

AGENCY & PARTNERSHIP

3 February 1998

- ◆ Partnership is Essentially an Agency Relation (ergo, they go together)
- ◆ Agency issues, WON'T Show up alone on the Exam. They will be buried in a contract or tort fact pattern
- ◆ Agency: 1 Person, the Agent, voluntarily UNDERTAKING to Act for Another Party, the Principal, with the CONSENT of Both Parties

AGENCY

I. NATURE OF THE AGENCY RELATIONSHIP

A. NATURE OF THE RELATIONSHIP: AGENT & PRINCIPAL

1. *Consensual*

- A Completely Consensual Relationship
- May not be entered into Unilaterally.

2. *Contractual*

- Not Quite a Normal Contract, since there is NO Consideration required; that is an agent may act gratuitously
- As far As CONTRACTUAL CAPACITY: an Agent does not need Capacity, however, the PRINCIPAL requires Capacity. The Agent, though, at a minimum requires minimal mental Capacity
- An Agent May be DISQUALIFIED if he purports to represent 2 directly adverse principals in the same transaction UNLESS he FULLY DISCLOSES and gets CONSENT from Both Sides
- No Contractual FORMALITIES are required to establish an agency relationship
- No Writing Is Required (Except for the EQUAL DIGNITIES Rule which Does NOT apply in Massachusetts); rule: if the underlying transaction requires a writing, the agreement appointing the agent must be in writing

B. DUTIES OF AGENT TO PRINCIPAL

1. *Reasonable Care*

- The Agent must use **reasonable care** in acting for the Principal
- Reasonable Care is the Care that is Expected according to the community standard, unless Special Skill (then held to the higher standard)
- This Standard includes the duty to **notify** the principal if the agent receives *material information relating to the transaction* (since ANY notice given to the Agent is IMPUTED to the Principal)

2. *Loyalty*

- An Agent has a Duty of Loyalty to the Principal: therefore, the Agent may not act in a **conflict of interest fashion**
- Conflicts of Interest usually arise in **Opportunity** Fact Patterns
 - If there is an Opportunity that should go to the Principal, the Agent may not take it for himself
 - The Agent may not make a SECRET Profit on the transaction
 - Before the AGENT may act for himself, he must **fully disclose** all *material facts* of the deal to the Principal, and the Principal must turn down the deal. Only then may the Agent take the deal himself

3. *Obedience*

- The Agent must obey all **reasonable instructions** given to him by the Principal
- The Agent need not obey ALL instructions, just the Reasonable ones

C. **DUTIES OF PRINCIPAL TO AGENT**

1. *Indemnification*

- The Principal owes a Duty to the Agent to **indemnify** him for *reasonable expenses & liabilities* pursuant to the Agent's relationship to the principal.

2. *Compensation*

- Although the relation may be completely gratuitous, compensation may be paid (for gratuitous, require an express agreement)
- Absent an Agreement, the Principle owes the Agent a Duty to pay **reasonable compensation**

3. *Co-operation*

- The Principle may NOT **hinder or interfere** with the Agent's duties
- Also, the Principal may not refuse to do something that he is required to do
- **MA: Real Estate Agent**: not entitled to a Commission UNTIL the Deal Actually Closes. If a Deal Fails owing to the Principles Failure to co-operate, then the Real Estate Agent may still be entitled to some Compensation. For a close call on the exam, try to find a breach of duty so may continue the analysis and earn points elsewhere.

D. **REMEDIES FOR BREACH OF DUTY**

1. *Damages*

- For a breach of duty, the remedy is usually the Standard Contractual Remedy of Damages
- However, if the breach is *egregious* there is the Possibility of Punitive Damages
- If the Agent breaches the Duty of Loyalty, the Agent is NOT entitled to ANY COMPENSATION
 - Also, in an opportunity fact pattern, the Principle's Alternate Remedy to Damages is to create a **constructive trust** over the property at issue in the opportunity transaction, and then eventually get it for himself.

