherwise, clearly and unmistakably impressed upon the minds of the jurors that appellant carried insurance on her car and that she personally would not be called upon to pay any verdict that might be rendered against her. Error for injecting the question of insurance in a case of this character is quite clearly stated in [citing numerous authorities]. . . .

The judgment should be reversed and the cause remanded for further proceedings as herein indicated.

ANALYSIS

1. The dissent obviously disagreed with the majority as to the existence of an agency relationship between Doty and the Coach. Did the dissent disagree as to the test to be applied or merely as to the way in which the test should be applied?

2. The majority stated: "It is not essential ... that there be a contract between principal and agent." What did the court mean by that?

3. Suppose that you were Ms. Doty's attorney and that a few months after the decision was handed down she stopped by your office. She tells you that the new football coach wants to use her car to take some players to another game. She asks for your advice as to how she could avoid liability in the event of an accident. What do you tell her?

4. Was the court using agency concepts to impose liability on the alleged principal in order to achieve some desired outcome? If so, what policy outcome was the court trying to implement?

INTRODUCTORY NOTE

In the next case, A. Gay Jenson Farms Co. v. Cargill, Inc., the context is that of a creditor exercising control over its debtors after the debtor has experienced financial difficulties. The plaintiffs were farmers who sold their grain crops to Warren Grain & Seed Co. (Warren). Warren was a local firm that operated a grain elevator (a storage facility). Cargill is a large, worldwide dealer in grain. On Cargill's view of the facts, Warren bought grain from the farmers and sold it to Cargill. On the farmers' view of the facts, Warren bought grain as an agent for Cargill. Warren became insolvent without having paid the farmers for their grain and they sued Cargill. The case offers a nice illustration of a legal issue of considerable impor-

tance to business firms like Cargill that provide trade credit to other firms, as well as to banks and other financial intermediaries.

A. Gay Jenson Farms Co. v. Cargill, Inc.

309 N.W.2d 285 (Minn.1981).

Plaintiffs, 86 individual, partnership or corporate farmers, brought this action against defendant Cargill, Inc. (Cargill) and defendant Warren Grain & Seed Co. (Warren) to recover losses sustained when Warren defaulted on the contracts made with plaintiffs for the sale of grain. After a trial by jury, judgment was entered in favor of plaintiffs, and Cargill brought this appeal. We affirm.

This case arose out of the financial collapse of defendant Warren Seed & Grain Co., and its failure to satisfy its indebtedness to plaintiffs. Warren, which was located in Warren, Minnesota, was operated by Lloyd Hill and his son, Gary Hill. Warren operated a grain elevator and as a result was involved in the purchase of . . . grain from local farmers. The cash grain would be resold through the Minneapolis Grain Exchange or to the terminal grain companies directly. Warren also stored grain for farmers and sold chemicals, fertilizer and steel storage bins. In addition, it operated a seed business which involved buying seed grain from farmers, processing it and reselling it for seed to farmers and local elevators.

Lloyd Hill decided in 1964 to apply for financing from Cargill. Cargill's officials from the Moorhead regional office investigated Warren's operations and recommended that Cargill finance Warren.

Warren and Cargill thereafter entered into a security agreement which provided that Cargill would loan money for working capital to Warren on "open account" financing up to a stated limit, which was originally set as $175,000.[2] Under this contract, Warren would receive funds and pay its expenses by issuing drafts drawn on Cargill through Minneapolis banks. The drafts were imprinted with both Warren's and Cargill's names. Proceeds from Warren's sales would be deposited with Cargill and credited to its account. In return for this financing, Warren appointed Cargill as its grain agent for transaction with the Commodity Credit Corporation. Cargill was also given a right of first refusal to purchase market grain sold by Warren to the terminal market.

A new contract was negotiated in 1967, extending Warren's credit line to $300,000 and incorporating the provisions of the original contract. It was also stated in the contract that Warren would provide Cargill with annual financial statements and that either Cargill would keep the books for Warren or an audit would be conducted by an independent firm. Cargill was given the right of access to Warren's books for inspection.

2. Loans were secured by a second mortgage on Warren's real estate and a first chattel mortgage on its inventories of grain and merchandise in the sum of $175,000 with 7% interest. . . .

In addition, the agreement provided that Warren was not to make capital improvements or repairs in excess of $5,000 without Cargill's prior consent. Further, it was not to become liable as guarantor on another's indebtedness, or encumber its assets except with Cargill's permission. Consent by Cargill was required before Warren would be allowed to declare a dividend or sell and purchase stock.

Officials from Cargill's regional office made a brief visit to Warren shortly after the agreement was executed. They examined the annual statement and the accounts receivable, expenses, inventory, seed, machinery and other financial matters. Warren was informed that it would be reminded periodically to make the improvements recommended by Cargill.[3] At approximately this time, a memo was given to the Cargill official in charge of the Warren account, Erhart Becker, which stated in part: "This organization [Warren] needs *very strong* paternal guidance."

In 1970, Cargill contracted with Warren and other elevators to act as its agent to seek growers for a new type of wheat called Bounty 208. Warren, as Cargill's agent for this project, entered into contracts for the growing of the wheat seed, with Cargill named as the contracting party. Farmers were paid directly by Cargill for the seed and all contracts were performed in full. In 1971, pursuant to an agency contract, Warren contracted on Cargill's behalf with various farmers for the growing of sunflower seeds for Cargill. The arrangements were similar to those made in the Bounty 208 contracts, and all those contracts were also completed. Both these agreements were unrelated to the open account financing contract. In addition, Warren, as Cargill's agent in the sunflower seed business, cleaned and packaged the seed in Cargill bags.

During this period, Cargill continued to review Warren's operations and expenses and recommend that certain actions should be taken.[4] Warren purchased from Cargill various business forms printed by Cargill and received sample forms from Cargill which Warren used to develop its own business forms.

Cargill wrote to its regional office in 1970 expressing its concern that the pattern of increased use of funds allowed to develop at Warren was similar to that involved in two other cases in which Cargill experienced severe losses. Cargill did not refuse to honor drafts or call the loan, however. A new security agreement which increased the credit line to

3. Cargill headquarters suggested that the regional office check Warren monthly. Also, it was requested that Warren be given an explanation for the relatively large withdrawals from undistributed earnings made by the Hills, since Cargill hoped that Warren's profits would be used to decrease its debt balance. Cargill asked for written requests for withdrawals from undistributed earnings in the future.

4. Between 1967 and 1973, Cargill suggested that Warren take a number of steps, including: (1) a reduction of seed grain and cash grain inventories; (2) improved collection of accounts receivable; (3) reduction or elimination of its wholesale seed business and its speciality grain operation; (4) marketing fertilizer and steel bins on consignment; (5) a reduction in withdrawals made by officers; (6) a suggestion that Warren's bookkeeper not issue her own salary checks; and (7) cooperation with Cargill in implementing the recommendations. These ideas were apparently never implemented, however.

$750,000 was executed in 1972, and a subsequent agreement which raised the limit to $1,250,000 was entered into in 1976.

Warren was at that time shipping Cargill 90% of its ... grain. When Cargill's facilities were full, Warren shipped its grain to other companies. Approximately 25% of Warren's total sales was seed grain which was sold directly by Warren to its customers.

As Warren's indebtedness continued to be in excess of its credit line, Cargill began to contact Warren daily regarding its financial affairs. Cargill headquarters informed its regional office in 1973 that, since Cargill money was being used, Warren should realize that Cargill had the right to make some critical decisions regarding the use of the funds. Cargill headquarters also told Warren that a regional manager would be working with Warren on a day-to-day basis as well as in monthly planning meetings. In 1975, Cargill's regional office began to keep a daily debit position on Warren. A bank account was opened in Warren's name on which Warren could draw checks in 1976. The account was to be funded by drafts drawn on Cargill by the local bank.

In early 1977, it became evident that Warren had serious financial problems. Several farmers, who had heard that Warren's checks were not being paid, inquired or had their agents inquire at Cargill regarding Warren's status and were initially told that there would be no problem with payment. In April 1977, an audit of Warren revealed that Warren was $4 million in debt. After Cargill was informed that Warren's financial statements had been deliberately falsified, Warren's request for additional financing was refused. In the final days of Warren's operation, Cargill sent an official to supervise the elevator, including disbursement of funds and income generated by the elevator.

After Warren ceased operations, it was found to be indebted to Cargill in the amount of $3.6 million. Warren was also determined to be indebted to plaintiffs in the amount of $2 million, and plaintiffs brought this action in 1977 to seek recovery of that sum. Plaintiffs alleged that Cargill was jointly liable for Warren's indebtedness as it had acted as principal for the grain elevator.

. . .

The major issue in this case is whether Cargill, by its course of dealing with Warren, became liable as a principal on contracts made by Warren with plaintiffs. Cargill contends that no agency relationship was established with Warren, notwithstanding its financing of Warren's operation and its purchase of the majority of Warren's grain. However, we conclude that Cargill, by its control and influence over Warren, became a principal with liability for the transactions entered into by its agent Warren.

Agency is the fiduciary relationship that results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act....

In order to create an agency there must be an agreement, but not necessarily a contract between the parties.... An agreement may result in the creation of an agency relationship although the parties did not call it an agency and did not intend the legal consequences of the relation to follow. The existence of the agency may be proved by circumstantial evidence which shows a course of dealing between the two parties.... When an agency relationship is to be proven by circumstantial evidence, the principal must be shown to have consented to the agency since one cannot be the agent of another except by consent of the latter....

Cargill contends that the prerequisites of an agency relationship did not exist because Cargill never consented to the agency, Warren did not act on behalf of Cargill, and Cargill did not exercise control over Warren. We hold that all three elements of agency could be found in the particular circumstances of this case. By directing Warren to implement its recommendations, Cargill manifested its consent that Warren would be its agent. Warren acted on Cargill's behalf in procuring grain for Cargill as the part of its normal operations which were totally financed by Cargill.[7] Further, an agency relationship was established by Cargill's interference with the internal affairs of Warren, which constituted de facto control of the elevator.

A creditor who assumes control of his debtor's business may become liable as principal for the acts of the debtor in connection with the business. Restatement (Second) of Agency § 14 O (1958). It is noted in comment a to section 14 O that:

> A security holder who merely exercises a veto power over the business acts of his debtor by preventing purchases or sales above specified amounts does not thereby become a principal. However, if he takes over the management of the debtor's business either in person or through an agent, and directs what contracts may or may not be made, he becomes a principal, liable as a principal for the obligations incurred thereafter in the normal course of business by the debtor who has now become his general agent. The point at which the creditor becomes a principal is that at which he assumes de facto control over the conduct of his debtor, whatever the terms of the formal contract with his debtor may be.

A number of factors indicate Cargill's control over Warren, including the following:

(1) Cargill's constant recommendations to Warren by telephone;

(2) Cargill's right of first refusal on grain;

(3) Warren's inability to enter into mortgages, to purchase stock or to pay dividends without Cargill's approval;

7. Although the contracts with the farmers were executed by Warren, Warren paid for the grain with drafts drawn on Cargill. While this is not in itself significant ... it is one factor to be taken into account in analyzing the relationship between Warren and Cargill.

(4) Cargill's right of entry onto Warren's premises to carry on periodic checks and audits;

(5) Cargill's correspondence and criticism regarding Warren's finances, officers salaries and inventory;

(6) Cargill's determination that Warren needed "strong paternal guidance";

(7) Provision of drafts and forms to Warren upon which Cargill's name was imprinted;

(8) Financing of all Warren's purchases of grain and operating expenses; and

(9) Cargill's power to discontinue the financing of Warren's operations.

We recognize that some of these elements, as Cargill contends, are found in an ordinary debtor-creditor relationship. However, these factors cannot be considered in isolation, but, rather, they must be viewed in light of all the circumstances surrounding Cargill's aggressive financing of Warren.

It is also Cargill's position that the relationship between Cargill and Warren was that of buyer-supplier rather than principal-agent. Restatement (Second) of Agency § 14K (1958) compares an agent with a supplier as follows:

> One who contracts to acquire property from a third person and convey it to another is the agent of the other only if it is agreed that he is to act primarily for the benefit of the other and not for himself.
>
> Factors indicating that one is a supplier, rather than an agent, are:
>
> (1) That he is to receive a fixed price for the property irrespective of price paid by him. This is the most important. (2) That he acts in his own name and receives the title to the property which he thereafter is to transfer. (3) That he has an independent business in buying and selling similar property.

Restatement (Second) of Agency § 14K, comment a (1958).

Under the Restatement approach, it must be shown that the supplier has an independent business before it can be concluded that he is not an agent. The record establishes that all portions of Warren's operation were financed by Cargill and that Warren sold almost all of its market grain to Cargill. Thus, the relationship which existed between the parties was not merely that of buyer and supplier.

. . .

The amici curiae assert that, if the jury verdict is upheld, firms and banks which have provided business loans to county elevators will decline to make further loans. The decision in this case should give no cause for such concern. We deal here with a business enterprise markedly different from an ordinary bank financing, since Cargill was an active participant in Warren's operations rather than simply a financier. Cargill's course of

dealing with Warren was, by its own admission, a paternalistic relationship in which Cargill made the key economic decisions and kept Warren in existence.

Although considerable interest was paid by Warren on the loan, the reason for Cargill's financing of Warren was not to make money as a lender but, rather, to establish a source of market grain for its business. As one Cargill manager noted, ''We were staying in there because we wanted the grain.'' For this reason, Cargill was willing to extend the credit line far beyond the amount originally allocated to Warren. It is noteworthy that Cargill was receiving significant amounts of grain and that, notwithstanding the risk that was recognized by Cargill, the operation was considered profitable.

On the whole, there was a unique fabric in the relationship between Cargill and Warren which varies from that found in normal debtor-creditor situations. We conclude that, on the facts of this case, there was sufficient evidence from which the jury could find that Cargill was the principal of Warren within the definitions of agency set forth in Restatement (Second) of Agency §§ 1 and 14 O.

NOTE

Warren, Minnesota was a town with a population of about 2,000 at the time this case was tried. Warren is located in Marshall County, which is in the northwest corner of Minnesota, on the North Dakota border, with a population of about 15,000. The plaintiffs were local farmers and the defendant was a corporate giant. The case was tried to a jury.

ANALYSIS

1. Why do you suppose Cargill kept extending more and more credit to Warren?

2. What could the farmers have done to protect themselves from the risk of nonpayment?

3. What could Cargill have done to ensure that the grain it bought from Warren was paid for?

4. In light of your answers to questions 2 and 3, does the result in the case place responsibility for avoiding loss on the person with the lower cost of doing so?

5. If Peter says to Amy, ''Go out and buy a thousand bushels of corn for me and I'll pay you the usual commission,'' Amy is Peter's nonservant agent (that is, she acts on behalf of Peter but is not subject to his control over how the objective is achieved). Peter is bound to contracts made by Amy to buy the corn. Control of the manner in which Amy accomplishes the assignment is not an issue. In the *Cargill* case, however, there seems to have been no evidence to support that kind of ordinary nonservant principal/agent relationship. Presumably that is why the court focuses on control

and on the Restatement (Second) of Agency § 14 O. Examine the nine factors listed by the court as supporting a conclusion that Cargill exercised control over Warren. How, if at all, does each of these factors tend to establish a principal/agent relationship rather than a relationship of creditor to debtor or buyer to supplier?

PLANNING

Suppose you are Cargill's lawyer. The chief executive officer (CEO) of the company, after hearing about the decision in the case involving Warren Grain & Seed Co., asks for your recommendations about how Cargill should change the way it does business to avoid liability in the future. She also wants your views on whether, with a supplier like Warren, at the time that its financial condition became desperate, it would have been advisable for Cargill to (a) call in its loans and force the supplier into bankruptcy or (b) notify all other potential creditors that Cargill would not be liable for any purchases by the supplier. What would you say? Bear in mind that you are expected to exercise sound business, as well as legal, judgment, but that your role is to offer alternatives, not to make decisions.

SECTION 2. LIABILITY OF PRINCIPAL TO THIRD PARTIES IN CONTRACT

A. THE AGENT'S AUTHORITY

Mill Street Church of Christ v. Hogan

785 S.W.2d 263 (Ky.1990).

Mill Street Church of Christ and State Automobile Mutual Insurance Company petition for review of a decision of the New Workers' Compensation Board [hereinafter ''New Board''] which had reversed an earlier decision by the Old Workers' Compensation Board [hereinafter ''Old Board'']. The Old Board had ruled that Samuel J. Hogan was not an employee of the Mill Street Church of Christ and was not entitled to any workers' compensation benefits. The New Board reversed and ruled that Samuel Hogan was an employee of the church.

. . . In 1986, the Elders of the Mill Street Church of Christ decided to hire church member, Bill Hogan, to paint the church building. The Elders decided that another church member, Gary Petty, would be hired to assist if any assistance was needed. In the past, the church had hired Bill Hogan for similar jobs, and he had been allowed to hire his brother, Sam Hogan, the respondent, as a helper. Sam Hogan had earlier been a member of the church but was no longer a member. . . .

Dr. David Waggoner, an Elder of the church, soon contacted Bill Hogan, and he accepted the job and began work. Apparently Waggoner made no mention to Bill Hogan of hiring a helper at that time. Bill Hogan painted the church by himself until he reached the baptistry portion of the church. This was a very high, difficult portion of the church to paint, and he decided that he needed help. After Bill Hogan had reached this point in his work, he discussed the matter of a helper with Dr. Waggoner at his office. According to both Dr. Waggoner and Hogan, they discussed the possibility of hiring Gary Petty to help Hogan. None of the evidence indicates that Hogan was told that he had to hire Petty. In fact, Dr. Waggoner apparently told Hogan that Petty was difficult to reach. That was basically all the discussion that these two individuals had concerning hiring a helper. None of the other Elders discussed the matter with Bill Hogan.

On December 14, 1986, Bill Hogan approached his brother, Sam, about helping him complete the job. Bill Hogan told Sam the details of the job, including the pay, and Sam accepted the job. On December 15, 1986, Sam began working. A half hour after he began, he climbed the ladder to paint a ceiling corner, and a leg of the ladder broke. Sam fell to the floor and broke his left arm. Sam was taken to the Grayson County Hospital Emergency

Room where he was treated. He later was under the care of Dr. James Klinert, a surgeon in Louisville. The church Elders did not know that Bill Hogan had approached Sam Hogan to work as a helper until after the accident occurred.

After the accident, Bill Hogan reported the accident and resulting injury to Charles Payne, a church Elder and treasurer. Payne stated in a deposition that he told Bill Hogan that the church had insurance. At this time, Bill Hogan told Payne the total number of hours worked which included a half hour that Sam Hogan had worked prior to the accident. Payne issued Bill Hogan a check for all of these hours. Further, Bill Hogan did not have to use his own tools and materials in the project. The church supplied the tools, materials, and supplies necessary to complete the project. Bill purchased needed items from Dunn's Hardware Store and charged them to the church's account.

It is undisputed in this case that Mill Street Church of Christ is an insured employer under the Workers' Compensation Act. Sam Hogan filed a claim under the Workers' Compensation Act.* . . .

As part of their argument, petitioners argue the New Board also erred in finding that Bill Hogan possessed implied authority as an agent to hire Sam Hogan. Petitioners contend there was neither implied nor apparent authority in the case at bar.

It is important to distinguish implied and apparent authority before proceeding further. Implied authority is actual authority circumstantially proven which the principal actually intended the agent to possess and includes such powers as are practically necessary to carry out the duties actually delegated. Apparent authority on the other hand is not actual authority but is the authority the agent is held out by the principal as possessing. It is a matter of appearances on which third parties come to rely.

Petitioners attack the New Board's findings concerning implied authority. In examining whether implied authority exists, it is important to focus upon the agent's understanding of his authority. It must be determined whether the agent reasonably believes because of present or past conduct of the principal that the principal wishes him to act in a certain way or to have certain authority. The nature of the task or job may be another factor to consider. Implied authority may be necessary in order to implement the express authority. The existence of prior similar practices is one of the most important factors. Specific conduct by the principal in the past permitting the agent to exercise similar powers is crucial.

The person alleging agency and resulting authority has the burden of proving that it exists. Agency cannot be proven by a mere statement, but it can be established by circumstantial evidence including the acts and conduct of the parties such as the continuous course of conduct of the parties covering a number of successive transactions. . . .

* [Eds.—If Bill Hogan had authority to hire Sam, then Sam would be deemed the Church's agent (technically, a sub-agent) and its employee for purposes of the Worker's Compensation Act.]

In considering the above factors in the case at bar, Bill Hogan had implied authority to hire Sam Hogan as his helper. First, in the past the church had allowed Bill Hogan to hire his brother or other persons whenever he needed assistance on a project. Even though the Board of Elders discussed a different arrangement this time, no mention of this discussion was ever made to Bill or Sam Hogan. In fact, the discussion between Bill Hogan and Church Elder Dr. Waggoner, indicated that Gary Petty would be difficult to reach and Bill Hogan could hire whomever he pleased. Further, Bill Hogan needed to hire an assistant to complete the job for which he had been hired. The interior of the church simply could not be painted by one person. Maintaining a safe and attractive place of worship clearly is part of the church's function, and one for which it would designate an agent to ensure that the building is properly painted and maintained.

Finally, in this case, Sam Hogan believed that Bill Hogan had the authority to hire him as had been the practice in the past. To now claim that Bill Hogan could not hire Sam Hogan as an assistant, especially when Bill Hogan had never been told this fact, would be very unfair to Sam Hogan. Sam Hogan relied on Bill Hogan's representation. The church treasurer in this case even paid Bill Hogan for the half hour of work that Sam Hogan had completed prior to the accident. Considering the above facts, we find that Sam Hogan was within the employment of the Mill Street Church of Christ at the time he was injured.

The decision of the New Workers' Compensation Board is affirmed.

ANALYSIS AND PROBLEMS

1. Is Sam Hogan's belief that his brother Bill had authority to hire Sam relevant to the issue of whether Bill had actual authority to do so?

2. The following problems are based on a simple fact pattern in which Paul owns an apartment building and has hired Ann to manage it.

   a. Paul tells Ann to hire a company to cut the grass. Ann does it. Is Paul bound by the contract?

   b. Without express instructions, Ann hires a janitor to clean the building. Is Paul bound by the employment contract with the janitor?

   c. Suppose Paul specifically instructed Ann not to hire a janitor, but that local custom gives apartment managers the power to hire janitors. Would Paul be bound by the contract?

Dweck v. Nasser

2008 WL 2602169 (Del.Ch.2008)

. . .

