

Agency, Partnership, and the LLC

**Agency, Partnership,
and the LLC**
**The Law of Unincorporated
Business Enterprises**

Cases, Materials, Problems

ELEVENTH EDITION

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*First through Fifth Editions (from Professor Hynes)
To my children*

*Professor Loewenstein dedicates this Eleventh Edition
to his family.*

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Preface

This Eleventh Edition seeks to incorporate developments in the law of agency and unincorporated business entities since the publication of the Tenth Edition of this casebook in 2019. The courts have considered many issues arising under the revised general and limited partnership acts as well as the limited liability company acts, and I have sought to capture the most important of those cases. Significant developments have occurred in relation to limited liability companies, where the courts have decided numerous cases in the past several years.

As in previous editions, most textual omissions, whether of a few words, a paragraph, or several pages, are indicated by an ellipsis. Occasionally the ellipsis is not used where the nature of the text is such that its use would be excessive or distracting, and sometimes text is slightly rearranged for ease of reading. In addition, omissions consisting of footnotes or of citations to cases or articles are not indicated. Under no circumstances has editing altered the substance of the text being presented. Footnotes that have been retained from cases retain their original numbers in brackets at the start of the text of the footnote. All citations in court opinions to legislation based on one of the uniform acts are treated as if made directly to the uniform act. This avoids the problem of forcing the reader to cope with the different numbering systems of the various states.

I am deeply indebted to my colleague, Professor J. Dennis Hynes, whose meticulous scholarship is reflected in the first five editions of this book and, of course, greatly influences the most recent six editions for which I have been responsible.

Mark J. Loewenstein
Boulder, Colorado
January, 2024

Glossary

Agency The agency relationship is a consensual relationship created when one person (the agent) acts on behalf of and subject to the control of another (the principal).

Agent An agent is a person (which can include an entity, like a corporation, partnership, or LLC) who acts on behalf of and subject to the control of another.

Agent's agent This sometimes confusing phrase describes the situation where a person acts on behalf of and subject to the control of an agent for another (the agent's principal) but is not responsible to and does not have the power to create liability for the agent's principal. The phrase is confusing because a subagent (see below) also is an agent of an agent. (The difference is that the subagent is also the agent of, and thus possesses the power to create liability for, the remote principal.) The confusion can be dispelled only by seeing the language in context. Although sometimes ambiguous, the phrase can serve the useful purpose, once a situation is analyzed, of sharply delineating the relationship of the parties in just a few words.

Apparent authority Apparent authority is the power of an agent to bind the principal to unauthorized contracts. The power is created by manifestations, which can be subtle and indirect, of the principal to the third party that are reasonably relied upon by the third party.

Borrowed servant A servant (employee) is borrowed when exposure to vicarious liability for the torts of the employee is shifted from the lending employer to the borrowing employer. The standards for determining when an employee is borrowed are in conflict and confusion in the law of many states today. The majority rule appears to require both a transfer of the allegiance of the employee and control by the borrowing employer before vicarious liability is shifted from the lending employer to the borrowing employer.

Business trust This is a form of doing business through use of a trust. The business trust recently has received significant statutory treatment in some states. At the present time it is infrequently used except in specialized security transactions. It is covered in the Introduction immediately following this glossary.

Co-agent A co-agent is one of two or more agents of a principal. Co-agents can be in a hierarchical relationship, like that of a president of a corporation and her secretary. Under such circumstances, co-agency appears confusingly like agency because the secretary functions throughout the working day under the direction and control

of the president and may even have been hired by the president. Yet the secretary is a co-agent, not the president's agent, because both the president and the secretary work on behalf of their common employer.

Control To exercise authority over; dominate; direct; regulate. This word has different meanings in the law of agency depending upon context. If, for example, the issue being pursued is liability for the physical torts of another, a special kind of control, over physical conduct and over the details of the activity, is required.

Disclosed principal A principal is disclosed when a third party has notice of the principal's existence and identity. Under such circumstances, the agent acting in the transaction is not a party to the resulting contract in the absence of special facts, like guaranteeing the contract.

Employee The term *employee* is a defined term in the Restatement (Third) of Agency §7.07 and is used to describe an agent for whose torts the principal is vicariously liable. Thus, an employee is "an agent whose principal controls or has the right to control the manner and means of the agent's performance or work." It replaces the term "servant," used in earlier Restatements of Agency and in many common law cases. The new definition makes clear that the term is not limited to traditional, compensated employees, as the definition goes on to provide that "the fact that work is performed gratuitously does not relieve a principal of liability." The term might also exclude an agent who is an employee for purposes of federal and state laws, but whose principal lacks the right to control the manner and means of the agent's performance of work.

Employer This term is used in the Restatement (Third) of Agency to describe a principal who is vicariously liable for the torts of its "employee" agent. See the definition of "employee." The term "employer" replaces the term "master," used in earlier Restatements of Agency and in many common law cases. As used in the Restatement (Third) of Agency, the term "employer" includes principals who, for other purposes (such as coverage under various federal and state laws regulating the employment relationship), are not "employers."

General agent A general agent is an agent authorized by the principal to conduct a series of transactions involving a continuity of service, like a manager of a business.