II. THIRD PARTY ISSUES

A. CONTRACT RELATED 3RD PARTY ISSUES

- The Agent enters a Contract on behalf of the Principal. The issue is whether the contract created between the Principle-Agent & the 3rd Party is valid enough to bind somebody
- Whether a Contract was created depends on whether the Agent had **authority**
- If the Agent had **authority**, the Principle will be bound. If not, the principle will not be bound.
- There are **3** types of Authority; Actual, Apparent, & Ratified (sequential analysis)

1. **Actual Authority**

- Self-explanatory: What transpired between the Principle & the Agent. Did the Principle Actually give the Agent authority to enter into a contract. Focus on what happened between the two of them.
- Actual Express Authority:
 - Either written, spoken, or some other manifestation of the Principle to grant the Agent authority to enter into contracts.
 - Actual Authority is **NARROWLY** construed. The Agent must act *within the scope of his authority in order to bind the Principal*
 - Actual Authority may not be revoked due to mistake or fraud
- Actual Implied Authority:
 - Test is the **REASONABLE Agent's Belief**
 - Basis of the Reasonable Belief is Industry Custom, Prior Dealings, Emergency Situation
- Delegation by Agent
 - Generally NOT permitted. Exception: Industry custom, Prior Dealing, Emergency, **PURELY MINISIRIAL ACT** (like typing)
- Termination of Actual Authority
 - 1st Question: Does the Agent Have Authority? If Actual (express-implied) If so, was it ever terminated?
 - Actual Authority **MAY** be Terminated by the **terms** of the grant of Agency Authority (typically Time or an Event)
 - Actual Authority **MAY** be Terminated by a **Unilateral Act** of Termination by Either the Principle or the Agent (since this is a Consensual Relationship)(note there is a difference between the *Power* to Terminate and the *Right* to terminate. Although one has the Power to terminate, he may breach his agreement)
 - Actual Authority **MAY** be Terminated by **the Agent's Breach of Loyalty**
 - Actual Authority **MAY** be Terminated by a **material change in circumstances**
 - Actual Authority **MAY** be Terminated by **DEATH or Incapacity** of Either the Principal or the Agent. (note; don't get suckered with a Sympathetic plaintiff. Like when an Agency terminated after the Principal dies **NO MATTER** how hard the Agent Worked. Exception: An Agency **COUPLED** with an **INTEREST** (like a Security interest)

will not terminate via death). Durable Power of Attorney: If give written power of attorney to an Agent & proved that **incapacity** will not terminate the relationship, it will be honored (this is a STATUTORY exception). DEATH however will still terminate, even a Durable Power of Attorney

2. *Apparent Authority*

- Relates to the Way an Agent presents himself to a 3rd Party
- Focus on the Perception of the 3rd Party
- It is a **2 Part Test**:
 - a.) Was the Agent **held out** by the Principle with Authority (Did the Principle do something or say something to give the 3rd party a reason to believe that the Agent had Actual Authority?)
 - b.) Did the 3rd Party **reasonably rely** on the apparent authority?
- An Agent Can NEVER create his OWN apparent authority; the Apparent authority derives from the actions of the Principal
- Typical Apparent Authority Fact Patterns
 - Secret Instructions
 - Agent has some Actual authority, but the Agent exceeds that actual authority. Say the Principal secretly tells the Agent NOT to pay more than \$1 Million for a piece of property. Agent then does the deal for \$1.05 Million. In that case, the Principal will be bound because the Agent had Apparent Authority to bind the Principle. However, the Principal may have a Cause of Action Against the Agent for Breach of Obedience.
 - Lingering Authority
 - The Agent had Actual Authority at one point, but it has since been terminated. However, the Agent may have *lingering apparent authority*. To CUT OFF the Apparent Authority (to avoid any lingering authority) the Principle must give **timely & proper NOTICE** of Termination to the 3rd party. Timely is Dependent upon the facts & circumstances. PROPER = **personal notice** to all those 3rd parties that the principal knows the agent has dealt with + **publication** to the rest of the world.
 - If the Agent has **Written Authority** or **Possession of Goods**, to terminate that Apparent Authority, the PRINCIPAL must take the WRITING AWAY or REMOVE THE GOODS. If the Agent still has the Writing or Goods, the Agent will Still have Lingering Apparent Authority.
 - General Agents
 - Unlike Special Agents, General Agents will have more probability of Finding Apparent Authority (such as corporate officers).