I.

A. *The Parties*

Plaintiff Gila Dweck formerly served as president, chief executive officer, and as a member of the board of directors of Kids International,

Inc; the corporation at the center of the underlying dispute between the parties. Dweck is a 30% stockholder in Kids. Defendant Alberto Nasser Missri (''Nasser'') is a Spanish citizen who resides in Geneva, Switzerland. Nasser is the chairman of the board of directors of Kids and controls 52.5% of its equity. . . .

C. *The Settlement Agreement*

. . . The settlement agreement purports to settle ''all claims and disputes among the parties,''. . . . The terms of the agreement require Dweck to pay 52.5% of the aggregate profits, from January 1, 2001 through May 18, 2005, generated by the entities that allegedly competed with Kids. In addition, the settlement agreement provides for a $1.05 million payment from Dweck to Nasser as reimbursement for the litigation expenses he incurred in connection with the Kids dispute. Nasser, for his part, is to compensate Dweck for the value of her 30% equity interest in Kids, to be determined by an arbitrator. . . .

D. *History Of The Case*

The dispute between the parties surfaced in January 2005, when Nasser discovered that Dweck was allegedly operating competing businesses out of Kids' offices in New York. On March 11, 2005, Nasser removed Dweck as president of Kids and replaced her with his nephew, Itzhak Djemal. The parties discussed a settlement beginning in early 2005, but could not reach an agreement. Due to this impasse, Dweck, on May 18, 2005, filed a complaint in this court challenging Nasser's termination of her employment at Kids. In response, Nasser promptly filed a motion to dismiss several counts of the complaint, including a claim that Nasser breached his fiduciary duties by replacing Dweck with his allegedly unqualified nephew. On November 23, 2005, this court granted Nasser's motion, in part, upholding Nasser's termination of Dweck.[8]

Following that decision, activity in the litigation slowed considerably. . . .

In early 2007, hoping to move discussions forward, Dweck retained William B. Wachtel to facilitate a settlement. Although Nasser's attorney of record in the litigation is Kurt Heyman, Wachtel reached out to Amnon Shiboleth, Nasser's close friend, business associate, and primary attorney for over 20 years. Wachtel had known Shiboleth professionally for many years ''most[ly] having to do with [Shiboleth's] representation of Nasser,'' and regarded Shiboleth as someone he felt he ''could have a forthright

8. However, this court also held that the plaintiff sufficiently pled that Nasser ''did not act in the best interest of the company when he replaced the plaintiff with his allegedly unfit nephew.''

conversation with.'' Wachtel asked Shiboleth whether he would be interested in working together to reach a settlement between the parties. As Wachtel discovered, Shiboleth was exceedingly familiar with the underlying dispute because he had assisted in forging the original business agreement between the parties and had ''continued to represent the entity'' from time to time over the years. Shiboleth had even attempted to settle the litigation at the outset of the dispute.

After securing approval, Shiboleth agreed to work with Wachtel.... Draft agreements were circulated among the parties during the spring of 2007. Nasser reviewed these agreements and instructed Heyman as to terms he objected to and considered non-negotiable. Specifically, Nasser felt that Dweck should be responsible for all the expenses and costs he incurred in the Kids dispute, that he would not compensate Dweck directly for her equity value in Kids, and he did not ''want to be the one who wound up with the company at the end of the day.'' Negotiations continued through the summer without significant progress due partly to these pre-conditions. In August 2007, however, Nasser changed his attitude and instructed Heyman that he wanted to reach a settlement and, thus, would relent, if necessary to resolve the dispute. Heyman testified that after this August 2007 discussion he understood that Nasser no longer wanted to ''interpose those issues as objections.'' ...

Significantly, Nasser also told Heyman that he had directed Shiboleth ''to get it done,'' which Heyman understood to mean settle the litigation. Before this conversation, Heyman had spoken with Shiboleth who related a substantially similar conversation with Nasser and told Heyman that Nasser had directed him to settle the dispute.

. . .

Beginning in November, the parties increased their efforts to reach a resolution to avoid the looming discovery necessary for the scheduled trial. ...

The settlement negotiations became intense and even ''frantic'' starting around November 13. Wachtel sent a proposed settlement agreement, signed by Dweck, on November 13, but it included proposed terms that were not included in the previously circulated drafts that Nasser had reviewed. The salient proposed terms included a cap on certain damages Dweck might owe to Nasser depending on the outcome of an agreed upon arbitration. In addition, the draft included a provision permitting Dweck, in lieu of a monetary payment, to transfer to Kids the two allegedly competing companies.

Since Shiboleth was out of town, Heyman, after speaking with Nasser, responded to the draft on November 14, notifying Wachtel of Nasser's objection to the possible transfer to Kids and stating that Nasser was willing ''to accept ... a 'floor' of $15 million and a 'cap' of $50 million.''[29]

29. ... Despite Heyman's more significant involvement in the negotiations at this point, he testified that Shiboleth was still the settlement attorney and ''remained the point person.'' ...

Wachtel sent a second draft settlement agreement at 3:17 p.m. on November 16, eliminating the provision regarding any transfer to Kids and setting the cap at $40 million. Like the other settlement drafts, this document was signed by Dweck.

Since November 16 was a Friday, settlement discussions did not resume until the morning of November 19. Dweck . . . agreed to remove the cap provision and the transfer provision entirely. Therefore, Wachtel sent Nasser an executed agreement at 11:37 a.m. with the cap provision removed, but otherwise substantially similar to the November 16 draft. Satisfied that all of Nasser's issues had been addressed, Heyman responded at 3:39 p.m. . . . thanking Wachtel for his "perseverance." As discussed below, Heyman was careful not to expressly agree to the settlement because he felt that authority was vested with Shiboleth. That afternoon, however, Shiboleth, who had already secured Nasser's final consent to the agreement, did notify Wachtel that the action was settled and that Nasser would promptly sign the agreement. Wachtel sent the final settlement agreement at 5:24 p.m. for Nasser's signature. At that time, Wachtel, Shiboleth, and Heyman believed that a final settlement had been reached between the parties.

Nasser testified that he took a 7 p.m. plane back to Geneva on November 19 and did not see the final settlement agreement on that date. Heyman testified, however, that the following day Nasser told him that "Shiboleth's office was forwarding the materials to him for his signature" and that he would sign the agreement. Instead of executing the agreement, Nasser sent Heyman an email on November 23 stating "there are things that I don't understand in the agreement, call me after the holiday to discuss. . . ."

On November 28, Nasser objected to several provisions, including the contemplated payment to Dweck, his continued interest in Kids, and the less than full restitution for his losses. These are the same principal objections identified at the outset of the settlement negotiations, but relented on during the August 2007 conversation with Heyman. These provisions were also included in the earlier draft agreements Nasser had reviewed without objection.

Nasser also rejected Shiboleth's authority to enter into the settlement, telling Heyman "that it was never his intention to give up the right to review and approve the agreement just as Ms. Dweck had refused to sign before, he could refuse to sign now." Heyman informed Nasser that he believed Shiboleth had been given the authority to enter into the settlement, but Nasser disagreed.

Shortly after this conversation, Nasser memorialized his objections to the settlement agreement in an email he sent to Heyman and Shiboleth on December 3. . . .

Offended by Nasser's conduct, Shiboleth sent him a strongly worded letter, dated February 18, 2008, expressing his disappointment with Nasser's retention of [new counsel] and his refusal to agree to the settlement. Shiboleth also reminded Nasser that he had authorization to settle the dispute and that Nasser independently agreed to the settlement on seven different occasions.

. . .

III.

A. *Nasser Is Bound To The Settlement Agreement*

"[A]n attorney of record in a pending action who agrees to the settlement of [a] case is presumed to have lawful authority to make such an agreement."[53] Heyman testified that while he understood that Shiboleth was actually authorized to enter into the settlement, he understood that he was not vested with that authority. For that reason Heyman testified that he tried "very hard" not to demonstrate an acceptance of the settlement to Wachtel. While it is possible that Heyman's words and actions amounted to a binding expression of acceptance, the court finds it unnecessary to consider that issue since both Shiboleth's authority to settle and his manifestation of acceptance are so clear.

Regardless of Shiboleth's close relationship with Nasser, this court cannot presume that Shiboleth had lawful authority to enter into the settlement agreement because he was not the attorney of record. Instead, the court must look to agency law to determine whether Shiboleth had the authority to bind the defendants to the agreement. Since Shiboleth testified that he agreed to the settlement, Shiboleth's authority is the only issue for this court to decide.

. . .

In the normal course of business dealing, there are three separate sources of an agency relationship. First, actual authority is expressly granted authority either orally or in writing. Second, implied authority is a derivation of actual authority and often means "actual authority either (1) to do what is necessary, usual, and proper to accomplish or perform an agent's express responsibilities or (2) to act in a manner in which an agent believes the principal wishes the agent to act based on the agent's reasonable interpretation of the principal's manifestation in light of the principal's objectives and other facts known to the agent."[60] Third, apparent authority "is such power as a principal holds his [a]gent out as possessing or permits him to exercise under such circumstances as to preclude a denial of its existence."[61] The plaintiffs claim that there is sufficient evidence to support a finding that Shiboleth was vested with all three sources of authority to enter into the settlement.

53. Aiken v. Nat'l Fire Safety Counselors, 127 A.2d 473, 475 (Del.Ch.1956).

60. RESTATEMENT (THIRD) OF AGENCY § 2.01 (2006).

61. [Liberty Mut. Ins. Co. v. Enjay, 316 A.2d 219 (Del.Super.Ct.1974).]

1. *Actual Authority*

With respect to actual authority, Shiboleth and Heyman testified that Nasser granted Shiboleth authority to settle the litigation. At his deposition, Shiboleth testified that he "clearly" had the authority to agree to the settlement "[b]ased on what [he] heard many times from Albert Nasser." According to Shiboleth, Nasser told him, with regard to signing the settlement agreement, "do what you want or what you understand." Shiboleth, based on 20 years of representing Nasser and having settled numerous cases for him, understood this to mean that he was "authorized to settle the case." Shiboleth also testified that he spoke with Nasser after Dweck capitulated on the cap provision and that Nasser was "ecstatic" and willing to settle upon receipt of an executed agreement. While Nasser testified that he never authorized Shiboleth to bind him to a settlement agreement, on direct examination Nasser stated that he instructed Shiboleth that "he can talk in my name" in settling the litigation. In addition, in his February 18 letter, Shiboleth reminded Nasser of his authority and identified seven different occasions when Nasser agreed to the settlement.[67]

. . .

Nasser argues that since the settlement agreement includes terms that he considers "non-negotiable," it is unenforceable. ... [However,] Nasser consistently told Shiboleth and Heyman that he would "blindly" sign a settlement at their direction. ... Thus, regardless of Nasser's objection to these terms, he is bound by the settlement agreement approved by Shiboleth.

... Heyman was aware of these purportedly "non-negotiable" terms, yet Nasser did not object to them because he told Heyman and Shiboleth that he would no longer "interpose those issues as objections." ...

2. *Implied Authority*

Regardless of Nasser's purported understanding that he expressly reserved the right to sign off on the settlement agreement, his actions in connection with the settlement negotiations and his course of dealings with Shiboleth over 20 years make clear that Shiboleth had at least implied authority to settle the litigation. As previously noted, implied authority is a form of apparent* authority that can extend the scope of the agency relationship under certain circumstances. More specifically:

67. It is important to note that Shiboleth's testimony and the corroborating statements in his February 18 letter are entirely credible given his long-standing and continuing close personal and business relationship with Nasser. Shiboleth has a clear personal and economic incentive to protect Nasser in this action. Indeed, in his February 18 letter, Shiboleth states: "I am not going to volunteer this information, however I do not see any way out of telling the truth in court if I am subpoenaed."

* [Eds.—The court stated above that "implied authority is a derivation of actual authority." The reference to apparent authority here presumably is a typographical error.]

> [I]mplied authority is authority that the agent reasonably believes he has as a result of the principal's actions. This may be proved by evidence of acquiescence [of the principal] with knowledge of the agent's acts, and such knowledge and acquiescence may be shown by evidence of the agent's course of dealing for so long a period of time that acquiescence may be assumed.[83]

Nasser directed Shiboleth to settle the action and permitted him to speak "in his name." Moreover, he told Shiboleth that he would execute any agreement that Shiboleth and Heyman presented to him. Given this behavior and Shiboleth's long-standing close personal and business relationship with Nasser, it was reasonable for Shiboleth to assume he was authorized to settle the litigation. At his deposition, Shiboleth testified that he had settled many cases for Nasser in the past and that . . . it was always his "role" to settle cases for Nasser. . . . When Shiboleth entered into the settlement agreement on the terms he knew to be acceptable to Nasser he understandably thought Nasser's signature was a "formality."

3. *Apparent Authority*

Finally, while such a determination is not necessary to grant the plaintiffs' motion, Nasser is also likely bound by Shiboleth's actions based on apparent authority. " 'A principal is bound by an agent's apparent authority which he knowingly permits the agent to assume of which he holds the agent out as possessing.' "[90] As Shiboleth recounted in his letter to Nasser:

> [You] should also remember that you have told not only Michael Goodman, [Dweck's] husband, but also Isaac and Haim, her brothers and said to me and to [Heyman] at various times that you did not intend to read the Settlement Agreement. You added that when [Heyman] and I will tell you to sign the agreement you shall do so.

. . .

IV.

For the foregoing reasons the motion to enforce the settlement agreement is GRANTED. . . .

ANALYSIS

1. What should Nasser have done to avoid this problem?

2. In assessing whether Shiboleth had actual authority, why is it relevant that he had "20 years of representing Nasser" and had "settled numerous cases for him"?

3. Restatement (Third) of Agency § 2.03 states:

83. Montgomery v. Achenbach, 2007 WL 3105812, at *2 (Del.Super. Ct. July 26, 2007) (alteration in original).

90. Liberty, 316 A.2d at 223. . . .

> Apparent authority is the power held by an agent or other actor to affect a principal's legal relations with third parties when a third party reasonably believes the actor has authority to act on behalf of the principal and that belief is traceable to the principal's manifestations.

Who is the relevant third party here? What were Nasser's manifestations that would leave the relevant third party to believe Shiboleth had apparent authority to settle the case?

4. Why is an attorney of record presumed to have authority to settle the case? Typically, upon employment, an attorney's general powers to manage the procedural aspects of a client's case include implied actual authority to engage in settlement negotiations with opposing counsel. The attorney's authority to open settlement negotiations, however, does not extend to reaching an actual settlement. The client retains legal control over the subject matter of litigation and important decisions affecting the client's substantial rights. Thus, the employment relationship alone does not provide an attorney with authority to settle a case on behalf of the client. Restatement (Third) of the Law Governing Lawyers § 21 (2000). Why then did the Delaware court adopt this presumption?

Three–Seventy Leasing Corporation v. Ampex Corporation

528 F.2d 993 (5th Cir.1976).

Three–Seventy Leasing Corporation (370) seeks damages from Ampex Corporation (Ampex) for breach of a contract to sell six computer core memories. The district court, sitting without a jury, found that there was an enforceable contract between 370 and Ampex. . . .

Three–Seventy Leasing Corporation was formed by Joyce, at all times its only active employee, for the purpose of purchasing computer hardware from various manufacturers for lease to end-users. In August of 1972, Kays, a salesman of Ampex and friend of Joyce, initiated discussions with Joyce regarding the possibility of 370 purchasing computer equipment from Ampex. A meeting was arranged between Kays, Joyce, and Mueller, Kays' superior at Ampex. Joyce was informed at this meeting that Ampex could sell to 370 only if 370 could pass Ampex's credit requirements. Joyce informed the two that he did not think this would be a problem.

At approximately the same time, Joyce began negotiations with Electronic Data Systems (EDS), which resulted in EDS's verbal commitment to lease six units of Ampex computer core memory from 370. Desiring to close the two transactions simultaneously, Joyce continued negotiations with Kays. These negotiations resulted in a written document submitted by Kays to Joyce at the direction of Mueller. The document provided for the purchase by Joyce of six core memory units at a price of $100,000 each, with a down payment of $150,000 and the remainder to be paid over a five year period. The document specified that delivery was to be made to EDS.

The document also contained a signature block for a representative of 370 and a signature block for a representative of Ampex.

Joyce received this document about November 3, 1972, and executed it on November 6, 1972. The document was never executed by a representative of Ampex. This document forms the core of the present controversy. 370 argues that the document was an offer to sell by Ampex, which was accepted upon Joyce's signature. Ampex contends that the document was nothing more than a solicitation which became an offer to purchase upon execution by Joyce, and that this offer was never accepted by Ampex. 370 counters by arguing in the alternative that even if the document when signed by Joyce was only an offer to purchase, the offer was later accepted by representatives of Ampex.

The district court, in concluding that there existed an enforceable contract, made no determination as to whether the document described above was an offer to sell accepted by Joyce's signature, or an offer to purchase when signed by Joyce which was later accepted by Ampex.

We reject the first alternative as being without evidentiary support. Elemental principles demand that there be a meeting of the minds and a communication that each party has consented to the terms of the agreement in order for a contract to exist.... There is no evidence, either written or oral, other than the document itself, which shows that Ampex had the requisite intent necessary to the formation of a contract prior to November 6, 1972, the date the document was executed by Joyce. And the document on its face does not supply that intent. Rather, the fact that the document had a signature block for a representative of Ampex which was unsigned at the time it was submitted to Joyce, in the absence of other evidence, negates any interpretation that Ampex intended this to be an offer to Joyce, without any further acts necessary on the part of Ampex.

Thus, the document, when signed by Joyce, at most constituted an offer by him to purchase. In order for there to be a valid contract, we must therefore find some act of acceptance on the part of Ampex.

On November 9, 1972, Mueller issued an intra-office memorandum which stated in part that "[o]n November 3, 1972, Ampex was awarded an Agreement by Three–Seventy Leasing, Dallas, Texas, for the purchase of six (6) ARM–3360 Memory Units," to be installed at EDS. This memorandum further informed those concerned at Ampex of Joyce's request that all contact with 370 be handled through Kays. On November 17, 1972, Kays sent a letter to Joyce which confirmed the delivery dates for the memory units.[2] We conclude, in light of the circumstances surrounding these

2. That letter stated:

Dear John:

With regard to delivery of equipment purchased by Three–Seventy Leasing: Ampex will ship three (3) million bytes of ARM–3360 magnetic core in sufficient time to install 1½ million bytes the weekend of December 16, 1972. The remaining balance of 1½ million bytes will be installed by the weekend of December 30, 1972.

The equipment will be installed in Camphill, Pennsylvania at a predetermined site by Electronic Data Systems.

negotiations, that the district court was not clearly erroneous when it found that Kays had apparent authority to accept Joyce's offer on behalf of Ampex, and we further conclude that the November 17 letter, in these circumstances, can reasonably be interpreted to be an acceptance.

An agent has apparent authority sufficient to bind the principal when the principal acts in such a manner as would lead a reasonably prudent person to suppose that the agent had the authority he purports to exercise.... Further, absent knowledge on the part of third parties to the contrary, an agent has the apparent authority to do those things which are usual and proper to the conduct of the business which he is employed to conduct....

In this case, Kays was employed by Ampex in the capacity of a salesman. It is certainly reasonable for third parties to presume that one employed as salesman has the authority to bind his employer to sell. And Ampex did nothing to dispel this reasonable inference. Rather, its actions and inactions provided a further basis for this belief. First, Kays, at the direction of Mueller, submitted the controversial document to Joyce for signature. The document contained a space for signature by an Ampex representative. Nothing in the document suggests that Kays did not have authority to sign it on behalf of Ampex.[3] Second, Joyce indicated to Kays and Mueller that he wished all communications to be channeled through Kays. Mueller agreed, and acknowledged this in the November 9 intra-company memorandum. Neither Mueller, nor anyone else at Ampex ever informed Joyce that communication regarding acceptance would come through anyone other than Kays. In light of this request and Ampex's agreement, Joyce could reasonably expect that Kays would speak for the company.

Various individuals in the Ampex hierarchy testified at trial that only the contract manager or other supervisor in the company's contract department had authority to sign a contract on behalf of Ampex. However, there is no evidence that this limitation was ever communicated to Joyce in any manner. Absent knowledge of such a limitation by third parties, that limitation will not bar a claim of apparent authority.

Thus, when Joyce received Kays' November 17 letter, he had every reason to believe, based upon Ampex's prior actions, that Kays spoke on behalf of the company. We thus agree with the district court's finding that Kays had apparent authority to act for Ampex.

Having determined that Kays had apparent authority to bind Ampex, we further conclude that his letter of November 17, in light of the pattern of negotiations, could reasonably be interpreted as a promise to ship the six memory units on the dates specified in the letter and on the terms

Regards,

Thomas C. Kays

Sales Representative

3. It would have been an easy matter to provide in the document that only certain officers of Ampex had authority to sign on its behalf. Any inference to the contrary resulting from Ampex's failure to specify such a limitation must weigh against Ampex.

previously set out in the document executed by Joyce and submitted to Ampex. The district court's finding that a contract was formed is therefore not clearly erroneous.

ANALYSIS

1. What was Joyce's function? Was he a sales representative of Ampex? A purchasing agent of EDS? Neither?

2. What was Kays's position and function?

3. Kays did not have authority to enter into the contract. Do you find this surprising as to (a) the agreement to sell the core memory units or (b) the agreement to extend credit, or both?

4. What were the defendant's manifestations that supported a finding of apparent authority?

PLANNING AND ECONOMIC EFFICIENCY

1. What should Ampex have done to protect itself against the problem that arose in this case?

2. What could Joyce have done to protect himself?

3. In light of your answer to questions 1 and 2, does the result in the case place responsibility for avoiding loss on the person with the lower cost of doing so?

QUESTION

As we have seen, contracts entered into on the principal's behalf by an agent lacking actual authority can still be binding on the principal if the agent has apparent authority. Apparent authority only exists, however, "when a third party reasonably believes the actor has authority to act on behalf of the principal and that belief is traceable to the principal's manifestations." Restatement (Third) of Agency § 2.03. What happens if the agent is acting on behalf of a so-called undisclosed principal? ("A principal is undisclosed if, when an agent and a third party interact, the third party has no notice that the agent is acting for a principal." Id. § 1.04(2)(b).) If the third party has no idea that a principal exists, how can there be the manifestation required for apparent authority? The next case considers that problem.

Watteau v. Fenwick

[1893] 1 Queen's Bench 346 (1892).

