

**A Study of the Provisions of Law Relating to Agency in Indian Contract Act**

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**Abstract:**

Although one person cannot, by contract with another, confer rights or impose liabilities on a third person, yet, he may represent another for the purpose of bringing him into legal relations with a third party. Employment for this purpose is called 'agency'. The law relating to agency is contained in Chapter X (Sec. 182 to 238 of the Indian Contract Act, 1872). Agency in law connotes an authority or capacity in one person to create legal relations between a person, occupying the position of Principal, and third parties. Thus, in an agency (contract of employment'), one person (principal) employs another person (agent) to represent him or to act on his behalf, in dealing with third person. It is almost impossible for any man in the modern complex world to transact all his business by himself. When you post a letter, the post office is acting as your agent. When you sent someone to deposit your telephone bill, he is acting as your agent. Whatever a person competent to contract may do by himself, he may do through an agent. There are, of course, certain exceptions to this rule. A person, for example, cannot marry through an agent. The agent may be expressly or impliedly authorised to do an act on behalf of principal. But at the same time an agent is a connecting link between the principal and third person.

**Keywords:** agency, operation of law, estoppels, necessity, ratification

## Introduction

According to Sec.182, an “agent” is a person employed to do any act for another or to represent another in dealing with third person. The person for whom such act is done, or who is so represented, is called the “principal.”

The function of an agent is essentially to bring about contractual relationship between the principal in dealings with third persons. Although the above definition is wide enough to embrace a servant pure and simple, even a casual employee like a painter, yet they all cannot be placed in the same category. What distinguishes an agent from a person appointed to do an act is the agent’s representative capacity coupled with a power to affect the legal relations of the principal with third person of an agent is his power of making the principal answerable to third person’s viz. to sue or be sued by the third party.

Representative character and derivative authority may briefly be said to be the distinguishing feature of an agent. A person performing ministerial acts is not an agent. A person merely giving advice to another in matters of his business does not thereby become his agent. The test is has he any power of representing the principal i.e. making the principal answerable to a third person? If he has this power, then there is the relation of agent and principal. The fiduciary element in agency, though the key to much of the law governing this relation, is not its essential element. It is not every agent who is in a fiduciary position vis-à-vis the principal. If A appoints B to be his agent merely to sign a memorandum and places no particular trust in B, there is no fiduciary relation.

## Test of Agency

The test for determining whether a person is an agent or not is by seeing that (i) whether he has the power to do any act for another or (ii) of representing that other in dealings with third person. The relationship is to be determined not by mere name. The principal may be called an employer, a constituent or a chief. The agent may be called a proxy, arhata or mukhtar. Whether an agency has been created or not is to be determined by the conduct of parties and purport of their dealings. The use of the word ‘agent’ without specifying the purpose of agency does not help to determine that the relationship is that of a principal and agent. A person giving advice to another in matter of business does not thereby become an agent. The employment must be made by a person for whom the agent is to act. Thus, a beamier is neither an agent nor the guardian of a minor, nor the committee of a lunatic even though they act for them.

## Essentials of Relationship of Agency

The essentials of the relationship of agency are:

### 1. Competency of principal and agent (Who can become an agent)

The principal should be competent to contract, but an agent may not be competent to contract. For the validity of a contract the parties should be competent to contract. Since through an agent a contract is to be created between the principal and the third person, it is necessary that both of these parties should be competent to contract. Sec. 183 provides that any person who is of the age of majority and of sound mind may employ an agent. A minor cannot appoint an agent, but the guardian of a minor can appoint an agent for him<sup>[1]</sup>. Where there occurred a change in the state of health of a client and he becomes mentally infirm, after giving a power of attorney to his counsel, it was held that such power of attorney becomes worthless<sup>[2]</sup>. So far as the agent’s capacity to bind the principal and the third person is concerned, for that any person may become an agent, even though he is not competent to contract (Sec. 184).

### 2. Agreement not contract is necessary

Agency depends on agreement but not necessarily on contract. It may arise out of an agreement which does not amount to a contract because one of the parties may lack contractual capacity.

3. **No consideration is necessary to create an agency (Sec. 185)**

From the fact that the principal agrees to be bound by the act of the agent, and he has a duty to indemnify the agent, sufficient consideration, is presumed, and therefore, no other consideration is necessary for such a contract. The fact that the principal has agreed to be represented by the agent is a sufficient 'detriment' to the principal to support the contract of agency. It may be noted that a person can become a partner in a firm, which is the position of an agent, without making any capital contribution<sup>[3]</sup>.

4. **Intention to act on behalf of the principal**

Whether a person intends to act on behalf of another is a question of fact. Where a person does intend to act on behalf of another, agency may arise although a contract between the parties provides that there is no such relationship. But the mere fact that a person says he is an agent does not make him one if he intends to act on his own behalf and not on behalf of his alleged principal. It is the true relationship between the parties. And not the terminology used by the parties, that is the relevant consideration. Even if a clause in a hire-purchase agreement provides that is the relevant consideration. Even if a clause in a hire-purchase agreement provides that the car dealer is not the agent of the finance company the dealer may be an agent in the eyes of the law. An agency can arise without any formal contract<sup>[4]</sup>. Agency is a legal concept which is employed by the court when it becomes necessary to explain and resolve the problems created by certain fact situation. In other words, when the existence of an agency relationship would help to decide an individual problem, and the fact permit a court to conclude that such a relationship existed at a material time, then whether or not any express or implied consent to the creation of an agency may have been given by one party to another, the court is entitled to conclude that such relationship was in existence at the time, and for the purpose in question<sup>[5]</sup>.