3. *Ratified Authority*

- After the Fact blessing by the Principal as to the Agent's Actions
- Pre-requisites
 - Principal must **KNOW all MATERIAL Facts** of the transaction
 - Principal must **Expressly or Impliedly Accept** the Benefit of the Deal
 - Ratification may NOT **Alter or Change** the Deal Entered into by the Agent (it's all or nothing)
 - Ratification is **INEFFECTIVE** unless the Principal is **Disclosed**
 - **Timing**: if the 3rd Party Dies, becomes incapacitated, or withdraws, the Transaction MAY NOT be ratified. Ergo, REQUIRE 3rd Party **capacity** at the time of Ratification
 - If no Authority, No Contract and the Principal Cannot be bound

4. *Liability*

- 3rd Party v Principal
 - Principal will be Liable to the 3rd Party if there is **VALID AUTHORITY** (any of the types). As soon as there is a breach, 3rd party may sue the principal
- 3rd Party v Agent
 - Agent's Liability Depends on whether the Principal was Disclosed:
 - *Disclosed Principal* (Existence + Identity Known to 3rd Party) is **ALWAYS** liable on the Contract, yet the Agent is generally not liable.
 - *Exceptions where Agent Liable for Disclosed Principal*: Agreement said so, Implied warranty to 3rd Party that Principal had contractual authority, etc.
 - *Undisclosed or Partially Disclosed Principal*: Liability **IMPOSED** on **BOTH** the Principal **AND** the Agent.
- 3rd Party Liability to Principal and Agent
 - An **AGENT** can never sue the 3rd party
 - The Principal may sue the 3rd Party as long as his agent had valid authority; in such a case, he may sue as if he himself had entered into the contract. **HOWEVER**, for **fraudulent concealment** if the Principal **KNEW** the 3rd Party would never enter into a contract with him, and he had the Agent enter into a contract with the 3rd Party while keeping the identity of the Principal Secret, then the Principal May NOT sue (although he is still bound to that contract). However for a **non-fraudulent concealment**, the Principal may still sue the 3rd party as long as there was a Valid Business Purpose for the Concealment.

B. TORT RELATED 3RD PARTY ISSUES

- Issues are when may the Principal be liable for the Acts of the Agent?
Essentially, it is VICARIOUS LIABILITY
- The Agent, however, is ALWAYS liable for his Own Tortious Acts
- The Principal, however, is generally liable only if meet the burdens of Respondeat Superior for Negligence

1. Negligence

- Negligence Liability for the Principal is Grounded in the Concept of **Respondeat Superior**; It has a **2 part Test**
 - a.) Was there a **proper agency relationship** between the principal & the agent to find liability in the principal (usually employer-employee)
 - b.) Was the Agent acting **within the scope of employment**?
- **A.) Proper Agency Relationship**
 - Principal = Employer, Agent = Employee
 - Fact Dependant Analysis. Certain Factors include: *Salary, Tools, RIGHT TO CONTROL* (the more control, the more an employment situation exists rather than an independent contractor)
 - Will the Principal be liable for the Torts of a Sub-Agent? If the Employee has a RIGHT to Delegate, the Principal will be liable whether or not that Sub-Agent was an employee of the employer
 - **Borrowed Servant Fact Pattern**: Usually Occurs in an Equipment Rental Situation. Rent a crane, and it comes with an operator. Usually the Employer will be liable for any negligence committed by that operator, however, sometimes the Borrower may be liable depending on whether the Borrower Exercised any control.
 - **Exception**: An Employer WILL be liable for an Independent Contract engaged in an *Ultra Hazardous Activity*
- **B.) Within the Scope of Employment**
 - Fact Sensitive; Ask Is the Employee doing the **type of work** he's expected to do; at the **time** he's expected to do it, at the **place** where the job should be, for the **benefit** of the employer?
 - Test of **Frolic & Detour**: If the deviation from the employment was SLIGHT, it was a **detour** and still within the Scope of Employment (i.e., salesman on way home from the sales call, goes to the cleaners to pick up his shirts, still acting within the scope, just on a slight DETOUR). However if it is a MAJOR deviation, it is **frolic** and NOT within the Scope of Employment (same salesman has an 8 Martini Lunch)

2. Intentional Torts

- Intentional Torts are NOT within the Scope of Employment, and there can be NO employer liability
- **Exception**: If work Requires FORCE, such as a Bar Bouncer, House Detective or Security Guard, (**Force Authorized, Friction Generated**), then Intentional torts will be within the scope of employment as long as done for the BENEFIT of the Employer.
- **Note**: A Principal-Employer can Still be DIRECTLY liable for Own Negligence in SUPERVISING or SELECTING Employees