From the evidence it appeared that one Humble had carried on business at a beerhouse called the Victoria Hotel, at Stockton-on-Tees, which business he had transferred to the defendants, a firm of brewers,

some years before the present action. After the transfer of the business, Humble remained as defendants' manager; but the licence was always taken out in Humble's name, and his name was painted over the door. Under the terms of the agreement made between Humble and the defendants, the former had no authority to buy any goods for the business except bottled ales and mineral waters; all other goods required were to be supplied by the defendants themselves. The action was brought to recover the price of goods delivered at the Victoria Hotel over some years, for which it was admitted that the plaintiff gave credit to Humble only: they consisted of cigars, bovril, and other articles. The learned judge allowed the claim for the cigars and bovril only, and gave judgment for the plaintiff for 22*l.* 12*s*. 6*d.* The defendants appealed.

1892. Nov. 19. *Finlay, Q.C.* (*Scott Fox,* with him), for the defendants. The decision of the county court judge was wrong. The liability of a principal for the acts of his agent, done contrary to his secret instructions, depends upon his holding him out as his agent—that is, upon the agent being clothed with an apparent authority to act for his principal. Where, therefore, a man carries on business in his own name through a manager, he holds out his own credit, and would be liable for goods supplied even where the manager exceeded his authority. But where, as in the present case, there is no holding out by the principal, but the business is carried on in the agent's name and the goods are supplied on his credit, a person wishing to go behind the agent and make the principal liable must show an agency in fact.

[Lord Coleridge, C.J. Cannot you, in such a case, sue the undisclosed principal on discovering him?]

Only where the act done by the agent is within the scope of his agency; not where there has been an excess of authority. Where any one has been held out by the principal as his agent, there is a contract with the principal by estoppel, however much the agent may have exceeded his authority; where there has been no holding out, proof must be given of an agency in fact in order to make the principal liable.

Boydell Houghton, for the plaintiff. The defendants are liable in the present action. They are in fact undisclosed principals, who instead of carrying on the business in their own names employed a manager to carry it on for them, and clothed him with authority to do what was necessary to carry on the business. The case depends upon the same principles as *Edmunds v. Bushell,* where the manager of a business which was carried on in his own name with the addition "and Co." accepted a bill of exchange, notwithstanding a stipulation in the agreement with his principal that he should not accept bills; and the Court held that the principal was liable to an indorsee who took the bill without any knowledge of the relations between the principal and agent. In that case there was no holding out of the manager as an agent; it was the simple case of an agent being allowed to act as the ostensible principal without any disclosure to the world of there being any one behind him. Here the defendants have so conducted themselves as to enable their agent to hold himself out to the

world as the proprietor of their business, and they are clearly undisclosed principals: *Ramazotti v. Bowring*. All that the plaintiff has to do, therefore, in order to charge the principals, is to show that the goods supplied were such as were ordinarily used in the business—that is to say, that they were within the reasonable scope of the agent's authority. . . .

Dec. 12. Lord Coleridge, C.J. The judgment which I am about to read has been written by my brother Wills, and I entirely concur in it.

■ WILLS, J. The plaintiff sues the defendants for the price of cigars supplied to the Victoria Hotel, Stockton-upon-Tees. The house was kept, not by the defendants, but by a person named Humble, whose name was over the door. The plaintiff gave credit to Humble, and to him alone, and had never heard of the defendants. The business, however, was really the defendants', and they had put Humble into it to manage it for them, and had forbidden him to buy cigars on credit. The cigars, however, were such as would usually be supplied to and dealt in at such an establishment. The learned county court judge held that the defendants were liable. I am of opinion that he was right.

There seems to be less of direct authority on the subject than one would expect. But I think that the Lord Chief Justice during the argument laid down the correct principle, viz., once it is established that the defendant was the real principal, the ordinary doctrine as to principal and agent applies that the principal is liable for all the acts of the agent which are within the authority usually confided to an agent of that character, notwithstanding limitations, as between the principal and the agent, put upon that authority. It is said that it is only so where there has been a holding out of authority—which cannot be said of a case where the person supplying the goods knew nothing of the existence of a principal. But I do not think so. Otherwise, in every case of undisclosed principal, or at least in every case where the fact of there being a principal was undisclosed, the secret limitation of authority would prevail and defeat the action of the person dealing with the agent and then discovering that he was an agent and had a principal.

But in the case of a dormant partner it is clear law that no limitation of authority as between the dormant and active partner will avail the dormant partner as to things within the ordinary authority of a partner. The law of partnership is, on such a question, nothing but a branch of the general law of principal and agent, and it appears to me to be undisputed and conclusive on the point now under discussion.

The principle laid down by the Lord Chief Justice, and acted upon by the learned county court judge, appears to be identical with that enunciated in the judgments of Cockburn, C.J., and Mellor, J., in Edmunds v. Bushell, the circumstances of which case, though not identical with those of the present, come very near to them. There was no holding out, as the plaintiff knew nothing of the defendant. I appreciate the distinction drawn by Mr. Finlay in his argument, but the principle laid down in the judgments referred to, if correct, abundantly covers the present case. I cannot find that any doubt has ever been expressed that it is correct, and I think it is

right, and that very mischievous consequences would often result if that principle were not upheld.

In my opinion this appeal ought to be dismissed with costs.

Appeal dismissed.

NOTE

The Restatement (Second) of Agency included a broad concept called ''inherent agency power,'' which Section 8A of the Restatement defined as follows:

> Inherent agency power is a term used in the restatement of this subject to indicate the power of an agent which is derived not from authority, apparent authority or estoppel, but solely from the agency relation and exists for the protection of persons harmed by or dealing with a servant or other agent.

The Restatement (Second) of Agency § 194 states that an undisclosed principal is liable for acts of an agent ''done on his account, if usual or necessary in such transactions, although forbidden by the principal.''

Under the Restatement (Second) of Agency § 195, ''An undisclosed principal who entrusts an agent with the management of his business is subject to liability to third persons with whom the agent enters into transactions usual in such business and on the principal's account, although contrary to the directions of the principal.''

Although some set of rules for dealing with cases like *Watteau* is necessary, the vaguely defined concept of inherent agency power was a poor tool for doing so.

The Restatement (Third) of Agency rejected the concept of inherent agency power in favor of a rule directly targeted at cases like *Watteau*:

> § 2.06 Liability of Undisclosed Principal
>
> (1) An undisclosed principal is subject to liability to a third party who is justifiably induced to make a detrimental change in position by an agent acting on the principal's behalf and without actual authority if the principal, having notice of the agent's conduct and that it might induce others to change their positions, did not take reasonable steps to notify them of the facts.
>
> (2) An undisclosed principal may not rely on instructions given an agent that qualify or reduce the agent's authority to less than the authority a third party would reasonably believe the agent to have under the same circumstances if the principal had been disclosed.

The comments to § 2.06 claim that it reflects the rule of *Watteau* and Restatement (Second) § 195, but the Restatement (Third) rule in fact may be substantially narrower. It concludes with the qualification that the principal is liable ''if the principal, having notice of the agent's conduct and that it might induce others to change their position, did not take reason-

able steps to notify them of the facts.'' This makes the rule seem more akin to estoppel than to the old inherent agency power. It seems that the defendants in *Watteau* were not aware that Humble was buying cigars from Watteau and therefore would not be liable under the Restatement (Third) rule—contrary to the actual result in *Watteau*.

ANALYSIS

1. Is there any basis in this case for holding the defendants liable on a theory of apparent authority?

2. Humble had authority to buy ''ales and mineral waters'' from third parties but not ''cigars, bovril, and other articles.'' (Bovril is a nonalcoholic drink.) The court claims that ''mischievous consequences'' would result from a decision for the defendants. What are those mischievous consequences? In responding to this question, ask yourself if there is any basis for distinguishing between ales and mineral waters, on the one hand, and cigars and bovril, on the other hand. Bear in mind that the plaintiffs seek recovery from the personal assets of the defendants, not just the assets (if any) invested by the defendants in the Victoria Hotel.

3. The Restatement (Third) offers the following hypothetical:

> P Corporation produces musical recordings and employs A to engage performers. A's counterparts in the recording industry have authority to make unconditional contracts with performers, but B, who is A's superior within P Corporation, directs A to condition all payments to performers on the sales revenues that P Corporation receives from their work. B's direction to A is not known outside P Corporation.

On P's behalf, A enters into a contract with T that is unconditional. T has never met B or anyone else who works for P other than A. Is there a manifestation by P on these facts sufficient to establish apparent authority or do you need some concept like inherent agency power to deal with these sort of cases? See Restatement (Third) § 1.03:

> A person manifests assent or intention through written or spoken words or other conduct.

REVIEW PROBLEMS

1. Suppose Professor Paula Potter has a student research assistant, Allie. Allie is about to graduate and Paula asks her to hire a successor. Paula says that she is willing to pay $9 per hour for 100 hours of work. Allie finds another student, Zelda, who wants the job but points out that the going rate is $10 per hour. Allie says, ''Well, if that's the going rate, that's O.K. You have the job.'' Thereafter Paula tells Zelda that she will pay only $9 and Zelda (who has turned down other job offers) seeks to enforce the contract that she thinks she has for $10 per hour. Who wins? Why? Suppose Paula had said to Allie, ''Find the best available person, tell that person what the job is and how much I am willing to pay, and send her

or him to me so I can offer the job if I am satisfied with your choice.'' Same result?

2. Suppose you are the lawyer for M/M Records, a small record company with good management and exciting prospects. The head of the company, Millie Mogul, has just hired a woman named Sheena Swiftie, who is friendly with a number of leading recording stars and hopes some day to establish herself as an independent agent in the entertainment industry, but wants to start out as an employee (largely because she needs a steady income). Sheena's job is to line up recording stars to make recordings for M/M Records. Sheena will be paid a salary plus bonuses based on what she produces. Millie tells you, ''Sheena seems a bit flaky, but I think she can deliver.'' In recent years, in the recording business, it has become common for record companies to offer substantial guarantees to star performers, but M/M Records does not do so, because it cannot afford to take the risk. Instead, it offers higher royalties than its competitors do. Millie wants Sheena to have authority to pin artists down to contracts when the moment is right, but has emphasized to Sheena the M/M Records policy of no guarantees. Millie asks you if she has anything to worry about and, if she does, what suggestions you might have. You are aware that Millie tends to resent lawyers in general because she thinks they are ''deal breakers.'' What is your response to her?

B. Ratification

Botticello v. Stefanovicz

177 Conn. 22, 411 A.2d 16 (1979).

This case concerns the enforceability of an agreement for the sale of real property when that agreement has been executed by a person owning only an undivided half interest in the property. . . .

The finding of the trial court discloses the following undisputed facts: The defendants, Mary and Walter Stefanovicz (hereinafter ''Mary'' and ''Walter'') in 1943 acquired as tenants in common a farm situated in the towns of Colchester and Lebanon. In the fall of 1965, the plaintiff, Anthony Botticello, became interested in the property. When he first visited the farm, Walter advised him that the asking price was $100,000. The following January, the plaintiff again visited the farm and made a counteroffer of $75,000. At that time, Mary stated that there was ''no way'' she could sell it for that amount. Ultimately the plaintiff and Walter agreed upon a price of $85,000 for a lease with an option to purchase; during these negotiations, Mary stated that she would not sell the property for less than that amount.

The informal agreement was finalized with the assistance of counsel for both Walter and the plaintiff. The agreement was drawn up by Walter's attorney after consultation with Walter and the plaintiff; it was then sent to, and modified by, the plaintiff's attorney. The agreement was signed by Walter and by the plaintiff. Neither the plaintiff nor his attorney, nor

Walter's attorney, was then aware of the fact that Walter did not own the property outright. The plaintiff, although a successful businessman with considerable experience in real estate never requested his attorney to do a title search of any kind, and consequently no title search was done. Walter never represented to the plaintiff or the plaintiff's attorney, or to his own attorney, that he was acting for his wife, as her agent. Mary's part ownership came to light in 1968, when a third party sought an easement over the land in question.

Shortly after the execution of the lease and option-to-purchase agreement, the plaintiff took possession of the property. He made substantial improvements on the property and, in 1971, properly exercised his option to purchase. When the defendants refused to honor the option agreement, the plaintiff commenced the present action against both Mary and Walter, seeking specific performance, possession of the premises, and damages.

The trial court found the issues for the plaintiff and ordered specific performance of the option-to-purchase agreement. In their appeal, the defendants [claim] that Mary was never a party to the agreement, and its terms may therefore not be enforced as to her. . . .

The plaintiff alleged, and the trial court agreed, that although Mary was not a party to the lease and option-to-purchase agreement, its terms were nonetheless binding upon her because Walter acted as her authorized agent in the negotiations, discussions, and execution of the written agreement. The defendants have attacked several findings of fact and conclusions of law, claiming that the underlying facts and applicable law do not support the court's conclusion of agency. We agree.

Agency is defined as " 'the fiduciary relationship which results from manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act. . . .' Restatement (Second), 1 Agency § 1." McLaughlin v. Chicken Delight, Inc., 164 Conn. 317, 322, 321 A.2d 456 (1973). Thus, the three elements required to show the existence of an agency relationship include: (1) a manifestation by the principal that the agent will act for him; (2) acceptance by the agent of the undertaking; and (3) an understanding between the parties that the principal will be in control of the undertaking. Restatement (Second), 1 Agency § 1, comment b (1958).

The existence of an agency relationship is a question of fact. The burden of proving agency is on the plaintiff and it must be proven by a fair preponderance of the evidence. Marital status cannot in and of itself prove the agency relationship. Nor does the fact that the defendants owned the land jointly make one the agent for the other.

The facts set forth in the court's finding are wholly insufficient to support the court's conclusion that Walter acted as Mary's authorized agent in the discussions concerning the sale of their farm and in the execution of the written agreement. . . . The finding indicates that when the farm was purchased, and when the couple transferred property to their sons, Walter handled many of the business aspects, including making

payments for taxes, insurance, and mortgage. The finding also discloses that Mary and Walter discussed the sale of the farm, and that Mary remarked that she would not sell it for $75,000, and would not sell it for less than $85,000. A statement that one will not sell for less than a certain amount is by no means the equivalent of an agreement to sell for that amount. Moreover, the fact that one spouse tends more to business matters than the other does not, absent other evidence of agreement or authorization, constitute the delegation of power as to an agent. What is most damaging to the plaintiff's case is the court's uncontradicted finding that, although Mary may have acquiesced in Walter's handling of many business matters, Walter never signed any documents as agent for Mary prior to 1966. Mary had consistently signed any deed, mortgage, or mortgage note in connection with their jointly held property.

. . .

The plaintiff argues, alternatively, that even if no agency relationship existed at the time the agreement was signed, Mary was bound by the contract executed by her husband because she ratified its terms by her subsequent conduct. The trial court accepted this alternative argument as well, concluding that Mary had ratified the agreement by receiving and accepting payments from the plaintiff, and by acquiescing in his substantial improvements to the farm. The underlying facts, however, do not support the conclusion of ratification.

Ratification is defined as ''the affirmance by a person of a prior act which did not bind him but which was done or professedly done on his account.'' Restatement (Second), 1 Agency § 82 (1958). Ratification requires ''acceptance of the results of the act with an intent to ratify, and with full knowledge of all the material circumstances.'' Ansonia v. Cooper, 64 Conn. 536, 544, 30 A. 760 (1894). . . .

The finding neither indicates an intent by Mary to ratify the agreement, nor establishes her knowledge of all the material circumstances surrounding the deal. At most, Mary observed the plaintiff occupying and improving the land, received rental payments from the plaintiff from time to time, knew that she had an interest in the property, and knew that the use, occupancy, and rentals were pursuant to a written agreement she had not signed. None of these facts is sufficient to support the conclusion that Mary ratified the agreement and thus bound herself to its terms. It is undisputed that Walter had the power to lease his own undivided one-half interest in the property and the facts found by the trial court could be referable to that fact alone. Moreover, the fact that the rental payments were used for ''family'' purposes indicates nothing more than one spouse providing for the other.

The plaintiff makes the further argument that Mary ratified the agreement simply by receiving its benefits and by failing to repudiate it. See Restatement (Second), 1 Agency § 98 (1958). The plaintiff fails to recognize that before the receipt of benefits may constitute ratification, the other requisites for ratification must first be present. ''Thus if the original

transaction was not purported to be done on account of the principal, the fact that the principal receives its proceeds does not make him a party to it.'' Restatement (Second), 1 Agency § 98, comment f (1958). Since Walter at no time purported to be acting on his wife's behalf, as is essential to effective subsequent ratification, Mary is not bound by the terms of the agreement, and specific performance cannot be ordered as to her.

. . .

We turn now to the question of relief. In view of our holding that Mary never authorized her husband to act as her agent for any purpose connected with the lease and option-to-purchase agreement, recovery against her is precluded. As to Walter, the fact that his ownership was restricted to an undivided one-half interest in no way limited his capacity to contract. He contracted to convey full title and for breach of that contract he may be held liable. The facts of the case are sufficient to furnish a basis for relief to the plaintiff by specific performance or by damages.

There is error as to the judgment against the defendant Mary Stefanovicz; the judgment as to her is set aside and the case remanded with direction to render judgment in her favor. As to the defendant Walter Stefanovicz, there is error only as to the remedy ordered. The judgment as to him is set aside and the case remanded for a new trial limited to the form of relief.

ANALYSIS AND PROBLEMS

Ratification is a means by which the principal can say, ''my agent didn't have the right to enter into this contract, but I'm glad she did so. Accordingly, I'll affirm the transaction and agree to be bound by the contract.'' Any ratification case involves two critical questions: First, what types of acts constitute an affirmation by the principal? Second, what effect should we give to that affirmation?

Obviously, one can expressly affirm a contract. The principal can say something like: ''Gosh, what a wonderful deal. I'll go forward with it.'' Harder questions arise in implied affirmation cases. Consider the following examples:

1. Suppose Pam is a writer. Her husband Alex enters into a contract with ABC Book Publishers under which Pam's next book is to go to ABC. Pam gets a check from ABC, representing the advance on the contract, which she cashes. She then spends the proceeds on a new computer for her office. Some months later Pam tries to sell her new book to another publisher. ABC claims the book. Pam correctly points out that Alex had no authority to act as her agent. ABC responds by saying that she had ratified the contract. Who wins?

2. Suppose Pam argues that she thought the check was for royalties on one of her previous books, which ABC had published. She asserts that she neither knew nor had reason to know that it was an advance on her next book. Who wins?

3. Alan is a slightly deranged fan of Pam's books. Alan goes to a local landscaping company. Pretending to be Pam's butler, he asks the company to cut Pam's grass. Pam arrives home just after the men finished up. Pam thanks them and goes inside. The company sues her for refusing to pay. Pam correctly points out that Alan had no authority to enter into this contract. The company claims she ratified the contract by accepting and retaining its benefits. Who wins?

4. Paula is an investor who has opened an account at a local brokerage. She instructs Al, her broker, only to purchase U.S. treasury bonds for the account. Al disregards those instructions and buys stock in a new very risky high-tech company. Paula does not learn about this until her first monthly statement arrives. She decides to take a wait and see attitude. When her next monthly statement arrives she notices that the stock's price has dropped rather drastically. She calls Al and demands that he close the account and reimburse her for the money she lost. She correctly claims he had no authority to buy the stock. Al closes the account, but refuses to make Paula's losses good. Al claims Paula ratified the purchase by waiting. Who is right: Paula or Al?

5. Paula owns a mansion called Whiteacre Manor. Alan, having no authority to do so, enters into a sale contract with Ted by which Ted is to purchase Whiteacre Manor. The next day the mansion burns to the ground. Paula then expressly affirms the contract. Ted says she's too late. Who wins?

C. ESTOPPEL

Hoddeson v. Koos Bros.

47 N.J.Super. 224, 135 A.2d 702 (App.Div.1957).

The occurrence which engages our present attention is a little more than conventionally unconventional in the common course of trade. Old questions appear in new styles. A digest of the story told by Mrs. Hoddeson will be informative and perhaps admonitory to the unwary shopper.

The plaintiff Mrs. Hoddeson was acquainted with the spacious furniture store conducted by the defendant, Koos Bros., a corporation, at No. 1859 St. George Avenue in the City of Rahway. On a previous observational visit, her eyes had fallen upon certain articles of bedroom furniture which she ardently desired to acquire for her home. It has been said that "the sea hath bounds but deep desire hath none." Her sympathetic mother liberated her from the grasp of despair and bestowed upon her a gift of $165 with which to consummate the purchase.

It was in the forenoon of August 22, 1956 that Mrs. Hoddeson, accompanied by her aunt and four children, happily journeyed from her home in South River to the defendant's store to attain her objective. Upon entering, she was greeted by a tall man with dark hair frosted at the temples and clad in a light gray suit. He inquired if he could be of

assistance, and she informed him specifically of her mission. Whereupon he immediately guided her, her aunt, and the flock to the mirror then on display and priced at $29 which Mrs. Hoddeson identified, and next to the location of the designated bedroom furniture which she had described.

Upon confirming her selections the man withdrew from his pocket a small pad or paper upon which he presumably recorded her order and calculated the total purchase price to be $168.50. Mrs. Hoddeson handed to him the $168.50 in cash. He informed her the articles other than those on display were not in stock, and that reproductions would upon notice be delivered to her in September. Alas, she omitted to request from him a receipt for her cash disbursement. The transaction consumed in time a period from 30 to 40 minutes.

Mrs. Hoddeson impatiently awaited the delivery of the articles of furniture, but a span of time beyond the assured date of delivery elapsed, which motivated her to inquire of the defendant the cause of the unexpected delay. Sorrowful, indeed, was she to learn from the defendant that its records failed to disclose any such sale to her and any such monetary credit in payment.

. . .

Although the amount of money involved is relatively inconsiderable, the defendant has resolved to incur the expense of this appeal. . . .

It eventuated that Mrs. Hoddeson and her aunt were subsequently unable positively to recognize among the defendant's regularly employed salesmen the individual with whom Mrs. Hoddeson had arranged for the purchase, although when she and her aunt were afforded the opportunities to gaze intently at one of the five salesmen assigned to that department of the store, both indicated a resemblance of one of them to the purported salesman, but frankly acknowledged the incertitude of their identification. The defendant's records revealed that the salesman bearing the alleged resemblance was on vacation and hence presumably absent from the store during the week of August 22, 1956.

As you will at this point surmise, the insistence of the defendant at the trial was that the person who served Mrs. Hoddeson was an impostor deceitfully impersonating a salesman of the defendant without the latter's knowledge.