5. **An agent is not a servant**

The distinction between an 'agent and a 'servant' and 'independent contractor' has been underlined in **Lakshminarayan Ram Gopal v Govt. of Hyderabad**<sup>[6]</sup>. The court observed: "An agent, though bound to exercise his authority in accordance with the lawful instructions of his principal, is not subject to the direct control or supervision of the principal, whereas a servant works under the direction and supervision of his master. An agent acts at his discretion and judgment, but within the limits of his authority."

A principal has the right to direct what the agent has to do; but a master has not only that right, but also the right to say how it is to be done. As an agent often has a large discretion, he is a 'superior' kind of servant. Thus, the amount of independence will be a test for agency; the reasons for holding him a servant.

6. **Type of acts for which agent can be appointed**

Generally, whatever a person has power to do himself, he may do so by appointing an agent. Conversely, what a person cannot do himself he cannot do by means of an agent. For instance, the right of audience before a tribunal cannot be delegated to an agent.

The contract Act is about the acts in respect of which a principal may appoint an agent. However, the right to appoint an agent is subject to well-known exceptions as was held in **Zonal Manager of life insurance Corpn. Of India v City Munsif**<sup>[7]</sup> such as

- (i) Where the act to be performed is personal in character;

(ii) Where the transaction is required by statute to be done by or to be evidenced by the signature of the principal himself;

(iii) Where the competency to do the act arises by virtue of the holding of some public officer;

(iv) The competency arises by virtue of some power, authority, or duty of a personal nature and requiring skill or discretion for its exercise; or

(v) Where a statute imposes on a person a duty which he is not free to delegate e.g. appearance of an accused in a criminal court<sup>[8]</sup>.

#### **Creation of the Agency Relationship**

The agency relationship can be created by the following ways:

- A. by agreement
- B. by operation of law
- C. by estoppels
- D. by necessity
- E. by ratification

#### **Some instances of agency**

(1) Where a firm was appointed sole banian of a company to sell its manufactured good to be responsible to the company for the monies due by the buyers, to guarantee the performance of the guarantee by the buyers through them, it was held the firm was a delcredere agent of the company.

(2) When goods are dispatched through post office by the V.P.P. system, it is the post office that is an agent of the seller for recovery of the price; so if it fails recover the price but delivers the goods, it is liable in damages to the seller. A post office is an agent of the payee.

(3) A person can appoint one branch of a bank as agent for him. All other branches of the bank cannot thereby become his agent.

#### **Sub-Agent and his Position**

A sub agent is a person employed by and action under the control of, the original agent in the business of agency (Sec. 91). In simple words, a sub agent is the agent of the original agent. The relation of the sub-agent to original agent is as between themselves, that of agent and principal. A sub-agent is bound by all the duties of an ordinary agent. A foreign government cannot be a sub-agent. The sub-agent is responsible for his acts to the agent, but not to the principal and the sub-agent depends upon this question i.e. whether the appointment of the sub-agent is proper or improper. Where a sub-agent is properly appointed, the principal is bound by the acts of the sub-agent as if he were an agent originally appointed by the principal. The agent is responsible for the acts of the sub-agent. The sub-agent is responsible for his acts to the agent, but not of the principal except in case of fraud or wilful neglect (Sec.192). Thus, a sub-agent is not directly responsible to the principal. Sub-agent is responsible to the agent and the agent is responsible to the principal.

#### **Liability of the Principal**

When the principal expressly or impliedly authorizes some act to be done he is liable for such an act of the agent if the same has been in the course of performance of his duties as an agent, on the ground that it is the principal who has selected the agent. This is also known as 'vicarious liability' i.e. liability incurred for, or instead of, another.

An agent acts on behalf of the principal for creating contractual relationship between the principal and the third persons, and therefore, for the contracts entered into through an agent the principal becomes bound towards a third person in the same manner as if he entered into the contract himself (Sec. 226). A part from being bound by the acts which are done under principal's authority or for which he is bound in emergency, by estoppels or ratification, the question of principal's liability arises in the following cases:

1. When agent exceeds authority,
2. When agent receives notice on principal's behalf, or
3. When agent commits fraud, etc. against a third party.

If a part of the agent's act is within the authority and a part outside it, and both can be separated, the principal is bound by that part which is within the authority and not for that part which is outside the authority (Sec. 227).