PARTNERSHIPS

I. OVERVIEW

- Partnerships are generally agency relationships
- Most Partnership Issues are Resolved through Agency Principals
- Each Partner is both a Principal and an Agent
- **MA** has the UNIFORM PARTNERSHIP ACT: Absent an Agreement to the contrary, the UPA provisions will govern
- Thus, the 1st part of the Analysis is to LOOK to the AGREEMENT; if the agreement contains a certain clause, that clause governs. The UPA is only in default of an agreement (UNLIKE Corporations where the Corp. Act Governs)
- **5 Major Areas:**
 - Partnership Formation
 - Partnership Property
 - Relations Between Partners
 - Relations between Partners, the Partnership, & 3rd Parties
 - Dissolution & Termination of the Partnership

II. PARTNERSHIP FORMATION

- Assume that any PARTNERSHIP is A General Partnership (absent specific instructions to the Contrary)
- A *Joint Venture* is a General Partnership (just a specific deal where a partnership is broader)
- NO FORMALITIES are required in the Formation of a Partnership: **All that is Required is INTENT**: No writing required, if ORAL, no need of express words to form the partnership
- UPA defines a Partnership: as **2 or more persons** *doing BUSINESS as co-owners FOR PROFIT*
- Factors in Determining INTENT to form a partnership via doing business as co-owners for Profit: Name designating a partnership, bank accounts, leases, et. al. are helpful to show an intent to form a partnership to do business for profit
- UPA states that the *Receipt of Profits* (In Lieu of or In Addition to Wages, Rent, Interest) Are NOT NECESSARILY Evidence of Partnership, HOWEVER, receipt of profits is **prima facie** evidence of an INTENT to form a Partnership
- Limited Partnership: Only Formed by following the Strict Formalities outlined in the Statute (like a corporation). Must file a Certificate and have at least 1 fully liable general partner, but additional partners will have limited liability so long as they stay out of the day to day management of the business.

III. PARTNERSHIP PROPERTY

- Who Owns? The Partner or the Partnership?
 - Depends on the Factual Intent
 - Factors to Consider include: Whether the Property was Kept on Partnership premises, who holds the title, AND if PURCHASED with PARTNERSHIP Funds, it BELONGS to the PARTNERSHIP, and not any individual Partner
- Does the Partner have a Right to Specific Property
 - No Individual Partner has a Right to Specific Partnership Property
- The Partnership Interest
 - Each Partner has a Right to his Own Partnership Interest (sort of like a share of stock)
 - A Partner May sell or transfer his INCOME interest to anyone at anytime
 - If the Partner transfers his interest, he can only transfer his ECONOMIC (Income) interest. The Person who buys the interest will have only an income right, and no other rights (like voting or management)
 - Nobody may become a Partner without the Consent of all the other partners (due to Agency Principals)

IV. RELATIONS BETWEEN PARTNERS

- A dispute among Partners is Called **an accounting**
- Partners have High Duties of **loyalty** to the Partnership and other Partners
 - Watch for Opportunity Fact Patterns. BEFORE a Partner may Act on an opportunity, he must:
 - *Fully Disclose the Opportunity to the Partnership*
 - *Offer the Opportunity to the Partnership*
 - *Have the Partnership Reject the Opportunity*
 - *Only then may the Partner Act on the Opportunity for himself* (like Agency Principals)
- Sharing of Profits & Losses: In the Absence of an Agreement, the UPA provides that Profits are to Be SHARED EQUALLY and Losses are to be allocated in the Same Percentage as the Profits. (Regardless of the Contributions, Actual Work, et. al: Again, Watch for the Sympathetic Plaintiff)
 - Note; Agreement Can Always Provide otherwise
 - If the Agreement is ABOUT Losses & Not Profits, the Agreement will control the losses, but the profits should be shared equally (Losses Always Follow Profit Allocation but NOT Vice Versa)
- Partners Have NO Right to Compensation; only time a partner has a right to compensation is during the Wind Down of the Partnership
 - Of course, the agreement may provide for compensation
- Management: Absent an Agreement, the UPA says that all partners have an Equal Voice in the management of the partnership
 - 1 partner, 1 Vote. In ordinary matters, a Majority controls; for extra-ordinary matters, require unanimity UNLESS the agreements is to the contrary