. . .

Where a party seeks to impose liability upon an alleged principal on a contract made by an alleged agent, as here, the party must assume the obligation of proving the agency relationship. It is not the burden of the alleged principal to disprove it.

Concisely stated, the liability of a principal to third parties for the acts of an agent may be shown by proof disclosing (1) express or real authority which has been definitely granted; (2) implied authority, that is, to do all that is proper, customarily incidental and reasonably appropriate to the exercise of the authority granted; and (3) apparent authority, such as

where the principal by words, conduct, or other indicative manifestations has ''held out'' the person to be his agent.

Obviously the plaintiffs' evidence in the present action does not substantiate the existence of any basic express authority or project any question implicating implied authority. The point here debated is whether or not the evidence circumstantiates the presence of apparent authority, and it is at this very point we come face to face with the general rule of law that the apparency and appearance of authority must be shown to have been created by the manifestations of the alleged principal, and not alone and solely by proof of those of the supposed agent. Assuredly the law cannot permit apparent authority to be established by the mere proof that a mountebank in fact exercised it.

. . .

Let us hypothesize for the purposes of our present comments that the acting salesman was not in fact an employee of the defendant, yet he behaved and deported himself during the stated period in the business establishment of the defendant in the manner described by the evidence adduced on behalf of the plaintiffs, would the defendant be immune as a matter of law from liability for the plaintiffs' loss? The tincture of estoppel that gives color to instances of apparent authority might in the law operate likewise to preclude a defendant's denial of liability. It matters little whether for immediate purposes we entitle or characterize the principle of law in such cases as ''agency by estoppel'' or ''a tortious dereliction of duty owed to an invited customer.'' That which we have in mind are the unique occurrences where solely through the lack of the proprietor's reasonable surveillance and supervision an impostor falsely impersonates in the place of business an agent or servant of his. Certainly the proprietor's duty of care and precaution for the safety and security of the customer encompasses more than the diligent observance and removal of banana peels from the aisles. Broadly stated, the duty of the proprietor also encircles the exercise of reasonable care and vigilance to protect the customer from loss occasioned by the deceptions of an apparent salesman. The rule that those who bargain without inquiry with an apparent agent do so at the risk and peril of an absence of the agent's authority has a patently impracticable application to the customers who patronize our modern department stores.

Our concept of the modern law is that where a proprietor of a place of business by his dereliction of duty enables one who is not his agent conspicuously to act as such and ostensibly to transact the proprietor's business with a patron in the establishment, the appearances being of such a character as to lead a person of ordinary prudence and circumspection to believe that the impostor was in truth the proprietor's agent, in such circumstances the law will not permit the proprietor defensively to avail himself of the impostor's lack of authority and thus escape liability for the consequential loss thereby sustained by the customer.

. . .

In reversing the judgment under review, the interests of justice seem to us to recommend the allowance of a new trial with the privilege accorded the plaintiffs to reconstruct the architecture of their complaint appropriately to project for determination the justiciable issue to which, in view of the inquisitive object of the present appeal, we have alluded. . . .

Reversed and new trial allowed.

ANALYSIS

1. This is one of several cases in this text in which parties vigorously litigated disputes involving seemingly trivial amounts. Why on earth would Koos Bros. have gone to such lengths and expense?

2. What will plaintiff need to prove on remand to justify an estoppel-based verdict in her favor?

3. What result if plaintiff and the alleged imposter had merely entered into a contract for the purchase of the furniture, rather than exchanging money?

D. Agent's Liability on the Contract

Atlantic Salmon A/S v. Curran

32 Mass.App.Ct. 488, 591 N.E.2d 206 (1992).

These are the plaintiffs' appeals from a Superior Court judgment for the defendant. The issue presented is as to the personal liability of an agent who at the relevant times was acting on behalf of a partially disclosed or unidentified principal. . . .

The facts are not in dispute, ... The defendant began doing business with the plaintiffs, Salmonor A/S (Salmonor) and Atlantic Salmon A/S (Atlantic), Norwegian corporations and exporters of salmon, in 1985 and 1987, respectively. At all times, the defendant dealt with the plaintiffs as a representative of "Boston International Seafood Exchange, Inc.," or "Boston Seafood Exchange, Inc." The salmon purchased by the defendant was sold to other wholesalers. Payment checks from the defendant to the plaintiffs were imprinted with the name "Boston International Seafood Exchange, Inc.," and signed by the defendant, using the designation "Treas.," intending thereby to convey the impression that he was treasurer. Wire transfers of payments were also made in the name of Boston International Seafood Exchange, Inc. The defendant gave the plaintiffs' representatives business cards which listed him as "marketing director" of "Boston International Seafood Exchange, Inc." Advertising placed by the defendant appeared in trade journals under both the names "Boston Seafood Exchange, Inc.," and "Boston International Seafood Exchange, Inc." (indicating in one instance as to the latter that it was "Est: 1982"). At the relevant times, no such Massachusetts or foreign corporation had been formed by the defendant or had existed.

On May 31, 1977, a Massachusetts corporation named ''Marketing Designs, Inc.,'' was organized. It was created for the purpose of selling motor vehicles. As of 1983, the defendant was the president, treasurer, clerk, a director and the sole stockholder of that corporation. The extent of activity or solvency of the corporation is not shown on the record. On October 19, 1983, however, Marketing Designs, Inc., was dissolved, apparently for failure to make requisite corporate filings.... On December 4, 1987, a certificate was filed with the city clerk of Boston declaring that Marketing Designs, Inc. (then dissolved), was conducting business under the name of Boston Seafood Exchange (not with the designation ''Inc.'' and not also under the name Boston International Seafood Exchange, Inc.)....

Salmonor is owed $101,759.65 and Atlantic $153,788.50 for salmon sold to a business known as Boston International Seafood Exchange or Boston Seafood Exchange during 1988. Marketing Designs, Inc., was dissolved at the time the debt was incurred. In that year, advertising in a trade journal appeared in the name of ''Boston Seafood Exchange, Inc.,'' and listed the plaintiffs as suppliers, and the defendant delivered to representatives of the plaintiffs his business card on which he was described as ''marketing director'' of ''Boston International Seafood Exchange, Inc.'' On July 8, August 19 and 30, and September 9, 1988, the defendant made checks, imprinted with the name ''Boston International Seafood Exchange, Inc.,'' to one or the other of the plaintiffs as payments for shipments of salmon.

The defendant never informed the plaintiffs of the existence of Marketing Designs, Inc., and the plaintiffs did not know of it until after the commencement of the present litigation on November 25, 1988. Marketing Designs, Inc., was revived for all purposes on December 12, 1988....

In the course of his direct testimony, the defendant said: ''We do business in seafood, and we're only in seafood. Boston Seafood Exchange is the name we use because it identifies us very closely with the industry and the products that we deal in. 'Marketing Designs, Inc.,' in the seafood business, would have absolutely no bearing or no recall or any factor at all. I picked the name Boston Seafood Exchange, Inc., because it defines where we are, who we deal with, the type of product we're into, and where our specialties are. The reason we have 'Inc.' on there is because also it seemed to me at the time—obviously it seemed to me at the time that it's incumbent upon me to tell people that I'm dealing with and to let them know that they're dealing with a corporation. So, we used 'Inc.' just to notify them; and I signed all my checks 'Treasurer' and so forth.''

At trial and on appeal the defendant argues that he was acting as an agent of Marketing Designs, Inc., in 1988 when he incurred the debt which the plaintiffs seek to recover from him individually. It makes no difference that the plaintiffs thought they were dealing with corporate entities which did not exist, the defendant contends, because they were ''aware'' that they were transacting business with a corporate entity and not with the defen-

dant individually. The judge essentially adopted the defendant's position. . . .[2]

"If the other party [to a transaction] has notice that the agent is or may be acting for a principal but has no notice of the principal's identity, the principal for whom the agent is acting is a partially disclosed principal." Restatement (Second) of Agency § 4(2) (1958). Here, the plaintiffs had notice that the defendant was purporting to act for a corporate principal or principals but had no notice of the identity of the principal as claimed by the defendant in this litigation. "Unless otherwise agreed, a person purporting to make a contract with another for a partially disclosed principal is a party to the contract." Id. at 321.

It is the duty of the agent, if he would avoid personal liability on a contract entered into by him on behalf of his principal, to disclose not only that he is acting in a representative capacity, but also the identity of his principal. . . .

The judge reasoned that since the defendant had filed a certificate with the city of Boston in December, 1987, that Marketing Designs, Inc., was doing business as Boston Seafood Exchange, the plaintiffs could have discerned "precisely with whom they were dealing by reference to public records before the 1988 credits were extended."[3] But the defendant had dealt with Salmonor, and probably Atlantic, before that date, continued to deal with both under the name Boston International Seafood Exchange, Inc., thereafter, and even proposed to the plaintiffs a corporate restructuring of that nonentity. In any event, it was not the plaintiffs' duty to seek out the identity of the defendant's principal; it was the defendant's obligation fully to reveal it. . . .

It is not sufficient that the plaintiffs may have had the means, through a search of the records of the Boston city clerk, to determine the identity of the defendant's principal. Actual knowledge is the test. . . . "The duty rests upon the agent, if he would avoid personal liability, to disclose his agency, and not upon others to discover it. It is not, therefore, enough that the other party has the means of ascertaining the name of the principal; the

2. On the evidence in this case, one might view with considerable skepticism the good faith of the defendant's claim that he was in fact acting as the agent of Marketing Designs, Inc. His use of "Inc." in the description of the two fictitious corporations (a criminal violation, . . .), the methods by which the business was conducted and advertised, the late filing of the business certificate, the purpose of Marketing Designs, Inc., and that in the defendant's own words that name "in the seafood business, would have absolutely no bearing or no recall or any factor at all," the use of only one fictitious name on the doing business certificate, the continuation thereafter of the use of business cards and checks in the other fictitious name of Boston International Seafood Exchange, Inc., and the suggestion to the plaintiffs of the reorganization of that nonentity strongly suggest manipulation and the attempted convenient illusion of personal liability by means of a corporation (then dissolved) never intended to conduct or be responsible for the business of salmon importing. Nevertheless, the judge found that the defendant was not culpable of any relevant "fraud or other reprehensible conduct."

3. Of course, had the plaintiffs checked the public corporate records, they would have found that Marketing Designs, Inc., had been dissolved.

agent must either bring to him actual knowledge or, what is the same thing, that which to a reasonable man is equivalent to knowledge or the agent will be bound. There is no hardship to the agent in this rule, as he always has it in his power to relieve himself from personal liability by fully disclosing his principal and contracting only in the latter's name. If he does not do this, it may well be presumed that he intended to make himself personally responsible.'' 1 Mechem on Agency § 1413 (2d ed. 1914).

Finally, the defendant's use of trade names or fictitious names by which he claimed Marketing Designs, Inc., conducted its business is not in the circumstances a sufficient identification of the alleged principal so as to protect the defendant from personal liability.... Indeed, the defendant's own testimony expresses the impossibility of any rational connection....

The judgment is reversed, and new judgments are to be entered against the defendant for Atlantic in the amount of $153,788.50 and for Salmonor in the amount of $101,759.65, both with appropriate interest and costs.

ANALYSIS

1. Suppose that before dealing with the plaintiffs, Curran had reinstated Marketing Designs, Inc. as a lawful corporation and had lawfully and effectively changed its name to Boston International Seafood Exchange, Inc. What result?

2. Does it seem that the plaintiffs got more than they bargained for?

3. What should Curran have done to protect himself from liability.

4. What should the plaintiffs have done to protect against the need for litigation to enforce their claims?

SECTION 3. LIABILITY OF PRINCIPAL TO THIRD PARTIES IN TORT

A. SERVANT VERSUS INDEPENDENT CONTRACTOR

The first two cases that follow, Humble Oil & Refining Co. v. Martin and Hoover v. Sun Oil Company, again present the issue of organization within the firm versus organization across markets. Here we have large oil companies faced with the business issue of how to sell their principal products, gasoline and oil. One possibility is to sell through independently owned and operated gasoline filling stations. Another possibility is to sell through stations that they own and operate through employees. As the cases illustrate, in practice the arrangements have some characteristics of each of these possibilities.

In the era in which these cases arose, most gasoline stations performed three functions. (1) They sold gasoline, with service. There were no self-serve pumps. (2) They sold tires, batteries, and accessories (TBA). And (3) they performed repair services. The oil companies wanted to supply the gasoline and oil and the tires, batteries, and accessories. The repair services were provided by, or under the direction of, the operator of the station, who generally was himself an automobile mechanic.

The cases involve the liability of the oil companies for personal injuries negligently inflicted by gasoline station personnel. The legal issue turns on whether the operator of the station was an employee—a ''servant'' in the language of the law—or an independent operator (independent contractor) or, in more modern language, a franchisee. Under the doctrine of respondeat superior, a ''master'' (employer) is liable for the torts of its servants (employees). A master-servant relationship exists where the servant has agreed (a) to work on behalf of the master and (b) to be subject to the master's control or right to control the ''physical conduct'' of the servant (that is, the manner in which the job is performed, as opposed to the result alone). See Restatement (Second) of Agency §§ 1 and 2.

Servants are distinguished from independent contractors. The latter are of two types, agents and non-agents. An agent-type independent contractor is one who has agreed to act on behalf of another, the principal, but not subject to the principal's control over how the result is accomplished (that is, over the ''physical conduct'' of the task). A non-agent independent contractor is one who operates independently and simply enters into arm's length transactions with others. For example, if a carpenter is hired to build a garage for a homeowner, and if it is agreed or understood that the carpenter is simply responsible for getting the job done and is not to take directions from the homeowner, the carpenter is an independent contractor and is not acting as an agent. If the carpenter agrees to buy lumber for the project, on the credit account of the homeowner, the carpenter will still be acting as an independent contractor (assuming again that the homeowner

does not have the right to tell the carpenter how to accomplish the task), but, because the carpenter is now acting on behalf of the homeowner in the purchase of the lumber, the carpenter is an (independent-contractor-type) agent of the homeowner. These cases are concerned only with the distinction between servants and nonagent independent contractors.

Humble Oil & Refining Co. v. Martin

148 Tex. 175, 222 S.W.2d 995 (1949).

Petitioners Humble Oil & Refining Company and Mrs. A.C. Love and husband complain here of the judgments of the trial court and the Court of Civil Appeals in which they were held [liable] in damages for personal injuries following a special issue verdict at the suit of respondent George F. Martin acting for himself and his two minor daughters. The injuries were inflicted on the three Martins about the noon hour on May 12, 1947, in the City of Austin, by an unoccupied automobile belonging to the petitioners Love, which, just prior to the accident, had been left by Mrs. Love at a filling station owned by petitioner Humble for servicing and thereafter, before any station employee had touched it, rolled by gravity off the premises into and obliquely across the abutting street, striking Mr. Martin and his children from behind as they were walking into the yard of their home, a short distance downhill from the station.

The trial court rendered judgment against petitioners Humble and Mrs. Love jointly and severally and gave the latter judgment over against Humble for whatever she might pay the respondents. The Court of Civil Appeals affirmed the judgment after reforming it to eliminate the judgment over in favor of Mrs. Love, without prejudice to the right of contribution by either defendant under Article 2212, Vernon's Ann.Civ.Stat., 216 S.W.(2d) 251. The petitioners here respectively complain of the judgment in favor of the Martins, and each seeks full indemnity (as distinguished from contribution) from the other.

The apparently principal contention of petitioner, Humble, is that it is liable neither to respondent Martin nor to petitioner Mrs. Love, since the station was in effect operated by an independent contractor, W.T. Schneider, and Humble is accordingly not responsible for his negligence nor that of W.V. Manis, who was the only station employee or representative present when the Love car was left and rolled away. In this connection, the jury convicted petitioner Humble of the following acts of negligence proximately causing the injuries in question: (a) Failure to inspect the Love car to see that the emergency brake was set or the gears engaged; (b) failure to set the emergency brake on the Love car; (c) leaving the Love car unattended on the driveway. The verdict also included findings that Mrs. Love "had delivered her car to the custody of the defendant Humble Oil & Refining Company, before her car started rolling from the position in which she had parked it"; that the accident was not unavoidable; and that no negligent act of either of petitioners was the sole proximate cause of the injuries in question. We think the Court of Civil Appeals properly held Humble

responsible for the operation of the station, which admittedly it owned, as it did also the principal products there sold by Schneider under the so-called "Commission Agency Agreement" between him and Humble which was in evidence. The facts that neither Humble, Schneider nor the station employees considered Humble as an employer or master; that the employees were paid and directed by Schneider individually as their "boss," and that a provision of the agreement expressly repudiates any authority of Humble over the employees, are not conclusive against the master-servant relationship, since there is other evidence bearing on the right or power of Humble to control the details of the station work as regards Schneider himself and therefore as to employees which it was expressly contemplated that he would hire. The question is ordinarily one of fact, and where there are items of evidence indicating a master-servant relationship, contrary items such as those above mentioned cannot be given conclusive effect....

Even if the contract between Humble and Schneider were the only evidence on the question, the instrument as a whole indicates a master-servant relationship quite as much as, if not more than, it suggests an arrangement between independent contractors. For example, paragraph 1 includes a provision requiring Schneider "to make reports *and perform other duties in connection with the operation of said station that may be required of him from time to time by Company.*" (Emphasis supplied). And while paragraph 2 purports to require Schneider to pay all operational expenses, the schedule of commissions forming part of the agreement does just the opposite in its paragraph (F), which gives Schneider a 75% "commission" on "the net public utility bills paid" by him and thus requires Humble to pay three-fourths of one of the most important operational expense items. Obviously the main object of the enterprise was the retail marketing of Humble's products with title remaining in Humble until delivery to the consumer. This was done under a strict system of financial control and supervision by Humble, with little or no business discretion reposed in Schneider except as to hiring, discharge, payment and supervision of a few station employees of a more or less laborer status. Humble furnished the all important station location and equipment, the advertising media, the products and a substantial part of the current operating costs. The hours of operation were controlled by Humble. The "Commission Agency Agreement," which evidently was Schneider's only title to occupancy of the premise, was terminable at the will of Humble. The so-called "rentals" were, at least in part, based on the amount of Humble's products sold, being, therefore, involved with the matter of Schneider's remuneration and not rentals in the usual sense. And, as above shown, the agreement required Schneider in effect to do anything Humble might tell him to do. All in all, aside from the stipulation regarding Schneider's assistants, there is essentially little difference between his situation and that of a mere store clerk who happens to be paid a commission instead of a salary. The business was Humble's business, just as the store clerk's business would be that of the store owner. Schneider was Humble's servant, and so accordingly were Schneider's assistants who were contemplated by the contract. Upon facts similar to those at bar but probably less indicative of a master-

servant relationship, the latter has been held to exist by respectable authority, which seems to reflect the prevailing view in the nation....

The evidence above discussed serves to distinguish the instant case from The Texas Company v. Wheat, 140 Texas 468, 168 S.W.(2d) 632, upon which petitioner Humble principally relies. In that case the evidence differed greatly from that now before us. It clearly showed a ''dealer'' type of relationship in which the lessee in charge of the filling station purchased from his landlord, The Texas Company, and sold as his own, and was free to sell at his own price and on his own credit terms, the company products purchased, as well as the products of other oil companies. The contracts contained no provision requiring the lessee to perform any duty The Texas Company might see fit to impose on him, nor did the company pay any part of the lessee's operating expenses, nor control the working hours of the station....

Hoover v. Sun Oil Company

58 Del. 553, 212 A.2d 214 (1965).

This case is concerned with injuries received as the result of a fire on August 16, 1962 at the service station operated by James F. Barone. The fire started at the rear of plaintiff's car where it was being filled with gasoline and was allegedly caused by the negligence of John Smilyk an employee of Barone. Plaintiffs brought suit against Smilyk, Barone and Sun Oil Company (Sun) which owned the service station.

Sun has moved for summary judgment as to it on the basis that Barone was an independent contractor and therefore the alleged negligence of his employee could not result in liability as to Sun. The plaintiffs contend instead that Barone was acting as Sun's agent and that Sun may therefore be responsible for plaintiff's injuries.

Barone began operating this business in October of 1960 pursuant to a lease dated October 17, 1960. The station and all of its equipment, with the exception of a tire-stand and rack, certain advertising displays and miscellaneous hand tools, were owned by Sun. The lease was subject to termination by either party upon thirty days' written notice after the first six months and at the anniversary date thereafter. The rental was partially determined by the volume of gasoline purchased but there was also a minimum and a maximum monthly rental.

At the same time, Sun and Barone also entered into a dealer's agreement under which Barone was to purchase petroleum products from Sun and Sun was to loan necessary equipment and advertising materials. Barone was required to maintain this equipment and to use it solely for Sun products. Barone was permitted under the agreement to sell competitive products but chose to do so only in a few minor areas. As to Sun products, Barone was prohibited from selling them except under the Sunoco label and from blending them with products not supplied by Sun.

Barone's station had the usual large signs indicating that Sunoco products were sold there. His advertising in the classified section of the telephone book was under a Sunoco heading and his employees wore uniforms with the Sun emblem, the uniforms being owned by Barone or rented from an independent company.

Barone, upon the urging of Robert B. Peterson, Sun's area sales representative, attended a Sun school for service station operators in 1961. The school's curriculum was designed to familiarize the station operator with bookkeeping and merchandising, the appearance and proper maintenance of a Sun station, and the Sun Oil products. The course concluded with the operator working at Sun's model station in order to gain work experience in the use of the policy and techniques taught at the school.

Other facts typifying the company-service station relationship were the weekly visits of Sun's sales representative, Peterson, who would take orders for Sun products, inspect the restrooms, communicate customer complaints, make various suggestions to improve sales and discuss any problems that Barone might be having. Besides the weekly visits, Peterson was in contact with Barone on other occasions in order to implement Sun's "competitive allowance system" which enabled Barone to meet local price competition by giving him a rebate on the gasoline in his inventory roughly equivalent to the price decline and a similarly reduced price on his next order of gasoline.

While Peterson did offer advice to Barone on all phases of his operation, it was usually done on request and Barone was under no obligation to follow the advice. Barone's contacts and dealings with Sun were many and their relationship intricate, but he made no written reports to Sun and he alone assumed the overall risk of profit or loss in his business operation. Barone independently determined his own hours of operation and the identity, pay scale and working conditions of his employees, and it was his name that was posted as proprietor.