The extent of an agent's authority was at issue in **State of Orissa v United India Insurance Co. Ltd**<sup>[9]</sup>. It was held that the branch manager of the Oriental Insurance Co. had exceeded his authority as an agent in undertaking liability (for his company) for risk of loss on account of non supply. He had no express authority to do so and the provisions of Sec. 237 (ostensible authority) also did not apply. It may be noted that ordinarily, knowledge of the agent is knowledge of the principal. Facts which the agent learns in the course of transacting the affairs in which he is employed are treated as known to the principal personally. This rule rests on the assumption that facts which the agent ought to have communicated to his employer have in fact been communicated.

An important exception to the rule that the knowledge of an agent is equivalent to that of the principal exists in cases where the agent has taken part in the commission of a fraud on the principal. In such cases, notice is not imputed to the principal of the fraud or the circumstances connected therewith, because of the extreme improbability of a person communicating his own fraud to the person defrauded. But the exception does not apply where the fraud is committed not against the principal, out as third person.

Principal's liability is based on the "qui facit per alium facit per se" which means "he who does an act through another is deemed in law to do it himself". The act of the agent is the act of the principal. A person, who puts another in his place to do a class of acts in his absence, necessarily leaves him to determine according to circumstances that arise, when an act of that class is to be done and trusts him for the manner in which it is done. Consequently, he is answerable for the wrongs of the persons so entrusted, either in the manner of doing such an act, or in doing such an act under circumstances in which it ought not to have been done, provided that what is done is not done from any caprice of the servant, in the course of his employment.

#### **Personal Liability of Agent**

As a general rule when an agent acts on behalf of his principal in his dealings with a third person, a contractual relationship between the principal and the third person is created and the agent is not personally liable. It is the principal who is liable to the third person. This is known as the principal of the agent's immunity from personal liability. "Neither the agent entitled to enforce the contracts entered into on behalf of the principal, nor is he personally bound by them. This is subject to contract to the contrary" (Sec. 230). As an agent acts for and on behalf of the principal prima facie a suit for specific performance is not maintainable against the agent<sup>[10]</sup>.

#### **Liability of pretended agent (Holding out)**

Where the agent pretends to have authority which he does not possess, he is personally liable. "If the agent purports to act on behalf of principal, but with any authority, and the principal does not ratify the act, but disowns it, the pretended agent himself will be liable" (Sec. 235).

Similarly, when an agent exceeds his authority, but the third person is misled in believing that the agent has the requested authority in doing the act, then, agent can be made liable personally for the 'breach of warranty of authority'. The liability of pretended agent, a special application of the principle of estoppel, is known as liability by 'holding out'. The expression 'holding out' means falsely leading another to believe something which is not true, and inducing him to act on the strength of the representation. This liability is based on the general principles of public policy to prevent frauds to which creditors would otherwise be exposed. Sec. 28 of the Partnership Act contains provisions relating to partnership by 'holding out', analogous to agency by holding out.

### **Modes of Termination of Agency**

The Indian Contract Act, 1872 tells about the various modes of termination of agency relationship between the two. These modes are as follows:

#### **1. By the death of the principal or the agent**

The death of the agent terminates his authority. If the principal dies, the agent is liable for loss caused to the estate if he acts otherwise. He may be liable for breach of warranty of authority in such a case. He cannot also sue for his remuneration. As to whether the executors of the deceased can ratify a contract made on behalf of the deceased. The rule applies also to a partnership and the death of one of the partners terminates the agency.

#### **2. By the bankruptcy of the principal or the agent**

The authority of any agent is automatically revoked by the bankruptcy of his principal in so far as by the bankruptcy of a different principal, the trustee in bankruptcy is created. This is not so where the authority is irrevocable or in the case of purely ministerial matters. If an agent continues to act after notice of act of bankruptcy he may be liable to the trustee, or to the third party for breach of warranty of authority.

#### **3. Termination by act of parties**

The parties to an agency contract may at any time mutually agree to bring it to an end.

There is normally a right in both the principal and the agent unilaterally to revoke the agency contract at any time before the agency has been completely performed by giving

#### **4. Termination by operation of law**

Unless there are special terms in the appointment contract or the contract is of an irrevocable type, an agency is normally terminated automatically when:

- i. End of fixed period in the contract or if no fixed period, contract terminates after the agent has completed all he has been authorized to do.
- ii. Death, mental incapacity or bankruptcy of either party. Notice of such event to the other party is immaterial.

### **Indemnity after Termination of Agency**

The general law of damages in India is contained in Section 73, 74 and 75 of the Act.

The Act provides that in the event of breach of a contract the non-defaulting party is entitled to receive compensation for any loss or damage caused to such non-defaulting party thereby. Such compensation is payable when the loss has arisen in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from such breach of it. The party in breach must make compensation in respect of direct consequences flowing from the breach and not in respect of loss or damage indirectly or remotely caused.

Subject to the terms of the Agency Contract, the Act provides for the following situations where an Agent has to be indemnified/ compensated by the Principal:

(i) Section 222 of the Act provides: -

“the employer of an Agent is bound to indemnify him against the consequences of all lawful acts done by such Agent in exercise of the authority conferred upon him”; and

(ii) Section 223 of the Act provides: -

“Where one person employs another to do an act, and the Agent does the act in good faith, the employer is liable to indemnify the Agent against the consequences of the act, though it causes an injury to the rights of third persons”.

**References**

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