V. RELATIONS BETWEEN PARTNERS, THE PARTNERSHIP, & 3RD PARTIES

- Similar to Agency Principals
- Contract
 - For a partnership to be bound for the Acts of a Partner: Require Authority:
 - *Actual*; in the partnership agreement
 - *Apparent*: in the ordinary course of business
 - *Ratification*
- Tort
 - There is NO Respondeat Superior for Partnerships
 - However, if a Tort is Committed in the Scope of the Partnership Business, the Partnership is liable
- Liability
 - If the Partnership has Liability, then each Partner has FULL PERSONAL individual Liability
- Knowledge & Notice
 - *Knowledge*: If a Partner has knowledge, it will be IMPUTED to the Partnership or other Partners ONLY if the other partners are Close enough to the transaction to reasonably know about it
 - *Notice*: when a 3rd Party places a Partner on notice, that NOTICE is IMPUTED to the entire partnership
- Liability to 3rd Parties : joint & several
 - *In-coming Partners*:
 - Will NOT be personally liable for the pre-existing debts or obligations of the partnership (except for any capital contributions)
 - *Out-going Partners*:
 - Will be Liable for the debts & obligations that the Partnership incurred while he was a partner. However, the out-going partner I NOT liable for Subsequent debts & obligations of the partnership IF there was **proper & timely notice** (same as for Agency); Personal notice to those with whom do business, & published notice to the rest of the world. Similar Lingering Authority Problems as in Agency
 - *Limited Partnerships*:
 - There is NO liability for the Debts & Obligations of the Limited Partnership so long as the Limited Partner DOES NOT Take an ACTIVE ROLE in the Management of the Business of the Limited Partnership. Also, as long as NO 3rd Party relied on the Limited Partner Acting as a General Partner due to the active role in the management of the business. However, if a Limited Partner lends his NAME for use in the partnership, he may incur personal liability
- Partnership by Estoppel
 - If 1 Misrepresents his status as a PARTNER & a 3rd Party relies on it, he MAY be liable as if he were a Partner. (he is not actually a partner, but treated as a partner for liability to 3rd parties)

VI. DISSOLUTION & TERMINATION OF THE PARTNERSHIP

- Dissolution ≠ Termination
- Dissolution: Change in the Legal Relationship of the Partners
- Termination: Post-dissolution, winding up of the business

- Dissolution: Ways to Have a Dissolution
 - by AGREEMENT (if express term dissolves after a time or an act)
 - by DEATH (automatic dissolution)
 - by BANKRUPTCY (automatic dissolution)
 - by EXIT of PARTNER (by express will, he chooses to leave)

- Termination: the Winding up of the affairs of the business after the dissolution
 UNLESS ALL partners agree to continue the business as a partnership
 - If the Partners do not Agree to continue the business after the dissolution, then move on to Termination
 - **Winding Up**: Finish all of the unsettled business, but CANNOT take on new business
 - Partners who wind up the business are ENTITLED to Compensation
 - Sell off the assets of the partnership
 - Distribute the Proceeds (sequentially)
 1. Creditors who are NOT partners
 2. Creditors who ARE partners
 3. Repay the Capital Contribution of the Partners
 4. Share the Profits as per agreement or UPA
 - If No profits, but **only Losses**, other concept of contribution: If any Partner PAYS more than his proportional share (absent an agreement) the other partners MUST **CONTRIBUTION** so that the 1st Partner DOES NOT PAY more than equal share.
 - For Example: 3 Partners (A, B, C) start a partnership.
 - A contributes \$10,000
 - B contributes \$ 5,000
 - C Contributes \$ 2,000
 - Total \$17,000

- The Partnership eventually DISSOLVES, and there is NO Continuation. Begin the Termination Process. After PAYING off the Creditors, there is \$5,000 Left (have \$12,000 in accumulated Losses). How to Distribute the Remaining \$5,000 (no agreement, UPA governs).
- \$12,000 Total Loss ÷ 3 Partners = \$4,000 proportional loss
- | <u>Cap. Act. Contribution</u> | <u>Share of Loss</u> | <u>Cap Act.</u> | <u>Contrib</u> | <u>Cap Act</u> |
|-------------------------------|----------------------|-----------------|----------------|----------------|
| A; \$10,000 | \$4,000 | \$6,000 | (6,000) | 0 |
| B: \$ 5,000 | \$4,000 | \$1,000 | (1,000) | 0 |
| C: \$ 2,000 | \$4,000 | (2,000) | 2,000 | 0 |

C MUST CONTRIBUTE 2,000 to balance his Capital Account
 B will receive 1,000 to balance his capital account
 A will receive 6,000 to balance his capital account

LLC; not much; MA recognize; hybrid P’ship (tax) & Corp (ltd. Liab)