Plaintiffs contend in effect that the aforegoing facts indicate that Sun controlled the day-to-day operation of the station and consequently Sun is responsible for the negligent acts of Barone's employee. Specifically, plaintiffs contend that there is an issue of fact for the jury to determine as to whether or not there was an agency relationship.

The legal relationships arising from the distribution systems of major oil-producing companies are in certain respects unique. As stated in an annotation collecting many of the cases dealing with this relationship:

"This distribution system has grown up primarily as the result of economic factors and with little relationship to traditional legal concepts in the field of master and servant, so that it is perhaps not surprising that attempts by the court to discuss the relationship in the standard terms have led to some difficulties and confusion." 83 A.L.R.2d 1282, 1284 (1962).

In some situations traditional definitions of principal and agent and of employer and independent contractor may be difficult to apply to service

station operations, but the undisputed facts of the case at bar make it clear that Barone was an independent contractor.

Barone's service station, unlike retail outlets for many products, is basically a one-company outlet and represents to the public, through Sunoco's national and local advertising, that it sells not only Sun's quality products but Sun's quality service. Many people undoubtedly come to the service station because of that latter representation.

However, the lease contract and dealer's agreement fail to establish any relationship other than landlord-tenant, and independent contractor. Nor is there anything in the conduct of the individuals which is inconsistent with that relationship so as to indicate that the contracts were mere subterfuge or sham. The areas of close contact between Sun and Barone stem from the fact that both have a mutual interest in the sale of Sun products and in the success of Barone's business.

The cases cited by both plaintiffs and defendant indicate that the result varies according to the contracts involved and the conduct and evidence of control under those contracts. Both lines of cases indicate that the test to be applied is that of whether the oil company has retained the right to control the details of the day-to-day operation of the service station; control or influence over results alone being viewed as insufficient. . . .

The facts of this case differ markedly from those in which the oil company was held liable for the tortious conduct of its service station operator or his employees. Sun had no control over the details of Barone's day-to-day operation. Therefore, no liability can be imputed to Sun from the allegedly negligent acts of Smilyk. Sun's motion for summary judgment is granted.

ANALYSIS

1. Important elements of business relationships include duration, control, risk of loss, and return. Which of these becomes the key issue in the two cases? How can the outcomes in the two cases be reconciled?

2. Pretend you know nothing about the legal rules that distinguish between employees (servants) and people working for themselves (independent contractors).

(a) If you were a person like Schneider (the gas station operator in the *Humble Oil* case), which terms or elements of the relationship with Humble Oil would make you feel like an employee? Which terms would make you feel that you were independent, working for yourself?

(b) If you were a person like Barone (the operator in the *Sun Oil* case), would you feel less like an employee and more like an independent business person than a person like Schneider? Why?

(c) Focus on those terms of each relationship that suggest that the operator is independent. Assume that the oil companies could have

changed those terms to make them consistent with an employment relationship. What would the new terms be? Why do you suppose the oil companies chose what may be thought of as a hybrid set of terms?

PLANNING

1. In *Humble Oil* the court states, ''The hours of operation were controlled by Humble.'' In *Sun Oil* the court states, ''Barone independently determined his own hours of operation.'' What do you suppose is the practical difference in the control of each of the oil companies over hours of operation? What do you suppose would happen to Barone if the people at Sun Oil concluded that he was not staying open late enough and that, as a result, Sun Oil was losing sales?

2. If you were advising Humble Oil and wanted to improve the prospects of avoiding liability for personal injuries, what changes would you suggest in the manner in which Humble Oil structured its relationship with its operators? What would be the likely substantive effect of these changes?

POLICY QUESTIONS

In the *Sun Oil* situation, presumably Sun Oil could have insisted that Barone take out a policy of liability insurance, protecting both him and Sun Oil, or that he agree to indemnify Sun Oil for damages and show that he had enough assets to meet his obligation.

1. Do you think that it was irresponsible for Sun Oil to fail to do that?

2. Assume that your answer to part 1 was yes. What if Barone had operated ten gas stations, under his own name (but still bought most of his gasoline and oil and tires, batteries, and accessories from Sun Oil)?

3. Should the law somehow impose an obligation on Sun Oil to ensure that Barone is able to pay his debts?

4. Assume your answer to part 3 was yes. How would you frame the law?

5. What is your general theory of when people who do business with one another should and should not be liable for each other's tort, or contract, damages?

Murphy v. Holiday Inns, Inc.

216 Va. 490, 219 S.E.2d 874 (1975).

On August 21, 1973, Kyran Murphy (plaintiff) filed a motion for judgment against Holiday Inns, Inc. (defendant), a Tennessee Corporation, seeking damages for personal injuries sustained on August 24, 1971, while she was a guest at a motel in Danville. Plaintiff alleged that ''Defendant

owned and operated'' the motel; that ''Defendant, its agents and employees, so carelessly, recklessly, and negligently maintained the premises of the motel that Plaintiff did slip and fall on an area of a walk where water draining from an air conditioner had been allowed to accumulate''; and that as a proximate result of such negligence, plaintiff sustained serious and permanent injuries.

Defendant filed grounds of defense and a motion for summary judgment ''on the grounds that it has no relationship with regard to the operator of the premises . . . other than a license agreement permitting the operator of a motel on the same premises to use the name 'Holiday Inns' subject to all the terms and conditions of such license agreement.'' That agreement, filed as an exhibit with defendant's motion for summary judgment, identifies defendant's licensee as Betsy–Len Motor [Hotel] Corporation (Betsy–Len).

Upon a finding that defendant did not own the premises upon which the accident occurred and that ''there exists no principal-agent or master-servant relationship between the defendant corporation and Betsy–Len Motor Hotel Corporation,'' the trial court entered a final order on April 25, 1974, granting summary judgment in favor of defendant.

Plaintiff's sole assignment of error is that the trial court erred ''in holding that no principal-agent or master-servant relationship exists.''

On brief, plaintiff argues that the license agreement gives defendant ''the authority and control over the Betsy–Len Corporation that establishes a true master/servant relationship.'' . . .

Actual agency is a consensual relationship.

> ''Agency is the fiduciary relation which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act. Restatement (Second) of Agency § 1 (1958).
>
> . . .
>
> ''It is the element of continuous subjection to the will of the principal which distinguishes the agent from other fiduciaries and the agency agreement from other agreements.'' Id., comment (b).
>
> . . .

When an agreement, considered as a whole, establishes an agency relationship, the parties cannot effectively disclaim it by formal ''consent.'' ''[T]he relationship of the parties does not depend upon what the parties themselves call it, but rather in law what it actually is.'' Chandler v. Kelley, 149 Va. 221, 231, 141 S.E. 389, 391–92 (1928). . . . Here, plaintiff and defendant agree that, if the license agreement is sufficient to establish an agency relationship, the disclaimer clause[1] does not defeat it.

1. That clause provides that ''Licensee, in the use of the name 'Holiday Inn' . . . shall identify Licensee as being the owner and operator [and] . . . the parties hereto are

Plaintiff and defendant also agree that, in determining whether a contract establishes an agency relationship, the critical test is the nature and extent of the control agreed upon.

The subject matter of the license defendant granted Betsy–Len is a "system". As defined in the agreement, the system is one "providing to the public . . . an inn service . . . of distinctive nature, of high quality, and of other distinguishing characteristics." Those characteristics include trade names using the words "Holiday Inn" and certain variations and combinations of those words, trade marks, architectural designs, insignia, patterns, color schemes, styles, furnishings, equipment, advertising services, and methods of operation.

In consideration of the license to use the "system," the licensee agreed to pay an initial sum of $5000; to construct one or more inns in accordance with plans approved by the licensor; to make monthly payments of 15 cents per room per day (5 cents of which was to be earmarked for national advertising expenditures); and "to conduct the operation of inns . . . in accordance with the terms and provisions of this license and of the Rules of operation of said System".

Plaintiff points to several provisions and rules which he says satisfy the control test and establish the principal-agent relationship. These include requirements:

That licensee construct its motel according to plans, specifications, feasibility studies, and locations approved by licensor;

That licensee employ the trade name, signs, and other symbols of the "system" designated by licensor;

That licensee pay a continuing fee for use of the license and a fee for national advertising of the "system";

That licensee solicit applications for credit cards for the benefit of other licensees;

That licensee protect and promote the trade name and not engage in any competitive motel business or associate itself with any trade association designed to establish standards for motels;

That licensee not raise funds by sale of corporate stock or dispose of a controlling interest in its motel without licensor's approval;

That training for licensee's manager, housekeeper, and restaurant manager be provided by licensor at licensee's expense;

That licensee not employ a person contemporaneously engaged in a competitive motel or hotel business; and

That licensee conduct its business under the "system," observe the rules of operation, make quarterly reports to licensor concerning operations, and submit to periodic inspections of facilities and procedures conducted by licensor's representatives.

completely separate entities, are not partners, joint adventurers, or agents of the other in any sense, and neither has power to obligate or bind the other."

The license agreement of which these requirements were made a part is a franchise contract. In the business world, franchising is a crescent phenomenon of billion-dollar proportions.

> ''[Franchising is] a system for the selective distribution of goods and/or services under a brand name through outlets owned by independent businessmen, called 'franchisees.' Although the franchisor supplies the franchisee with know-how and brand identification on a continuing basis, the franchisee enjoys the right to profit and runs the risk of loss. The franchisor controls the distribution of his goods and/or services through a contract which regulates the activities of the franchisee, in order to achieve standardization.'' R. Rosenberg, *Profits From Franchising* 41 (1969). (Italics omitted).

The fact that an agreement is a franchise contract does not insulate the contracting parties from an agency relationship. If a franchise contract so ''regulates the activities of the franchisee'' as to vest the franchisor with control within the definition of agency, the agency relationship arises even though the parties expressly deny it.

Here, the license agreement contains the principal features of the typical franchise contract, including regulatory provisions. Defendant owned the ''brand name,'' the trade mark, and the other assets associated with the ''system''. Betsy–Len owned the sales ''outlet''. Defendant agreed to allow Betsy–Len to use its assets. Betsy–Len agreed to pay a fee for that privilege. Betsy–Len retained the ''right to profit'' and bore the ''risk of loss''. With respect to the manner in which defendant's trade mark and other assets were to be used, both parties agreed to certain regulatory rules of operation.

Having carefully considered all of the regulatory provisions in the agreement, we are of opinion that they gave defendant no ''control or right to control the methods or details of doing the work,'' Wells v. Whitaker, 207 Va. 616, 624, 151 S.E.2d 422, 429 (1966), and, therefore, agree with the trial court that no principal-agent or master-servant relationship was created.[2] As appears from the face of the document, the purpose of those provisions was to achieve system-wide standardization of business identity, uniformity of commercial service, and optimum public good will, all for the benefit of both contracting parties. The regulatory provisions did not give defendant control over the day-to-day operation of Betsy–Len's motel. While defendant was empowered to regulate the architectural style of the buildings and the type and style of furnishings and equipment, defendant was given no power to control daily maintenance of the premises. Defendant was given no power to control Betsy–Len's current business expenditures, fix customer rates, or demand a share of the profits. Defendant was given no power to hire or fire Betsy–Len's employees, determine employee wages or working conditions, set standards for employee skills or productivity, supervise employee work routine, or discipline employees for nonfea-

2. Because defendant had no such control or right to control, the distinction between a principal-agent and a master-servant relationship is not relevant here. . . .

sance or misfeasance. All such powers and other management controls and responsibilities customarily exercised by an owner and operator of an on-going business were retained by Betsy–Len.

We hold that the regulatory provisions of the franchise contract did not constitute control within the definition of agency, and the judgment is

Affirmed.

ANALYSIS AND PLANNING

1. Restatement (Second) of Agency § 219(1) provides: "A master is subject to liability for the torts of his servants committed while acting in the scope of their employment." The comments to that section make clear that, as a general rule, a principal is not liable for the torts of his non-servant agents—i.e., independent contractors. See also Restatement § 250. Restatement § 1 indicates, as stated by the *Holiday Inns* court, that control is an essential element of the definition of an agency relationship, whether one is dealing with a servant or an independent contractor. A key distinction between the servant and independent contractor types of agents, however, is the differing natures and degrees of control exercised by the principal. See Restatement § 220. Did Holiday Inns have sufficient control over Betsy–Len to make the latter a servant? Are the factors set forth in Restatement § 220 helpful in this regard?

2. According to the court in *Holiday Inns,* "Plaintiff and defendant agree that, in determining whether a contract establishes an agency relationship, the critical test is the nature and extent of the control agreed upon." Is it possible for a franchisor to have a degree of control consistent with the master-servant relationship without that master-servant relationship arising as a matter of law? What other requirement, if any, must be satisfied? See Restatement (Second) of Agency § 1, quoted by the court. To put the issue another way, does it seem to you that the defendant might have prevailed even if it had lost on the control issue? In other words, did the defendant have another, unused, string to its bow?

3. In *Vandemark v. McDonald's Corp.*, 904 A.2d 627 (N.H. 2006), an employee of a McDonald's franchise was injured when the restaurant was robbed. The employee sued McDonald's, claiming that the franchisee was an agent of the franchisor. In support of that claim, the employee pointed to the extensive franchise agreement governing the McDonald's-franchisee relationship and argued that:

> McDonald's has maintained a continuous prescription of what [franchisee] shall and shall not do. McDonald's mandates compliance with the "McDonald's System." McDonald's mandates particular methods for preparing foods, as well as food preparation and service times. McDonald's mandates through the "QSC Play Book" that franchisee restaurants ... implement "key success factors" in their restaurants. Moreover, McDonald's sends out field consultants ... to ensure that McDonald's specifications are met.

Id. at 634.

The *Vandemark* court rejected the employee's argument, holding that:

> [T]he ... weight of authority construes franchiser liability narrowly, finding that absent a showing of control over security measures employed by the franchisee, the franchiser cannot be vicariously liable for the security breach....
>
> [T]he trial court relied primarily upon Wendy Hong Wu v. Dunkin' Donuts, Inc., 105 F.Supp.2d 83 (E.D.N.Y.2000), in which the United States District Court for the Eastern District of New York surveyed extensive state and federal case law concerning the vicarious liability of a franchiser for the security breaches of its franchisee. In *Wendy Hong Wu*, an employee of a Dunkin' Donuts' franchisee brought a vicarious liability claim against Dunkin' Donuts after she was raped and assaulted while working the night shift. The court specifically examined whether Dunkin' Donuts had control over the alleged ''instrumentality'' that caused the harm. The court held that since there was no evidence that Dunkin' Donuts actually mandated specific security equipment or otherwise controlled the steps taken by its franchisees in general to protect employees, it was not vicariously liable for the alleged lapse in security. The court reasoned that the franchise agreement was ''primarily designed to maintain uniform appearance among its franchisees and uniform quality among their products and services to protect and enhance the value of the Dunkin' Donuts trademark. [The franchisee] remain[ed] solely responsible for hiring, firing, and training its employees and for making all day-to-day decisions necessary to run the business.'' In addition to finding a lack of control over security matters within the franchise agreement, the court stated that ''the undisputed evidence in the record demonstrates that [Dunkin' Donuts] merely made security equipment available for purchase and suggested that alarm systems and other burglary prevention techniques were important[.]''
>
> ... [T]he evidence demonstrates that although the defendant maintained authority to insure the uniformity and standardization of products and services offered by the [franchise] restaurant, such authority did not extend to the control of security operations. Thus, there was no genuine issue of material fact as to whether the defendant exercised control over the relevant security policies at the [franchisee's] restaurant through adopting the QSC Play Book. ...

Id. at 634–36 (citations omitted).

Does this analysis help explain the outcomes in any or all of *Humble Oil*, *Sun Oil*, or *Holiday Inns*? In particular, if the court's holding that the ''issue turns narrowly upon the defendant's level of control over the alleged 'instrumentality' which caused the harm'' had been applied in those cases, would the outcome in those cases have changed?

Is such a narrow focus on ''control over the alleged 'instrumentality' which caused the harm'' consistent with sound social and economic policy?

4. How do firms like Holiday Inns, Inc. make their profit? What are their risks? In their relationships with franchisors, what legal rights are likely to be important to them?

5. How do the franchisees make their profit? What are their risks? In their relationship with the franchisors, what legal rights are likely to be important to them?

6. How much freedom does a franchisee like Betsy–Len have to run its business? Suppose that a field representative of Holiday Inns, Inc. visits the Betsy–Len motor hotel and finds that the desk clerk, who is a son of one of the owners of the franchise, is surly and inefficient, and that the restaurant, managed by the other owner, is badly run, with poor food and slow service. What are the various steps that Holiday Inns, Inc. can take to induce its franchisee to improve its performance? What do your answers to these questions tell you about drafting a franchise contract?

B. Tort Liability and Apparent Agency

Miller v. McDonald's Corp.

945 P.2d 1107 (Ore. App. 1997).

Plaintiff seeks damages from defendant McDonald's Corporation for injuries that she suffered when she bit into a heart-shaped sapphire stone while eating a Big Mac sandwich that she had purchased at a McDonald's restaurant in Tigard. The trial court granted summary judgment to defendant on the ground that it did not own or operate the restaurant; rather, the owner and operator was a non-party, 3K Restaurants (3K), that held a franchise from defendant. Plaintiff appeals, and we reverse.

. . . 3K owned and operated the restaurant under a License Agreement (the Agreement) with defendant that required it to operate in a manner consistent with the "McDonald's System." The Agreement described that system as including proprietary rights in trade names, service marks and trade marks, as well as "designs and color schemes for restaurant buildings, signs, equipment layouts, formulas and specifications for certain food products, methods of inventory and operation control, bookkeeping and accounting, and manuals covering business practices and policies." . . .

The Agreement described the way in which 3K was to operate the restaurant in considerable detail. It expressly required 3K to operate in compliance with defendant's prescribed standards, policies, practices, and procedures, including serving only food and beverage products that defendant designated. 3K had to follow defendant's specifications and blueprints for the equipment and layout of the restaurant, including adopting subsequent reasonable changes that defendant made, and to maintain the restaurant building in compliance with defendant's standards. 3K could not make any changes in the basic design of the building without defendant's approval.

The Agreement required 3K to keep the restaurant open during the hours that defendant prescribed, including maintaining adequate supplies and employing adequate personnel to operate at maximum capacity and efficiency during those hours. 3K also had to keep the restaurant similar in appearance to all other McDonald's restaurants. 3K's employees had to wear McDonald's uniforms, to have a neat and clean appearance, and to provide competent and courteous service. 3K could use only containers and other packaging that bore McDonald's trademarks. The ingredients for the foods and beverages had to meet defendant's standards, and 3K had to use "only those methods of food handling and preparation that [defendant] may designate from time to time." In order to obtain the franchise, 3K had to represent that the franchisee had worked at a McDonald's restaurant; the Agreement did not distinguish in this respect between a company-run or a franchised restaurant. The manuals gave further details that expanded on many of these requirements.

In order to ensure conformity with the standards described in the Agreement, defendant periodically sent field consultants to the restaurant to inspect its operations. 3K trained its employees in accordance with defendant's materials and recommendations and sent some of them to training programs that defendant administered. Failure to comply with the agreed standards could result in loss of the franchise.

Despite these detailed instructions, the Agreement provided that 3K was not an agent of defendant for any purpose. Rather, it was an independent contractor and was responsible for all obligations and liabilities, including claims based on injury, illness, or death, directly or indirectly resulting from the operation of the restaurant.

Plaintiff went to the restaurant under the assumption that defendant owned, controlled, and managed it. So far as she could tell, the restaurant's appearance was similar to that of other McDonald's restaurants that she had patronized. Nothing disclosed to her that any entity other than defendant was involved in its operation. The only signs that were visible and obvious to the public had the name "McDonald's,"[2] the employees wore uniforms with McDonald's insignia, and the menu was the same that plaintiff had seen in other McDonald's restaurants. The general appearance of the restaurant and the food products that it sold were similar to the restaurants and products that plaintiff had seen in national print and television advertising that defendant had run. To the best of plaintiff's knowledge, only McDonald's sells Big Mac hamburgers.

In short, plaintiff testified, she went to the Tigard McDonald's because she relied on defendant's reputation and because she wanted to obtain the same quality of service, standard of care in food preparation, and general

2. This is plaintiff's testimony in her affidavit. Representatives of 3K testified in their depositions that there was a sign near the front counter that identified Bob and Karen Bates and 3K Restaurants as the owners. There is no evidence of the size or prominence of the sign, nor is there evidence of any other non-McDonald's identification in the restaurant.

attention to detail that she had previously enjoyed at other McDonald's restaurants....

The kind of actual agency relationship that would make defendant vicariously liable for 3K's negligence requires that defendant have the right to control the method by which 3K performed its obligations under the Agreement....[3]

A number of other courts have applied the right to control test to a franchise relationship. The Delaware Supreme Court, in Billops v. Magness Const. Co., 391 A.2d 196 (Del.1978), stated the test as it applies to that context:

> "If, in practical effect, the franchise agreement goes beyond the stage of setting standards, and allocates to the franchisor the right to exercise control over the daily operations of the franchise, an agency relationship exists." 391 A.2d at 197–98.

This statement expresses the general direction that courts have taken .... We therefore adopt it for the purposes of this case.

... [We] believe that a jury could find that defendant retained sufficient control over 3K's daily operations that an actual agency relationship existed. The Agreement did not simply set standards that 3K had to meet. Rather, it required 3K to use the precise methods that defendant established .... Defendant enforced the use of those methods by regularly sending inspectors and by its retained power to cancel the Agreement. That evidence would support a finding that defendant had the right to control the way in which 3K performed at least food handling and preparation. In her complaint, plaintiff alleges that 3K's deficiencies in those functions resulted in the sapphire being in the Big Mac and thereby caused her injuries. Thus, ... there is evidence that defendant had the right to control 3K in the precise part of its business that allegedly resulted in plaintiff's injuries. That is sufficient to raise an issue of actual agency.

Plaintiff next asserts that defendant is vicariously liable for 3K's alleged negligence because 3K was defendant's apparent agent.[4] The relevant standard is in Restatement (Second) of Agency, § 267 ...:

> "One who represents that another is his servant or other agent and thereby causes a third person justifiably to rely upon the care or skill of such apparent agent is subject to liability to the third person for harm caused by the lack of care or skill of the one appearing to be a servant or other agent as if he were such."

3. Under the right to control test it does not matter whether the putative principal actually exercises control; what is important is that it has the right to do so. See Peeples v. Kawasaki Heavy Indust., Ltd., 288 Or. 143, 149, 603 P.2d 765 (1979).