Independent contractor This is an ambiguous phrase in the law of agency. It can mean a nonagent, such as a building contractor who contracts to build something for an owner but who is not subject to control over the physical conduct of the work and who does not act on the owner's behalf, but rather merely benefits the owner by the work being done as performance under an ordinary contract. The phrase "independent contractor" also refers to a nonservant agent, such as a real estate broker or a lawyer, who acts as agent for another but who is not subject to control over the physical conduct of the work. A principal is not liable for the physical torts of a nonservant agent (independent contractor).

The Restatement (Third) of Agency abandons this term. To determine whether a principal is vicariously liable for the tortious conduct of its agent, the Restatement (Third) has a special definition of the term “employee.” If the agent falls within this definition (which focuses on the degree of control that the principal has over the agent), the agent is an employee and the principal has respondeat superior liability for the employee’s tortious conduct. The Restatement (Third) also uses the term “nonagent service provider” in some comments to capture one of the meanings of “independent contractor” set forth here.

Inherent agency power This is a controversial doctrine in the literature of agency. It states that a general agent has the power to bind a principal to unauthorized acts beyond the customary doctrines of apparent authority and estoppel if the acts done “usually accompany or are incidental to” authorized transactions. The Restatement (Third) of Agency abandons this term.

LLC The acronym “LLC” stands for “limited liability company.” This relatively new form of doing business in an unincorporated form is described in the Introduction immediately following this glossary and is covered in detail in Chapter 15. All states allow the creation of LLCs.

LLLLP The acronym “LLLLP” stands for “limited liability limited partnership.” It refers to a limited partnership in which not only the limited partners but also the general partners have limited liability. This form of doing business is described in the Introduction immediately following this glossary and is covered in Chapter 14.

LLP The acronym “LLP” stands for “limited liability partnership.” It is a recent innovation in the law of partnership, following the widespread adoption of statutes authorizing the LLC. It refers to a general partnership in which the partners have limited liability. This form of doing business is described in the Introduction immediately following this glossary and is covered in Chapter 11. All states have legislation providing for the LLP.

Master The word “master” is a term of art in the law of agency. It identifies a principal who employs an agent to perform services and who controls or has the right to control the physical conduct of the agent in the performance of the service. A master is vicariously liable for the physical torts of its servant under the doctrine of respondeat superior. The Restatement (Third) of Agency has abandoned this term in favor of the term “employer.” See the definition of “employer” above.

On behalf of This is an essential element of the agency relationship. It means acting *primarily* for the benefit of another, not merely benefiting another by one’s actions. A person who acts on behalf of another ordinarily is a fiduciary of the other, due to the trust being placed in the actor under such circumstance.

Partially disclosed principal A principal is partially disclosed when the third party has notice that the agent is acting on behalf of someone but does not know the identity of the principal. Under this circumstance it is inferred, subject to agreement, that the agent is a party to the contract. The Restatement (Third) of Agency abandons this term in favor of the term “unidentified principal.”

Partnership A partnership is an association of two or more persons to carry on as co-owners a business for profit. It can be formed without any papers being filed and without the owners even realizing that they are creating a partnership. The partnership is described more fully in the Introduction immediately following this glossary and is covered in detail in Chapters 11–13.

Principal A principal is the one for whom action is taken. The action is taken on behalf of and subject to the principal’s control.

Respondeat superior This Latin phrase means “let the master answer.” It is a shorthand and classic expression for the doctrine that a master (or employer) is vicariously liable for the torts of its servant (or employee) committed within the scope of employment.

Servant The word “servant” is a term of art in the law of agency. A servant is an agent who is employed to perform service and whose physical conduct in the performance of the service is controlled or is subject to the right of control by the master. Janitors and construction workers are examples of servants, although they are unlikely to appreciate being called servants. In part because the word “servant” is passé in today’s language, the word “employee” is usually used in its place. “Employee” is less exact, however, because there are servants who are not employees and employees who are not servants. Despite this possible confusion, the Restatement (Third) of Agency abandons the term “servant” in favor of the term “employee,” albeit one specially defined. See the definition of “employee” above.

Sole proprietorship A sole proprietorship occurs when a person carries on a business as its sole owner. No forms need be filed with the state in order to create a sole proprietorship. The proprietor is personally liable for the debts of the business and pays income taxes on the net income of the business. The sole proprietorship is covered in the Introduction immediately following this glossary.

Special agent A special agent is an agent who is authorized to conduct a single transaction or a series of transactions not involving continuity of service, such as a real estate broker.

Subagent Subagency exists when an agent (A) is authorized expressly or (more commonly) implicitly by the principal (P) to appoint another person (B) to perform all or part of the actions A has agreed to take on behalf of P. If A remains responsible to P for the actions taken, B is a subagent and A is both an agent (to P) and a principal (to B). B is an agent of P as well as A, which underscores the importance of P’s express or implied consent to this relationship.

Undisclosed principal A principal is undisclosed when the third party is unaware that the agent is acting for a principal and thus assumes that the agent is contracting on its own behalf. Under these circumstances the agent is a party to the contract (as is the undisclosed principal).

Unidentified principal This term is employed in the Restatement (Third) of Agency to describe what many courts and the earlier Restatements referred to as a “partially disclosed principal.” See the definition of that term above.