4. Apparent agency is a distinct concept from apparent authority. Apparent agency creates an agency relationship that does not otherwise exist, while apparent authority expands the authority of an actual agent. ... In this case, the precise issue is whether 3K was defendant's apparent agent, not whether 3K had apparent authority....

. . . We have not applied § 267 to a franchisor/franchisee situation, but courts in a number of other jurisdictions have done so in ways that we find instructive. In most cases the courts have found that there was a jury issue of apparent agency. The crucial issues are whether the putative principal held the third party out as an agent and whether the plaintiff relied on that holding out. . . .

In each of these cases, the franchise agreement required the franchisee to act in ways that identified it with the franchisor. The franchisor imposed those requirements as part of maintaining an image of uniformity of operations and appearance for the franchisor's entire system. Its purpose was to attract the patronage of the public to that entire system. The centrally imposed uniformity is the fundamental basis for the courts' conclusion that there was an issue of fact whether the franchisors held the franchisees out as the franchisors' agents.

In this case, for similar reasons, there is an issue of fact about whether defendant held 3K out as its agent. Everything about the appearance and operation of the Tigard McDonald's identified it with defendant and with the common image for all McDonald's restaurants that defendant has worked to create through national advertising, common signs and uniforms, common menus, common appearance, and common standards. The possible existence of a sign identifying 3K as the operator does not alter the conclusion that there is an issue of apparent agency for the jury. There are issues of fact of whether that sign was sufficiently visible to the public, in light of plaintiff's apparent failure to see it, and of whether one sign by itself is sufficient to remove the impression that defendant created through all of the other indicia of its control that it, and 3K under the requirements that defendant imposed, presented to the public.

Defendant does not seriously dispute that a jury could find that it held 3K out as its agent. Rather, it argues that there is insufficient evidence that plaintiff justifiably relied on that holding out. It argues that it is not sufficient for her to prove that she went to the Tigard McDonald's because it was a McDonald's restaurant. Rather, she also had to prove that she went to it because she believed that McDonald's Corporation operated both it and the other McDonald's restaurants that she had previously patronized. It states:

> "All [that] the Plaintiff's affidavit proves is that she went to the Tigard McDonald's based in reliance on her past experiences at other McDonald's. But her affidavit does nothing to link her experiences with ownership of those restaurants by McDonald's Corporation."

Defendant's argument both demands a higher level of sophistication about the nature of franchising than the general public can be expected to have and ignores the effect of its own efforts to lead the public to believe that McDonald's restaurants are part of a uniform national system of restaurants with common products and common standards of quality. A jury could find from plaintiff's affidavit that she believed that all McDonald's restaurants were the same because she believed that one entity owned and operated all of them or, at the least, exercised sufficient control that the

standards that she experienced at one would be the same as she experienced at others.

Plaintiff testified in her affidavit that her reliance on defendant for the quality of service and food at the Tigard McDonald's came in part from her experience at other McDonald's restaurants. Defendant's argument that she must show that it, rather than a franchisee, operated those restaurants is, at best, disingenuous. A jury could find that it was defendant's very insistence on uniformity of appearance and standards, designed to cause the public to think of every McDonald's, franchised or unfranchised, as part of the same system, that makes it difficult or impossible for plaintiff to tell whether her previous experiences were at restaurants that defendant owned or franchised. . . .

ANALYSIS

1. What's going on here? Why is the franchisor fighting this case? Isn't it in the franchisor's interest to ensure that plaintiffs like Billops will not have to worry about finding a solvent defendant?

2. If the jury finds that an apparent agency relationship exists between the franchisee and McDonald's, would that suffice for vicarious liability, or would plaintiff also have to show that the franchisee had apparent authority?

3. Should McDonald's reduce the amount of control it exercises over its franchisees, so as to avoid the risk of liability in cases such as this one?

4. Franchising as a way of organizing economic activity arose after the servant/independent contractor dichotomy was well-established. In many ways, the franchisor-franchisee relationship is a hybrid having attributes of both servant and independent contractor status. Accordingly, case outcomes often appear inconsistent and even arbitrary. What might be a better way of handling these cases doctrinally?

5. In its ruling on apparent agency, the court adopts the Restatement's requirement that the plaintiff must have relied on a manifestation by the apparent principal (here, McDonald's) and it must have been that reliance that exposed the plaintiff to harm. In most cases, this requirement makes good sense. Are there cases, however, in which requiring proof of justifiable reliance might seem unfair or inefficient?

PROBLEM

Suppose that the owners of twenty-five motels in a certain state decide that in order to compete they need a trade name and some statewide advertising. They realize that in order to benefit from the trade name they must ensure that each motel maintains high standards and that all the motels set room rates at a figure that is consistent with their intended image. They agree that they will remodel their lobbies to create a common attractive appearance and will require their employees to wear an agreed-

upon uniform. They form a corporation called Finest Motels Corp., in which they share ownership. They are required to make periodic payments to Finest Motels Corp. to pay for advertising and for policing compliance with standards. They hire a former executive of Hilton Inns, Inc. and tell her that they want their motels to live up to Hilton standards. Each of the motels is to change its name, with the new name beginning with the location, followed by "Finest Motel"—for example, "Anaheim Finest Motel." If any of the motels become insolvent, is Finest Motel Corp., or any of the other motels, liable for its debts? What suggestions would you offer to protect against that outcome?

C. Scope of Employment

Ira S. Bushey & Sons, Inc. v. United States

398 F.2d 167 (2d Cir.1968).

■ Friendly, Circuit Judge:

While the United States Coast Guard vessel Tamaroa was being overhauled in a floating drydock located in Brooklyn's Gowanus Canal, a seaman returning from shore leave late at night, in the condition for which seamen are famed, turned some wheels on the drydock wall. He thus opened valves that controlled the flooding of the tanks on one side of the drydock. Soon the ship listed, slid off the blocks and fell against the wall. Parts of the drydock sank, and the ship partially did—fortunately without loss of life or personal injury. The drydock owner sought and was granted compensation by the District Court for the Eastern District of New York in an amount to be determined, 276 F.Supp. 518; the United States appeals.

. . .

The Tamaroa had gone into drydock on February 28, 1963; her keel rested on blocks permitting her drive shaft to be removed and repairs to be made to her hull. The contract between the Government and Bushey provided in part:

> (*o*) The work shall, whenever practical, be performed in such manner as not to interfere with the berthing and messing of personnel attached to the vessel undergoing repair, and provision shall be made so that personnel assigned shall have access to the vessel at all times, it being understood that such personnel will not interfere with the work or the contractor's workmen.

Access from shore to ship was provided by a route past the security guard at the gate, through the yard, up a ladder to the top of one drydock wall and along the wall to a gangway leading to the fantail deck, where men returning from leave reported at a quartermaster's shack.

Seaman Lane, whose prior record was unblemished, returned from shore leave a little after midnight on March 14. He had been drinking heavily; the quartermaster made mental note that he was "loose." For

reasons not apparent to us or very likely to Lane,[4] he took it into his head, while progressing along the gangway wall, to turn each of three large wheels some twenty times; unhappily, as previously stated, these wheels controlled the water intake valves. After boarding ship at 12:11 A.M., Lane mumbled to an off-duty seaman that he had "turned some valves" and also muttered something about "valves" to another who was standing the engineering watch. Neither did anything; apparently Lane's condition was not such as to encourage proximity. At 12:20 A.M. a crew member discovered water coming into the drydock. By 12:30 A.M. the ship began to list, the alarm was sounded and the crew were ordered ashore. Ten minutes later the vessel and dock were listing over 20 degrees; in another ten minutes the ship slid off the blocks and fell against the drydock wall.

The Government attacks imposition of liability on the ground that Lane's acts were not within the scope of his employment. It relies heavily on § 228(1) of the Restatement of Agency 2d which says that "conduct of a servant is within the scope of employment if, but only if: * * * (c) it is actuated, at least in part, by a purpose to serve the master." Courts have gone to considerable lengths to find such a purpose, as witness a well-known opinion in which Judge Learned Hand concluded that a drunken boatswain who routed the plaintiff out of his bunk with a blow, saying "Get up, you big son of a bitch, and turn to," and then continued to fight, might have thought he was acting in the interest of the ship. Nelson v. American–West African Line, 86 F.2d 730 (2 Cir.1936), cert. denied, 300 U.S. 665 (1937). It would be going too far to find such a purpose here; while Lane's return to the Tamaroa was to serve his employer, no one has suggested how he could have thought turning the wheels to be, even if—which is by no means clear—he was unaware of the consequences.

In light of the highly artificial way in which the motive test has been applied, the district judge believed himself obliged to test the doctrine's continuing vitality by referring to the larger purposes respondeat superior is supposed to serve. He concluded that the old formulation failed this test. We do not find his analysis so compelling, however, as to constitute a sufficient basis in itself for discarding the old doctrine. It is not at all clear, as the court below suggested, that expansion of liability in the manner here suggested will lead to a more efficient allocation of resources. As the most astute exponent of this theory has emphasized, a more efficient allocation can only be expected if there is some reason to believe that imposing a particular cost on the enterprise will lead it to consider whether steps should be taken to prevent a recurrence of the accident. Calabresi, The Decision for Accidents: An Approach to Non-fault Allocation of Costs, 78 Harv.L.Rev. 713, 725–34 (1965). And the suggestion that imposition of liability here will lead to more intensive screening of employees rests on highly questionable premises....[5] The unsatisfactory quality of the alloca-

4. Lane disappeared after completing the sentence imposed by a courtmartial and being discharged from the Coast Guard.

5. We are not here speaking of cases in which the enterprise has negligently hired an employee whose undesirable propensities are known or should have been....

tion of resource rationale is especially striking on the facts of this case. It could well be that application of the traditional rule might induce drydock owners, prodded by their insurance companies, to install locks on their valves to avoid similar incidents in the future,[6] while placing the burden on shipowners is much less likely to lead to accident prevention.[7] It is true, of course, that in many cases the plaintiff will not be in a position to insure, and so expansion of liability will, at the very least, serve respondeat superior's loss spreading function.... But the fact that the defendant is better able to afford damages is not alone sufficient to justify legal responsibility ... and this overarching principle must be taken into account in deciding whether to expand the reach of respondeat superior.

A policy analysis thus is not sufficient to justify this proposed expansion of vicarious liability. This is not surprising since respondeat superior, even within its traditional limits, rests not so much on policy grounds consistent with the governing principles of tort law as in a deeply rooted sentiment that a business enterprise cannot justly disclaim responsibility for accidents which may fairly be said to be characteristic of its activities. It is in this light that the inadequacy of the motive test becomes apparent. Whatever may have been the case in the past, a doctrine that would create such drastically different consequences for the actions of the drunken boatswain in *Nelson* and those of the drunken seaman here reflects a wholly unrealistic attitude toward the risks characteristically attendant upon the operation of a ship. We concur in the statement of Mr. Justice Rutledge in a case involving violence injuring a fellow-worker, in this instance in the context of workmen's compensation:

> Men do not discard their personal qualities when they go to work. Into the job they carry their intelligence, skill, habits of care and rectitude. Just as inevitably they take along also their tendencies to carelessness and camaraderie, as well as emotional make-up. In bringing men together, work brings these qualities together, causes frictions between them, creates occasions for lapses into carelessness, and for fun-making and emotional flare-up. * * * These expressions of human nature are incidents inseparable from working together. They involve risks of injury and these risks are inherent in the working environment.

Hartford Accident & Indemnity Co. v. Cardillo, 72 App.D.C. 52, 112 F.2d 11, 15, cert. denied, 310 U.S. 649 (1940);....

Put another way, Lane's conduct was not so ''unforeseeable'' as to make it unfair to charge the Government with responsibility. We agree with a leading treatise that ''what is reasonably foreseeable in this context (of respondeat superior) * * * is quite a different thing from the foreseeably unreasonable risk of harm that spells negligence * * *. The foresight

6. The record reveals that most modern drydocks have automatic locks to guard against unauthorized use of valves.

7. Although it is theoretically possible that shipowners would demand that drydock owners take appropriate action, see Coase, The Problem of Social Cost, 3 J.L. & Economics 1 (1960), this would seem unlikely to occur in real life.

that should impel the prudent man to take precautions is not the same measure as that by which he should perceive the harm likely to flow from his long-run activity in spite of all reasonable precautions on his own part. The proper test here bears far more resemblance to that which limits liability for workmen's compensation than to the test for negligence. The employer should be held to expect risks, to the public also, which arise 'out of and in the course of' his employment of labor.'' 2 Harper & James, The Law of Torts 1377–78 (1956).... Here it was foreseeable that crew members crossing the drydock might do damage, negligently or even intentionally, such as pushing a Bushey employee or kicking property into the water. Moreover, the proclivity of seamen to find solace for solitude by copious resort to the bottle while ashore has been noted in opinions too numerous to warrant citation. Once all this is granted, it is immaterial that Lane's precise action was not to be foreseen.... Consequently, we can no longer accept our past decisions that have refused to move beyond the Nelson rule, ... since they do not accord with modern understanding as to when it is fair for an enterprise to disclaim the actions of its employees.

One can readily think of cases that fall on the other side of the line. If Lane had set fire to the bar where he had been imbibing or had caused an accident on the street while returning to the drydock, the Government would not be liable; the activities of the ''enterprise'' do not reach into areas where the servant does not create risks different from those attendant on the activities of the community in general.... We agree with the district judge that if the seaman ''upon returning to the drydock, recognized the Bushey security guard as his wife's lover and shot him,'' 276 F.Supp. at 530, vicarious liability would not follow; the incident would have related to the seaman's domestic life, not to his seafaring activity, and it would have been the most unlikely happenstance that the confrontation with the paramour occurred on a drydock rather than at the traditional spot. Here Lane had come within the closed-off area where his ship lay, ... to occupy a berth to which the Government insisted he have access, ... and while his act is not readily explicable, at least it was not shown to be due entirely to facets of his personal life. The risk that seamen going and coming from the Tamaroa might cause damage to the drydock is enough to make it fair that the enterprise bear the loss. It is not a fatal objection that the rule we lay down lacks sharp contours; in the end, as Judge Andrews said in a related context, ''it is all a question (of expediency,) * * * of fair judgment, always keeping in mind the fact that we endeavor to make a rule in each case that will be practical and in keeping with the general understanding of Mankind.'' Palsgraf v. Long Island R.R. Co., 248 N.Y. 339, 354–355, 162 N.E. 99, 104, 59 A.L.R. 1253 (1928) (dissenting opinion).

. . .

Affirmed.

NOTE

In Clover v. Snowbird Ski Resort, 808 P.2d 1037 (Utah 1991), Chris Zulliger, an employee of the ski resort, was skiing, at high speed, down an

intermediate slope. He had ignored a sign instructing skiers to ski slowly. He reached a crest in the slope and used it to launch himself into a jump. From where he began the jump he was unable to see his landing area, and by the time he was able to to see where he would land, he was airborne. He struck and severely injured the plaintiff.

The trial court granted summary judgment in favor of the ski resort, on the theory that the employee was not acting within the scope of his employment. The employee was a chef at one of the resort's restaurants and a supervisor of others. He was expected to ski between restaurant locations. Like many other employees, he had a season ski pass. He was an expert skier. After monitoring the Mid–Gad Restaurant on the mountain, he took about four runs and then started to head for the bottom of the mountain, where he was to begin work as a chef at the resort's Plaza Restaurant. It was on his way down the mountain that he took the reckless and fateful jump.

The Supreme Court concluded that summary judgment should not have been granted in favor of the ski resort and remanded for trial. According to the court, the only doubt about scope of employment arose because Zulliger did not return to the Plaza immediately after monitoring the Mid–Gad. It reasoned, however, that a jury could reasonably find that "Zulliger had resumed his employment and that [his] deviation was not substantial enough to constitute a total abandonment of his employment." The court rejected an alternative argument by the plaintiff, based on *Bushey*, that the employer's liability should depend "not on whether the employee's conduct is motivated by serving the employer's interest, but on whether the employee's conduct is foreseeable." The Utah court noted simply that this is not the test under Utah case law.

ANALYSIS

1. Restatement (Second) of Agency § 228 provides that a servant's conduct "is not within the scope of employment if it is ... too little actuated by a purpose to serve the master." In *Bushey*, Judge Friendly acknowledged that no purpose to serve the master could be found in this case—no matter how hard one tried. Apparently, the trial court had likewise concluded that no such purpose could be found. Accordingly, the district court opined, the law should be changed. No longer would plaintiffs be required to show that the agent was motivated by a purpose to serve the master. Instead, it would suffice to show that the conduct arose out of and in the course of the employment. The district court's analysis amounted to virtually a rule of strict liability for the torts of an employee as long as any connection in time and space could be made between the conduct and the employment. Judge Friendly affirmed the district court's result but rejected its rationale, noting that it was not at all clear that the proposed rule would lead to a more efficient allocation of resources. On the other hand, does Judge Friendly articulate a standard different from that of the Restatement?

2. Judge Friendly declines to base the decision on considerations of "policy"—that is, economic incentives and deterrence. Instead, he states that respondeat superior derives from "deeply rooted sentiment that a business enterprise cannot justly disclaim responsibility for accidents which may fairly be said to be characteristic of its activities." What is the significance of the court's use of the word "sentiment"? Where does the court find evidence of this sentiment?

3. In what way was Lane's conduct "characteristic of [the] activities" of the Coast Guard?

4. In the last paragraph of the opinion, the court states, "If Lane had set fire to the bar where he had been imbibing or had caused an accident on the street while returning to the drydock, the Government would not be liable. . . ." Why not? What if Lane and other crew members had gone to the bar to relax after a long and arduous voyage and Lane had acted along with several other crew members in setting the fire negligently?

Manning v. Grimsley

643 F.2d 20 (1st Cir.1981).

In this diversity action involving the law of Massachusetts the plaintiff, complaining that he as a spectator at a professional baseball game was injured by a ball thrown by a pitcher, sought in a battery count and in a negligence count to recover damages from the pitcher and his employer. The district judge directed a verdict for defendants on the battery count and the jury returned a verdict for defendants on the negligence count. The district court having entered judgment for defendants on both counts, the plaintiff appeals from the judgment on the battery count.

(1) In deciding whether the district court correctly directed a verdict for defendants on the battery count, we are to consider the evidence in the light most favorable to the plaintiff. That evidence was to the following effect.

On September 16, 1975 there was a professional baseball game at Fenway Park in Boston between the defendant, the Baltimore Baseball Club, Inc. playing under the name the Baltimore Orioles, and the Boston Red Sox. The defendant Ross Grimsley was a pitcher employed by the defendant Baltimore Club. Some spectators, including the plaintiff, were seated, behind a wire mesh fence, in bleachers located in right field. In order to be ready to pitch in the game, Grimsley, during the first three innings of play, had been warming up by throwing a ball from a pitcher's mound to a plate in the bullpen located near those right field bleachers. The spectators in the bleachers continuously heckled him. On several occasions immediately following heckling Grimsley looked directly at the hecklers, not just into the stands. At the end of the third inning of the game, Grimsley, after his catcher had left his catching position and was walking over to the bench, faced the bleachers and wound up or stretched as though to pitch in the direction of the plate toward which he had been

throwing but the ball traveled from Grimsley's hand at more than 80 miles an hour at an angle of 90 degrees to the path from the pitcher's mound to the plate and directly toward the hecklers in the bleachers. The ball passed through the wire mesh fence and hit the plaintiff.

We, unlike the district judge, are of the view that from the evidence that Grimsley was an expert pitcher, that on several occasions immediately following heckling he looked directly at the hecklers, not just into the stands, and that the ball traveled at a right angle to the direction in which he had been pitching and in the direction of the hecklers, the jury could reasonably have inferred that Grimsley intended (1) to throw the ball in the direction of the hecklers, (2) to cause them imminent apprehension of being hit, and (3) to respond to conduct presently affecting his ability to warm up and, if the opportunity came, to play in the game itself.

The foregoing evidence and inferences would have permitted a jury to conclude that the defendant Grimsley committed a battery against the plaintiff. This case falls within the scope of Restatement Torts 2d § 13, which provides, inter alia, that an actor is subject to liability to another for battery if, intending to cause a third person to have an imminent apprehension of a harmful bodily contact, the actor causes the other to suffer a harmful contact.... It, therefore, was error for the district court to have directed a verdict for defendant Grimsley on the battery count.

[The court holds that the plaintiff is not collaterally estopped by the jury verdict and non-appealed judgment for the defendants on the negligence count.]

It follows that the plaintiff is entitled to a vacation of the judgment on the battery count in favor of the defendant Grimsley.

The plaintiff is also entitled to a vacation of the judgment on the battery count in favor of the Baltimore Club, Grimsley's employer.

(5) In Massachusetts "where a plaintiff seeks to recover damages from an employer for injuries resulting from an employee's assault ... [w]hat must be shown is that the employee's assault was in response to the plaintiff's conduct which was presently interfering with the employee's ability to perform his duties successfully. This interference may be in the form of an affirmative attempt to prevent an employee from carrying out his assignments...." Miller v. Federated Department Stores, Inc., 364 Mass. 340, 349–350, 304 N.E.2d 573 (1973).

(6) The defendant Baltimore Club, relying on its reading of the *Miller* case, contends that the heckling from the bleachers constituted words which annoyed or insulted Grimsley and did not constitute "conduct" and that those words did not "presently" interfere with his ability to perform his duties successfully so as to make his employer liable for his assault in response thereto. Our analysis of the *Miller* case leads us to reject the contention. There a porter, whose duties consisted of cleaning the floors and emptying the trash cans in Filene's basement store, slapped a customer who had annoyed or insulted him by a remark that "If you would say 'excuse me,' people could get out of your way." The Massachusetts Supreme Judicial Court held that while the employee "may have been

annoyed or insulted by'' the customer's remark, ''that circumstance alone does not justify imposition of liability on'' the employer. 364 Mass. 350–351, 304 N.E.2d 573.

Miller's holding that a critical comment by a customer to an employee did not in the circumstances constitute conduct interfering with the employee's performance of his work is obviously distinguishable from the case at bar. Constant heckling by fans at a baseball park would be, within the meaning of *Miller*, conduct. The jury could reasonably have found that such conduct had either the affirmative purpose to rattle or the effect of rattling the employee so that he could not perform his duties successfully. Moreover, the jury could reasonably have found that Grimsley's assault was not a mere retaliation for past annoyance, but a response to continuing conduct which was ''presently interfering'' with his ability to pitch in the game if called upon to play. Therefore, the battery count against the Baltimore Club should have been submitted to the jury.

Vacated and remanded for a new trial on the battery count.

ANALYSIS

1. Restatement (Second) of Agency § 231 provides that a servant's acts ''may be within the scope of employment although consciously criminal or tortious,'' but the comments to that section indicate that ''serious crimes'' are outside the scope. Why? Is Manning v. Grimsley inconsistent with the Restatement?

2. Restatement § 228(2) provides that a servant's use of force against another is within the scope of employment if ''the use of force is not unexpectable by the master.'' Consequently, for example, the owner of a nightclub probably would be held liable for injuries inflicted by a bouncer in ejecting someone from the bar. After all, the owner presumably hired the bouncer for the very purpose of using force to eject drunken or otherwise undesirable patrons. Was Grimley's conduct a use of force that should have been foreseeable by the Club?

3. What could the Club have done to prevent the injury?

4. Once again, if Manning recovers from the Club, what is the likelihood that it would try to recover from Grimsley?

5. Suppose the jury verdict is that Grimsley is liable, but not the Club, and that Grimsley asks the Club to pay the amount he owes. What would you advise the Club?

D. Statutory Claims

Arguello v. Conoco, Inc.

207 F.3d 803 (5th Cir.2000).

The appellants, a group of Hispanic and African–American consumers, filed suit against appellees, Conoco, Inc. (''Conoco'' or ''Conoco, Inc.'')

alleging that they were subjected to racial discrimination while purchasing gasoline and other services. Appellants challenge the district court's 12(b)(6) dismissal of their disparate impact claim under 42 U.S.C. § 2000a, and the district court's grant of summary judgment to Conoco on the appellants remaining 42 U.S.C. §§ 1981 and 2000a claims. For the following reasons we affirm in part, and reverse in part.

FACTUAL AND PROCEDURAL BACKGROUND

There are three different incidents which form the background for this appeal. In March 1995, Denise Arguello (''Arguello''), and her father Alberto Govea (''Govea''), along with various other members of their family stopped at a Conoco-owned store[1] in Fort Worth, Texas. After pumping their gasoline Arguello and Govea entered the store to pay for the gasoline and purchase other items. When Arguello approached the counter she presented the store cashier, Cindy Smith (''Smith''), with her items and a credit card. Smith asked to see Arguello's identification. When Arguello gave Smith her Oklahoma driver's license Smith stated that an out-of-state driver's license was not acceptable identification. Arguello disagreed with Smith and Smith began to insult Arguello using profanity and racial epithets. Smith also knocked a six-pack of beer off the counter toward Arguello. After Arguello retreated from the inside of the store, Smith used the store's intercom system to continue yelling racial epithets. Smith also made obscene gestures through the window.

Moments after the incident occurred Arguello and Govea used a pay phone outside the station to call a Conoco customer service phone number and complain about Smith's conduct. Govea also attempted to reenter the store to discover Smith's name. When Govea attempted to reenter the store, Smith and another store employee locked the doors. Linda Corbin (''Corbin''), a district manager, received Arguello and Govea's complaints. Corbin reviewed video tape from the store, which had no audio, and concluded that Smith had acted inappropriately. When she was confronted by Corbin, Smith admitted to using the profanity, racial epithets, and obscene gestures. Corbin counseled Smith about her behavior but did not suspend, or terminate Smith. Several months after the incident Corbin transferred Smith to another store for Smith's protection after receiving phone calls that a group was planning to picket the store at which the incident took place.

In September 1995, Gary Ivory (''Ivory''), Anthony Pickett (''Pickett''), and Michael Ross (''Ross'') visited a Conoco-branded store in Fort Worth, Texas. While inside the store they allege that they were followed by a store employee and after complaining about this treatment a store employee told them ''we don't have to serve you people'' and ''you people are always acting like this.'' The employee refused to serve them and asked them to

1. We will use the term ''Conoco-owned'' to denote stores that are owned and operated by Conoco, Inc. ''Conoco-branded'' stores are stores which are independently owned marketers of Conoco products and are subject to the Petroleum Marketer Agreements.

leave. Eventually the police were summoned and the policeman ordered the store employee to serve the group.

In November 1996, Manuel Escobedo (''Escobedo'') and Martha Escobedo (''Mrs. Escobedo'') stopped at a Conoco-branded store in San Marcos, Texas. Escobedo claims that while visiting this store the store employee refused to provide toilet paper for the restroom, shouted profanities at his wife, and said ''you Mexicans need to go back to Mexico.'' Escobedo called Conoco to complain about this incident, and was told by a Conoco customer service supervisor, Pamela Harper, that there was nothing Conoco could do because that station was not owned by Conoco. In a separate incident at a Conoco-branded store in Grand Prairie, Texas Escobedo was allegedly told by the store clerk that ''you people steal gas.'' Finally, Escobedo claims that at two Conoco-branded stores in Laredo, Texas he was required to pre-pay for his gasoline while Caucasian customers were allowed to pump their gas first and then pay.

In March 1997, Arguello, Govea, the Escobedos, Ivory, Pickett, and Ross (''plaintiffs'' or ''appellants'') filed suit against Conoco, Inc.... In October 1998, the district court granted summary judgment to Conoco on all of the plaintiffs' remaining claims.

DISCUSSION

Appellants raise several issues on appeal. First, appellants contend that the district court erred in finding no agency relationship between Conoco, Inc. and the Conoco-branded stores. Appellants also argue that the district court erred in finding no agency relationship between Conoco, Inc. and Cindy Smith because Smith acted outside the scope of her employment....

B. Agency Relationship between Conoco, Inc. and Conoco-branded Stores

The incidents involving Ivory, Ross, Pickett and the Escobedos occurred at Conoco-branded stores. These Conoco-branded stores are independently owned, and have entered into Petroleum Marketing Agreements (''PMA'') that allow them to market and sell Conoco brand gasoline and supplies in their stores. The district court held that no agency relationship existed between Conoco, Inc. and the Conoco branded stores. The district court found that Conoco, Inc. did not control the details of the daily operations of the Conoco branded stores, including personnel decisions.

The Supreme Court has suggested that in order to impose liability on a defendant under § 1981 for the discriminatory actions of a third party, the plaintiff must demonstrate that there is an agency relationship between the defendant and the third party. ... [T]o establish an agency relationship between Conoco, Inc. and the branded stores the plaintiffs must show that Conoco, Inc. has given consent for the branded stores to act on its behalf and that the branded stores are subject to the control of Conoco, Inc.

Appellants argue that the PMAs establish that Conoco, Inc. has an agency relationship with the branded stores. They argue that the PMAs give Conoco, Inc. control of the branded stores because the PMAs require the branded stores to maintain their businesses according to the standards

set forth in the PMAs. Plaintiffs further contend that Conoco, Inc. controls the customer service dimension of the Conoco-branded stores. As evidence the plaintiffs point to a statement in the PMA that instructs the branded stores that "all customers shall be treated fairly, honestly, and courteously." Furthermore, the plaintiffs assert that Conoco, Inc. has the power to debrand the Conoco-branded stations for not complying with the contractual terms of the PMA. Thus, because of this debranding power the plaintiffs reason that Conoco controls the operations of their brand marketers in all areas which are discussed in the PMA, including customer service. The plaintiffs also produced summary judgment evidence that Conoco, Inc. conducts random, bi-yearly inspections of the branded stores to determine if business is being conducted in accordance with the standards of the PMA.[6]

Despite the plaintiffs' interpretation of the PMAs and the evidence of inspections, the plain language of the PMA defines the relationship between Conoco, Inc. and its branded stores. The PMA states:

> Marketer [Conoco branded store] is an independent business and is not, nor are its employees, employees of Conoco. Conoco and Marketer are completely separate entities. They are not partners, general partners . . . nor agents of each other in any sense whatsoever and neither has the power to obligate or bind the other.

In the present case, our review of the record and pleadings do not reveal any allegation by the plaintiffs that the language in the PMA is ambiguous as to its meaning. . . . The language of the PMA, while offering guidelines to the Conoco-branded stores, does not establish that Conoco, Inc. has any participation in the daily operations of the branded stores nor that Conoco, Inc. participates in making personnel decisions.

Therefore, we find that there is no agency relationship between Conoco, Inc. and the branded stores in question, and that Conoco, Inc. as a matter of law cannot be held liable for the unfortunate incidents which happened to Ivory, Pickett, Ross, and the Escobedos at the Conoco-branded stores.

C. Scope of Employment

Arguello and Govea complain of discriminatory treatment at a Conoco-owned store. Appellants argue that the district court erred in finding that Conoco could not be held liable . . . for the acts of its store clerk, Smith. The district court found that as a matter of law there was no agency relationship between Smith and Conoco because Smith's acts of discrimination towards Arguello and Govea were outside the scope of Smith's employment. . . .

Under general agency principles a master is subject to liability for the torts of his servants while acting in the scope of their employment. See Restatement § 219. Some of the factors used when considering whether an

6. These inspections normally focus on product displays and labeling. Customer service is not considered a main focus of the random inspections.

employee's acts are within the scope of employment are: 1) the time, place and purpose of the act; 2) its similarity to acts which the servant is authorized to perform; 3) whether the act is commonly performed by servants; 4) the extent of departure from normal methods; and 5) whether the master would reasonably expect such act would be performed.

First, we must consider the time, place and purpose of Smith's actions. Smith's behavior toward Arguello and Govea occurred while she was on duty inside of the Conoco station where she was employed. The plaintiffs also put forth summary judgment evidence that Smith asked Arguello to present identification for credit card purchases. The purpose of Smith's interaction with Arguello was to complete the sale of gas and other store items. The initial confrontation and subsequent use of racial epithets occurred while Smith was completing Arguello's purchase of her items and processing the credit card transaction.

Second, we must consider whether Smith's actions were similar to those she was authorized by Conoco to perform. The sale of gasoline, other store items, and the completion of credit card purchases are the customary functions of a gasoline store clerk. The plaintiffs presented summary judgment evidence that Smith also used the intercom, which is also a customary action of gasoline store clerks.

Third, we will examine the extent of Smith's departure from normal methods. It is self-evident that Smith did not utilize the normal methods for conducting a sale. There was no summary judgment evidence presented that Conoco expected or anticipated that Smith would perform her functions in this manner. The appellees would have this court adopt the position that because Smith's use of racial epithets is comparable to the commission of an intentional tort, Conoco should not be held liable for Smith's behavior. However, the fact that an employee engages in intentional tortious conduct does not require a finding that the employee was outside the scope of his employment. . . . [A]lthough Conoco could not have expected Smith to shout racial epithets at Arguello and Govea, Smith's actions took place while she was performing her normal duties as a clerk. Conoco, Inc. had authorized Smith to interact with customers as they made purchases. Therefore, although Smith did depart from the normal methods of conducting a purchase this does not lead to the conclusion that as a matter of law she was outside the scope of her employment.

Finally, we must consider whether Conoco could have reasonably expected Smith to act in a racially discriminatory manner. There is no evidence in the record on this prong of the test. However, we note that even if Conoco is able to show that they could not have expected this conduct by Smith, the jury is entitled to find that the other factors outweigh this consideration.

In assessing whether Smith was within the scope of her employment the district court found that the only summary judgment evidence presented by the plaintiffs was that Smith was working in her job as cashier when the offensive behavior occurred. The district court concluded that the summary judgment evidence was insufficient to "overcome the common-

sense conclusion'' that Smith's offensive actions were not within the scope of her employment. However, we reject the presumption that because Smith behaved in an unacceptable manner that she was obviously outside the scope of her employment. The plaintiffs did present summary judgment evidence that Smith was on duty as a clerk, and that she was performing authorized duties such as conducting sales. This summary judgment evidence is not insignificant. Smith's position as clerk, and her authorization from Conoco to conduct sales allowed her to interact with Arguello and Govea, and put Smith in the position to commit the racially discriminatory acts. The plaintiffs also presented summary judgment evidence that Smith used her authority to conduct credit card transactions and use the gas station intercom system to commit the acts in question.

It is also important to note that Conoco does not challenge whether this incident occurred. Smith admitted to a Conoco district manager that she did subject Arguello and Govea to the use of racial epithets, profanity, and obscene gestures. The only dispute is whether there is a legal remedy for Arguello and Govea by holding Conoco liable for Smith's actions. The plaintiffs contend that the inference that should be drawn from Smith's actions is that Smith was authorized by Conoco to perform the actions of a clerk and that this meant that her actions while on duty as clerk were within the scope of her employment. Conoco, utilizing the same facts asks us to draw the inference that because Smith was acting on personal racial bigotry and animosity that she was outside the scope of her employment.

[The court holds that summary judgment should not have been granted in favor of Conoco on the agency relationship and scope of employment.]

ANALYSIS

1. Do you agree with the court's conclusion that the Conoco-branded stores were not agents of Conoco? Is that decision here consistent with the franchise cases, such as Murphy v. Holiday Inns, Inc., or the gas station cases, i.e., Humble Oil & Refining Co. v. Martin and Hoover v. Sun Oil Company?

2. Do you agree with the court's conclusion that Smith acted within the scope of her employment?

E. LIABILITY FOR TORTS OF INDEPENDENT CONTRACTORS

Majestic Realty Associates, Inc. v. Toti Contracting Co.

30 N.J. 425, 153 A.2d 321 (1959).

Plaintiffs Majestic Realty Associates, Inc., and Bohen's Inc., owner and tenant, sought compensation from defendants Toti Contracting Co., Inc. and Parking Authority of the City of Paterson, New Jersey, for damage to Majestic's building and to Bohen's goods. The claim arose out of the

activity of Toti in demolishing certain structures owned by the Authority. . . .

Majestic is the owner of the two-story premises at 297 Main Street, Paterson, New Jersey. Bohen's is the tenant of the first floor and basement thereof in which it conducted a dry goods business. The Authority acquired properties along Main Street beginning immediately adjacent to Majestic's building on the south and continuing to Ward Street, the next intersecting street, and then east on the latter street for 150 feet. The motive for the acquisition was to establish a public parking area. Main Street is one of the principal business arteries of the city and the locality was completely built up.

Accomplishment of the Authority's object required demolition of the several buildings on both streets. Some time prior to October 26, 1956, a contract was entered into by the Authority with Toti to do the work. The razing began on the Ward Street side and moved northwardly until the structure next to Majestic's premises was reached. It was at least a story (about 20 feet) higher than Majestic's roof; the northerly wall of the one was "right up against" the southerly wall of the other and the two walls ran alongside each other for 40 feet.

In the process of leveling this adjacent building, the contractor first removed the roof, then the front and south sidewalls and all of the interior partitions and floors. Thus, the north wall of brick and masonry next to Majestic's structure was left standing free. Expert testimony was adduced to show that the proper method of demolition under the existing circumstances would have been to remove the roof, leaving the interior partition work for support, and to begin to take the north wall down "never leaving any portion (of it) at a higher point than the interior construction of the building would form a brace."

In demolishing the walls, Toti used a large metal ball, said to weigh 3,500 pounds, suspended from a crane which was stationed in the street. There was testimony that during the week prior to the accident, every time the ball would strike a wall, debris and dirt would fly and the Majestic building "rocked." Further expert testimony indicated that in dealing with the free-standing north wall, the ball should have been made to hit the very top on each occasion so as to level it a few bricks at a time. This course was followed at first; the ball was swung from north to south and the dislodged bricks were catapulted away from Majestic's building and onto the adjoining lot. After a time, work ceased for a few minutes. On resumption, the operator of the crane swung the ball in such a manner that it struck at a point some 15 feet below the top of the wall. The impact propelled the uppermost section of the wall back in the direction from which the blow had come with the result that a 15 by 40 foot section fell on Majestic's roof, causing a 25 by 40 foot break therein. One of Bohen's employees, who saw the incident, asked the crane operator in the presence of Toti's president: "What did you do to our building?" He replied, "I goofed."

In characterizing a demolition undertaking of this type in a built up and busy section of a city, and in particular where one building to be razed

adjoined another which was to remain untouched, plaintiffs' expert witness said it was ''hazardous work''; ''one of the most hazardous operations in the building business.'' And with reference to the leveling of a building so close to another structure which was not to be harmed, he asserted that the recognized procedure is to take it down in small sections so as not to lose control of the operation. This standard conforms with N.J.S.A. 34:5–15 which specifies that ''(i)n the demolition of buildings, walls shall be removed part by part.''

On the proof outlined, the trial court recognized that the work was hazardous in its very nature, but did not feel that it constituted a nuisance per se. Therefore, he ruled that the Authority, not having had or exercised control over the manner and method or means of performing the demolition operation, could not be held for the negligent act of its independent contractor. [The Appellate Division reversed.]

The problem must be approached with an awareness of the long settled doctrine that ordinarily where a person engages a contractor, who conducts an independent business by means of his own employees, to do work not in itself a nuisance (as our cases put it), he is not liable for the negligent acts of the contractor in the performance of the contract.... Certain exceptions have come to be accepted, i.e., (a) where the landowner retains control of the manner and means of the doing of the work which is the subject of the contract; (b) where he engages an incompetent contractor, or (c) where, as noted in the statement of the general rule, the activity contracted for constitutes a nuisance per se....

As to exception (b), noted above, it is not claimed that the proof makes out a jury question on the charge that an incompetent contractor was hired for the task of demolition. Incidental comment thereon, however, may be fruitful.

It has been intimated that the matter of the competency of a contractor should not be restricted to considerations of skill and experience but should encompass financial responsibility to respond to tort claims as well. Research has not disclosed a case where the proposal has been applied....

Inevitably the mind turns to the fact that the injured third party is entirely innocent and that the occasion for his injury arises out of the desire of the contractee to have certain activities performed. The injured has no control over or relation with the contractor. The contractee, true, has no control over the doing of the work and in that sense is also innocent of the wrongdoing; but he does have the power of selection and in the application of concepts of distributive justice perhaps much can be said for the view that a loss arising out of the tortious conduct of a financially irresponsible contractor should fall on the contractee. Professor Morris, in ''Torts of Independent Contractors,'' [29 Ill. L. Rev. 339, 344 (1934)], put it this way:

> If the contractee has to look out for the interests of others by using due care to pick a man with requisite skill to whom to entrust his enterprises, why should he not also have to look out for the

> interests of others by selecting a man with sufficient financing? And since there is usually a fool proof method of assuring himself that the contractor will meet all tort obligations in requiring an indemnity bond signed by responsible sureties, it would seem that in most cases the contractee would only measure up to the standard of due care so as to avoid responsibility when the contractor is able to discharge tort claims arising out of the enterprise.

This passage was written in 1934. At the present time it is a matter of common knowledge that liability insurance to cover such demolition operations is available to contractors and it may be assumed fairly that procurement of that type coverage is regarded as an ordinary business expense. Financial responsibility has nothing to do with legal liability of the contractor. . . .

But this precise facet of the problem of Toti's competency was not raised at the trial or in the briefs. It arose as an emanation of the oral argument. Consequently, no decision is rendered with respect to it and the matter is expressly reserved.

Under exception (c), on which plaintiffs rely principally, liability will be imposed upon the landowner in spite of the engagement of an independent contractor if the work to be done constitutes a nuisance per se. The phrase "nuisance per se," although used with some frequency in the reported cases, is difficult of definition. . . .

Without undertaking an exhaustive review of the cases in our State where the expression appears, it seems proper to say that the legal content of "nuisance per se" and the application thereof in a factual framework such as that now before us, is anything but clear. . . . In Sarno v. Gulf Refining Co., 99 N.J.L. 340, 342 (Sup. Ct. 1924), affirmed 102 N.J.L. 223 (E. & A. 1925), the court equated it with "inherently dangerous" and this appears to have set in motion a trend toward the view now espoused by the Restatement, Torts, §§ 835(e), 416.

Section 416 of the Restatement propounds a rule which would impose liability upon the landowner who engages an independent contractor to do work which he should recognize as necessarily requiring the creation during its progress of a condition involving a peculiar risk of harm to others unless special precautions are taken, if the contractor is negligent in failing to take those precautions. Such work may be said to be inherently dangerous, i.e., an activity which can be carried on safely only by the exercise of special skill and care, and which involves grave risk of danger to persons or property if negligently done. . . .

It is important to distinguish an operation which may be classed as inherently dangerous from one that is ultra-hazardous. The latter is described as one which "(a) necessarily involves a serious risk of harm to the person, land or chattels of others which cannot be eliminated by the exercise of the utmost care, and (b) is not a matter of common usage." Restatement, supra, § 520. The distinction is important because liability is absolute where the work is ultra-hazardous, ...

There is no doubt that the line between work which is ordinary, usual and commonplace, and that which is inherently dangerous because its very nature involves a peculiar and high risk of harm to members of the public or adjoining proprietors of land unless special precautions are taken, is somewhat shadowy.... For the present, we need deal only with the case before us.... The current New York rule is that the razing of buildings in a busy, built up section of a city is inherently dangerous within the contemplation of section 416 of the Restatement.... In our judgment, the doctrine adopted by New York ... represents the sound and just concept to be applied.

ANALYSIS

1. Under exception (b), for cases in which the principal retained an incompetent contractor, is the principal liable simply upon a showing that the contractor was incompetent? Or should plaintiff be obliged to show that the principal was negligent in selecting an incompetent contractor?

2. Do you agree with the court's dicta implying that hiring a financially irresponsible contractor is tantamount to hiring one who is incompetent? If not, why not? In answering that question, it may be helpful to consider the following: As between Majestic and the Authority, which was best able to monitor Toti's conduct? As between Majestic and the Authority, which was in the best position to insure against these sorts of accidents?

3. Under exception (c), for inherently dangerous activities, is the principal liable simply because the contractor was negligent in failing to take adequate precautions? Or should plaintiff be obliged to show negligence on the principal's part?

4. In light of this decision, what should the Authority do in the future when hiring independent contractors to conduct hazardous activities?

5. Do the exceptions recognized by the *Majestic* opinion swallow the rule that principals are not liable for the tortious acts of their independent contractors?

Section 4. Fiduciary Obligation of Agents

We now shift our attention to the fiduciary obligation, or duty of loyalty, owed by agents to their principals. Note that several of the cases to be examined involve agents of corporate principals. They are included in this text because the fact that the principal is a corporation, rather than an individual, is unimportant.

A. Duties During Agency

Reading v. Regem

[1948] 2 KB 268, [1948] 2 All ER 27, [1948] WN 205.

The plaintiff joined the army in 1936, and at the beginning of 1944 he was a sergeant in the Royal Army Medical Corps stationed at the general hospital in Cairo, where he was in charge of the medical stores.*

The plaintiff had not had any opportunities, in his life as a soldier, of making money, but in March, 1944, there were found standing to his credit at banks in Egypt, several thousands of pounds, and he had more thousands of pounds in notes in his flat. He had also acquired a motor car worth £1,500. The Special Investigation Branch of the army looked into the matter, and he was asked how he came by these moneys. He made a statement, from which it appears that they were paid to him by a man by the name of Manole in these circumstances. A lorry used to arrive loaded with cases, the contents of which were unknown. Then the plaintiff, in full uniform, boarded the lorry, and escorted it through Cairo, so that it was able to pass the civilian police without being inspected. When it arrived at its destination, it was unloaded, or the contents were transferred to another lorry. After the first occasion when this happened, the plaintiff saw Manole in a restaurant in Cairo. Manole handed him an envelope which he put in his pocket. On examining it when he arrived home, he found that it contained £2,000. Two or three weeks later, another load arrived, and another £2,000 was paid. £3,000 was paid after the third load, and so it went on until eventually some £20,000 had gone into the pocket of the suppliant. The services which he rendered for that money were that he accompanied this lorry from one part of Cairo to another, and it is plain that he got it because he was a sergeant in the British army, and, while in uniform, escorted these lorries through Cairo. It is also plain that he was clearly violating his duty in so doing. The military authorities took possession of the money. . . .

* [Eds.—Cognizant of Winston Churchill's dictum that the United States and the United Kingdom are "separated by a common language," we have taken the liberty of converting some British legal terms into their American equivalents.]

In this petition of right, the plaintiff alleges that these moneys are his and should be returned to him by the Crown. In answer, the Crown say: ''These were bribes received by you by reason of your military employment, and you hold the money for the Crown. Even if we were wrong in the way in which we seized them, we are entitled to recover the amount of them, and to set off that amount against any claim you may have.'' In these circumstances, it is not necessary to dwell on the form of the claim. The question is whether or not the Crown is entitled to the money. It is not entitled to it simply because it is the Crown moneys which are unlawfully obtained are not ipso facto forfeited to the Crown. The claim of the Crown rests on the fact that at the material time it was the plaintiff's employer.

. . . In my judgment, it is a principle of law that, if a servant takes advantage of his service and violates his duty of honesty and good faith to make a profit for himself, in the sense that the assets of which he has control, the facilities which he enjoys, or the position which he occupies, are the real cause of his obtaining the money as distinct from merely affording the opportunity for getting it, that is to say, if they play the predominant part in his obtaining the money, then he is accountable for it to his master. It matters not that the master has not lost any profit nor suffered any damage, nor does it matter that the master could not have done the act himself. If the servant has unjustly enriched himself by virtue of his service without his master's sanction, the law says that he ought not to be allowed to keep the money, but it shall be taken from him and given to his master, because he got it solely by reason of the position which he occupied as a servant of his master. Instances readily occur to mind. Take the case of the master who tells his servant to exercise his horses, and while the master is away, the servant lets them out and makes a profit by so doing. There is no loss to the master, the horses have been exercised, but the servant must account for the profits he makes.

The ATTORNEY–GENERAL put in argument the case of a uniformed policeman who, at the request of thieves and in return for a bribe, directs traffic away from the site of the crime. Is he to be allowed to keep the money? So, also, here, the use of the facilities provided by the Crown in the shape of the uniform and the use of his position in the army were the only reason why the plaintiff was able to get this money. It was solely on that account that he was able to sit in the front of these lorries and give them a safe conduct through Cairo. There was no loss of profit to the Crown. The Crown would have been violating its duty if it had undertaken the task, but the plaintiff was certainly violating his duty, and it is money which must be paid over to his master—in this case, the Crown.

. . . The uniform of the Crown and the position of the plaintiff as a servant of the Crown were the only reasons why he was able to get this money, and that is sufficient to make him liable to hand it over to the Crown. The case is to be distinguished from cases where the service merely gives the opportunity of making money. A servant may, during his master's time, in breach of his contract, do other things to make money for himself, such as gambling, but he is entitled to keep that money himself. The

master has a claim for damages for breach of contract, but he has no claim to the money. So, also, the fact that a soldier is stationed in a certain place may give him the opportunity, contrary to the King's Regulations, of engaging in trade and making money in that way. In such a case, the mere fact that his service gave the opportunity for getting the money would not entitle the Crown to it, but if, as here, the wearing of the King's uniform and his position as a soldier is the sole cause of his getting the money and he gets it dishonestly, that is an advantage which he is not allowed to keep. Although the Crown, has suffered no loss, the court orders the money to be handed over to the Crown, because the Crown is the only person to whom it can properly be paid. The plaintiff must not be allowed to enrich himself in this way. He got the money by virtue of his employment, and must hand it over.

DISPOSITION: Petition dismissed with costs.

ANALYSIS

1. The court opines, the sergeant "must not be allowed to enrich himself in this way." Why not?

2. Would a different result obtain under U.S. agency law? Consider Restatement (Third) of Agency § 8.02:

> An agent has a duty not to acquire a material benefit from a third party in connection with transactions conducted or other actions taken on behalf of the principal or otherwise through the agent's use of the agent's position.

Restatement (Third) § 8.05 may also be relevant: "An agent has a duty (1) not to use property of the principal for the agent's own purposes or those of a third party . . . ."

3. Why should the Crown be able to recover even though it "suffered no loss"? Put another way, why is the remedy disgorgement of secret profits rather than actual damages?

PROBLEMS

How, if at all, would you distinguish the following cases from Reading v. Regem?

1. The facts are the same as in the actual case, except that the sergeant had been discharged by the Royal Army before riding along in the smuggler's truck. Would it make a difference if discharged personnel were permitted to wear their uniforms for 30 days, to ease the transition to civilian life?

2. Imagine a U.S. Army Sergeant who, during the Gulf War, single-handedly wiped out an enemy machine gun emplacement; earned the Congressional Medal of Honor; received huge coverage in newspapers and magazines and on television; and became a public hero. One night, while in New York, he went to a popular restaurant, in uniform. The owner of the

restaurant called reporters, who arrived and took pictures, which appeared in papers across the country the next day. As the sergeant left the restaurant, the owner gave him an envelope with $1,000 in cash and urged him to return. (And, of course, the owner would not let him pay for his food and drinks.) The sergeant returned many times and received a total of $10,000 in cash.

3. General Norman Schwarzkopf, culminating a long, distinguished career in the U.S. Army, became well known to the public as head of the U.S. military forces in the Gulf War. After that war he published his autobiography, ''It Doesn't Take a Hero,'' for which he presumably received substantial royalties. Assume that, to promote the book, he appeared at various gatherings and on television, always in civilian clothes.

4. Suppose that the long-time Chief Executive Officer of a major corporation authored a book about his experience as CEO and about the principles that he followed in guiding the corporation to its enormous success. The CEO earned substantial royalties, which he gave to charity.

5. Michael Jordan received substantial royalties for the use of his name by a restaurant in Chicago.

6. Suppose an expert witness appeared in court and was identified as a Harvard Law School professor. Her fee for two days of preparation and one day in court was $100,000.

7. A senior executive in an oil company learned that the company's geologists had discovered a huge oil field, but were required to maintain secrecy until the company could buy the drilling rights. The executive bought shares of stock of the company and, after the announcement of the discovery several months later, sold those shares for a large profit.

General Automotive Manufacturing Co. v. Singer

19 Wis.2d 528, 120 N.W.2d 659 (1963).

Action commenced by General Automotive Manufacturing Company, hereinafter referred to as ''Automotive,'' against John Singer, a former employee, to account for secret profits received while in its employ. Trial was to the court without a jury, which found defendant liable to plaintiff for $64,088.08 and costs. Appeal is from that judgment.

Automotive, plaintiff-respondent, is a Wisconsin corporation engaged in the machine shop jobbing business and has about five employees. Louis Glavin controlled Automotive and was its secretary.

John Singer, defendant-appellant, is a machinist-consultant and manufacturer's representative. Singer has worked in the machine shop field for over thirty years. He is adept at machine work and had ability not only as a machinist but also as to metal treatment, grinding techniques and special techniques. He enjoys this reputation in machine shop circles. None of Automotive's employees has defendant's ability to handle these machines.

He is also known to be qualified in estimating the costs of machine-shop products and the competitive prices for which such products can be sold.

. . .

We have carefully reviewed the evidence and have ourselves reached conclusions as stated by the trial court and set forth in its Findings of Fact, as follows:

> "3. That heretofore and on or about the 28th day of March 1953, the plaintiff hired and employed the defendant as general manager of its business and affairs and the defendant accepted such employment under and pursuant to a written contract.
>
> . . .
>
> "6. That in and by said contract as aforesaid, the plaintiff promised and agreed to pay to the defendant as compensation, a fixed monthly salary together with a sum equal to 3% of the gross sales of the plaintiff.
>
> . . .
>
> "8. That in and by said contract, in consideration of compensation to be paid by the plaintiff to the defendant, the defendant promised and agreed:
>
> > "A. To devote his entire time, skill, labor and attention to said employment, during the term of this employment, and not to engage in any other business or vocation of a permanent nature during the term of this employment, and to observe working hours for 5½ days.
> >
> > "B. Not to, either during the term of his employment, or at any time thereafter, disclose to any person, firm or corporation any information concerning the business or affairs of the Employer which he may have acquired in the course of or as incident to his employment hereunder, for his own benefit, or to the detriment or intended or probable detriment of the Employer."
>
> . . .

Although stated as a Finding of Fact, Finding No. 10 is mainly a conclusion of law. It produces the principal issue in the case and deserves further discussion. It reads:

> "10. That the defendant breached his contract of employment with the plaintiff and violated the duty of loyalty which he owed to the plaintiff and his fiduciary duty of general manager thereof during the existence of such employment by engaging in business activities directly competitive with the plaintiff, to-wit by obtaining orders from a customer for his own account."

The record leaves no room for doubt of the correctness of Finding 11, as follows:

"11. That thereafter, instead of turning such orders over to the plaintiff the defendant turned such orders over to other concerns to be filled, collected the proceeds thereof from the customers for his own account and kept the profits accruing therefrom."

Finding 12 is: "That such activities of the defendant were carried on in secret and without the knowledge of the plaintiff."

The evidence on which Finding 12 is based is in dispute. It is not against the great weight and clear preponderance of the evidence and the finding should not be disturbed.

. . .

Study of the record discloses that Singer was engaged as general manager of Automotive's operations. Among his duties was solicitation and procurement of machine shop work for Automotive. Because of Singer's high reputation in the trade he was highly successful in attracting orders.

Automotive is a small concern and has a low credit rating. Singer was invaluable in bolstering Automotive's credit. For instance, when collections were slow for work done by Automotive Singer paid the customer's bill to Automotive and waited for his own reimbursement until the customer remitted. Also, when work was slack, Singer set Automotive's shop to make parts for which there were no present orders and himself financed the cost of materials for such parts, waiting for recoupment until such stock-piled parts could be sold. Some parts were never sold and Singer personally absorbed the loss upon them.

As time went on a large volume of business attracted by Singer was offered to Automotive but which Singer decided could not be done by Automotive at all, for lack of suitable equipment, or which Automotive could not do at a competitive price. When Singer determined that such orders were unsuitable for Automotive he neither informed Automotive of these facts nor sent the orders back to the customer. Instead, he made the customer a price, then dealt with another machine shop to do the work at a less price, and retained the difference between the price quoted to the customer and the price for which the work was done. Singer was actually behaving as a broker for his own profit in a field where by contract he had engaged to work only for Automotive. We concur in the decision of the trial court that this was inconsistent with the obligations of a faithful agent or employee.

Singer finally set up a business of his own, calling himself a manufacturer's agent and consultant, in which he brokered orders for products of the sort manufactured by Automotive,—this while he was still Automotive's employee and without informing Automotive of it. Singer had broad powers of management and conducted the business activities of Automotive. In this capacity he was Automotive's agent and owed a fiduciary duty to it. . . . Under his fiduciary duty to Automotive Singer was bound to the exercise of the utmost good faith and loyalty so that he did not act adversely to the interests of Automotive by serving or acquiring any private interest of his own. . . . He was also bound to act for the furtherance and advancement of the interest of Automotive. . . .

If Singer violated his duty to Automotive by engaging in certain business activities in which he received a secret profit he must account to Automotive for the amounts he illegally received. . . .

The present controversy centers around the question whether the operation of Singer's side line business was a violation of his fiduciary duty to Automotive. The trial court found this business was conducted in secret and without the knowledge of Automotive. . . .

The trial court found that Singer's side line business, the profits of which were $64,088.08, was in direct competition with Automotive. However, Singer argues that in this business he was a manufacturer's agent or consultant, whereas Automotive was a small manufacturer of automotive parts. The title of an activity does not determine the question whether it was competitive but an examination of the nature of the business must be made. In the present case the conflict of interest between Singer's business and his position with Automotive arises from the fact that Singer received orders, principally from a third-party called Husco, for the manufacture of parts. As a manufacturer's consultant he had to see that these orders were filled as inexpensively as possible, but as Automotive's general manager he could not act adversely to the corporation and serve his own interests. On this issue Singer argues that when Automotive had the shop capacity to fill an order he would award Automotive the job, but he contends that it was in the exercise of his duty as general manager of Automotive to refuse orders which in his opinion Automotive could not or should not fill and in that case he was free to treat the order as his own property. However, this argument ignores, as the trial court said, "defendant's agency with plaintiff and the fiduciary duties of good faith and loyalty arising therefrom."

Rather than to resolve the conflict of interest between his side line business and Automotive's business in favor of serving and advancing his own personal interests, Singer had the duty to exercise good faith by disclosing to Automotive all the facts regarding this matter. . . . Upon disclosure to Automotive it was in the latter's discretion to refuse to accept the orders from Husco or to fill them if possible or to sub-job them to other concerns with the consent of Husco if necessary, and the profit, if any, would belong to Automotive. Automotive would then be able also to decide whether to expand its operations, install suitable equipment, or to make further arrangements with Singer or Husco. By failing to disclose all the facts relating to the orders from Husco and by receiving secret profits from these orders, Singer violated his fiduciary duty to act solely for the benefit of Automotive. Therefore he is liable for the amount of the profits he earned in his side line business.

. . .

During the trial the parties stipulated that in the event the court should find that Automotive was entitled to recover profits realized by Singer in his side line business, Singer should be given a credit equal to three percent of the gross sales of that business. Based upon this stipulation the sum of $64,088.08 would be reduced by $10,183. . . .

Judgment . . . affirmed.

ANALYSIS

1. The court says that when Singer received an order that he thought the corporation could not fill, he was supposed to tell someone higher up about it. What is the point of that observation?

2. Paragraph 8A of the employment contract has two parts: "devote his entire time . . ." and "not to engage in any other business. . . ." What is the relationship between these two parts? Are they redundant? What is the effect of the phrase "of a permanent nature"?

3. Finding of Fact 10 states that Singer "breached his contract of employment" and "violated [his] duty of loyalty." Would either legal theory be sufficient to support the result (Singer's liability)? What difference would it have made if the court had rested its decision on one or the other of the two theories? Would it have been possible to conclude that Singer had breached his contract without violating his duty of loyalty, or vice versa?

4. Suppose that before Singer was hired, he and the owner of General Automotive had consciously and expressly addressed the possibility that Singer would receive offers of work that he would consider beyond General Automotive's capability. Suppose further that it was clear that it would not have been feasible for Singer to consult with the owner, or any representative of the owner, on what to do with such offers. It is conceivable that the parties might have agreed that Singer would simply turn down these offers. It is also conceivable that they would have agreed that Singer could act as broker, as he did in the actual case, and keep all the profit. Which of these two alternatives seems more likely? Which is more likely to lead to optimal results for both parties? What other solution might you suggest and why?

5. The rule applied by the court is a default rule—that is, one that applies in the absence of agreement. Some default rules reduce the costs of contracting, and achieve fairness, by approximating as closely as possible the provision that the parties would have adopted had they addressed the matter. Other default rules do not have this characteristic but instead are calculated to induce one or the other party to reveal his or her wishes to the other and seek agreement. Into which category does the rule in this case fall?

B. DUTIES DURING AND AFTER TERMINATION OF AGENCY: HEREIN OF "GRABBING AND LEAVING"

Town & Country House & Home Service, Inc. v. Newbery

3 N.Y.2d 554, 170 N.Y.S.2d 328, 147 N.E.2d 724 (1958).

This action was brought for an injunction and damages against appellants on the theory of unfair competition. The complaint asks to restrain

them from engaging in the same business as plaintiff, from soliciting its customers, and for an accounting and damages. The individual appellants were in plaintiff's employ for about three years before they severed their relationships and organized the corporate appellant through which they have been operating. The theory of the complaint is that plaintiff's enterprise "was unique, personal and confidential," and that appellants cannot engage in business at all without breach of the confidential relationship in which they learned its trade secrets, including the names and individual needs and tastes of its customers.

The nature of the enterprise is house and home cleaning by contract with individual householders. Its "unique" quality consists in superseding the drudgery of ordinary house cleaning by mass production methods. The house cleaning is performed by a crew of men who descend upon a home at stated intervals of time, and do the work in a hurry after the manner of an assembly line in a factory. They have been instructed by the housewife but work without her supervision. The householder is supplied with liability insurance, the secrets of the home are kept inviolate, the tastes of the customer are served and each team of workmen is selected as suited to the home to which it is sent. The complaint says that the customer relationship is "impregnated" with a "personal and confidential aspect."

The complaint was dismissed at Special Term on the ground that the individual appellants were not subjected to negative covenants under any contract with plaintiff, and that the methods and techniques used by plaintiff in conducting its business are not confidential or secret as in the case of a scientific formula; that house cleaning and housekeeping "are old and necessary chores which accompany orderly living" and that no violation of duty was involved in soliciting plaintiff's customers by appellants after resigning from plaintiff's employ. The contacts and acquaintances with customers were held not to have been the result of a confidential relationship between plaintiff and defendants or the result of the disclosure of secret or confidential material.

By a divided vote the Appellate Division reversed, but on a somewhat different ground, namely, that while in plaintiff's employ, appellants conspired to terminate their employment, form a business of their own in competition with plaintiff and solicit plaintiff's customers for their business. The overt acts under this conspiracy were found by the Appellate Division to have been that, in pursuance of this plan, they formed the corporate appellant and bought equipment and supplies for their operations—not on plaintiff's time—but during off hours, before they had severed their relations as employees of plaintiff. The Appellate Division concluded that "it is our opinion that their agreement and encouragement to each other to carry out the course of conduct thus planned by them, and their consummation of the plan, particularly their termination of employment virtually en masse, were inimical to, and violative of, the obligations owed by them to appellant as its employees; and that therefore appellant was entitled to relief." . . .

Although the Appellate Division implied more relief than we consider to have been warranted, we think that the trial court erred in dismissing the complaint altogether. The only trade secret which could be involved in this business is plaintiff's list of customers. Concerning that, even where a solicitor of business does not operate fraudulently under the banner of his former employer, he still may not solicit the latter's customers who are not openly engaged in business in advertised locations or whose availability as patrons cannot readily be ascertained but "whose trade and patronage have been secured by years of business effort and advertising, and the expenditure of time and money, constituting a part of the good will of a business which enterprise and foresight have built up" (Witkop & Holmes Co. v. Boyce, 61 Misc. 126, 131, 112 N.Y.S. 874, 878, affirmed 131 App.Div. 922, 115 N.Y.S. 1150, . . .). . . .

The testimony in the instant record shows that the customers of plaintiff were not and could not be obtained merely by looking up their names in the telephone or city directory or by going to any advertised locations, but had to be screened from among many other housewives who did not wish services such as respondent and appellants were equipped to render, but preferred to do their own housework. In most instances housewives do their own house cleaning. The only appeal which plaintiff could have was to those whose cleaning had been done by servants regularly or occasionally employed, except in the still rarer instances where the housewife was on the verge of abandoning doing her own work by hiring some outside agency. In the beginning, prospective customers of plaintiff were discovered by Dorothy Rossmoore, wife of plaintiff's president, by telephoning at random in "sections of Nassau that we thought would be interested in this type of cleaning, and from that we got directories, town directories, and we marked the streets that we had passed down, and I personally called, right down the list." In other words, after selecting a neighborhood which they felt was fertile for their kind of business, they would telephone to all of the residents of a street in the hope of discovering likely prospects. On the first day Mrs. Rossmoore called 52 homes. If she enlisted their interest, an appointment would be made for a personal call in order to sell them the service. At the end of the first year, only 40 to 50 customers had thus been secured. Two hundred to three hundred telephone calls netted 8 to 12 customers. Moreover, during the first year it was not possible to know how much to charge these customers with accuracy, inasmuch as the cleaning requirements of each differed from the others, so that special prices had to be set. In the beginning the customer usually suggested the price which was paid until some kind of cost accounting could demonstrate whether it should be raised or lowered. These costs were entered on cards for every customer, and this represented an accumulated body of experience of considerable value. After three years of operation, and by August, 1952, when the individual appellants resigned their employment by plaintiff, the number of customers amounted to about 240. By that time plaintiff had 7 or 8 crews doing this cleaning work, consisting of 3 men each.

Although appellants did not solicit plaintiff's customers until they were out of plaintiff's employ, nevertheless plaintiff's customers were the only ones they did solicit. Appellants solicited 20 or 25 of plaintiff's customers who refused to do business with appellants and about 13 more of plaintiff's customers who transferred their patronage to appellants. These were all the people that appellants' firm solicited. It would be different if these customers had been equally available to appellants and respondent, but, as has been related, these customers had been screened by respondent at considerable effort and expense, without which their receptivity and willingness to do business with this kind of a service organization could not be known. So there appears to be no question that plaintiff is entitled to enjoin defendants from further solicitation of its customers, or that some profits or damage should be paid to plaintiff by reason of these customers whom they enticed away.

For more than this appellants are not liable. . . .

ANALYSIS

1. Just what could the defendants have done to lure away Town & Country customers, without incurring liability to the plaintiffs?

2. Assume (reasonably) that the law would allow a competitor with no prior relationship with Town & Country to follow Town & Country trucks and thereby discover the addresses, and then the names and telephone numbers, of Town & Country customers, and then to solicit those customers. Is there any good reason why the defendants should not be permitted to hire a detective to do the same sleuthing and then use the list put together by the detective as a basis for telephone solicitation?