**Advanced Contracts, Tendering and Public Procurement**
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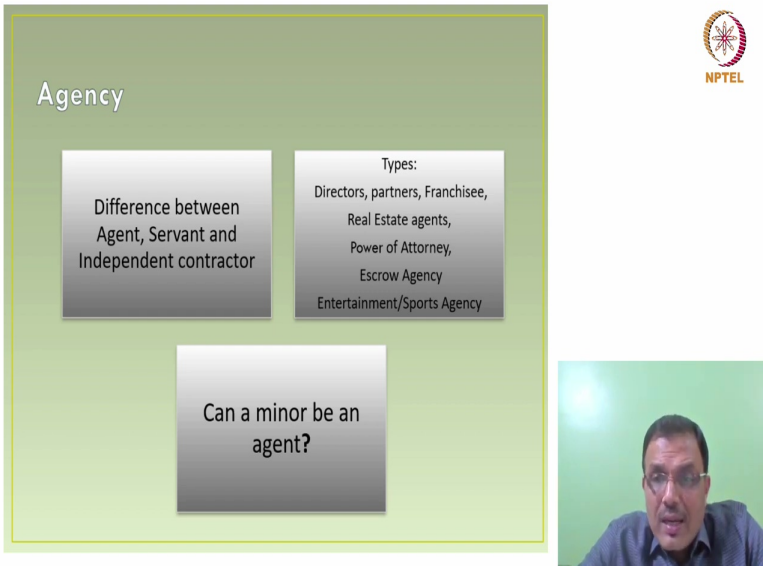
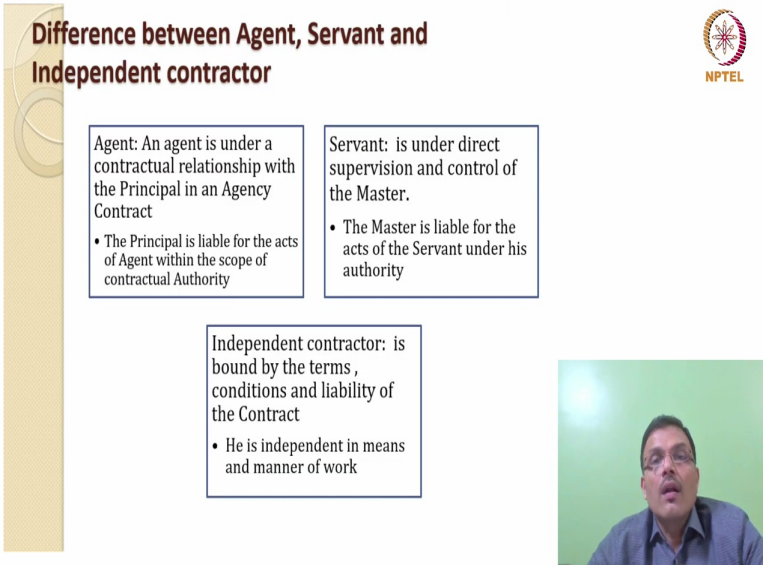
**Lecture 37: Special Contract: Agency – Part 02**








This session is to understand the difference between agent, servant and independent contractor. It is important to look at these characteristics in contracts to try and look at application of law, especially from the perspective of the rights, duties and liabilities of an agent as prescribed by the Indian Contract Act 1872. Now that the Indian Contract Act, to certain extent curtails the freedom of contract, there is no absolute freedom.

In certain circumstances the law prescribes what the agents should do. But the law also says when there are rights of an agent and when the statute or the law prescribes the rights of an agent, then he can actually go about exercising those rights. Through a court of law, he can

enforce those rights through a court of law. For example, the agents have the right to be reimbursed all the expenses that they have incurred in an agency contract, this is provided by law. Therefore, the principal cannot deny those rights of an agent wherein he has acted within the scope of authority.

We make a distinction between agent and servant for the simple reason that servant is responsible to his master, agent is responsible to his principal. While a servant receives the salary and agent receives commission, there are distinctions between an agent and servant. However, coming to the difference between agent, servant and independent contractor an independent contractor is basically a person who does not represent the Principal, he does not make contracts for him rather he actually executes work for him. In a government contract if there works contract or works order for construction, for laying down or pipes, roads, any electrical work, plumbing work, they are called independent contractor. The word independent here assumes greater significance.

When a contract is awarded, they work on the specifications mentioned, but the contractor goes about doing his work Now, the contractor here is not the servant, because he does not work for full time he is not an employee. So when he is not an employee, nor the servant, he cannot get the entitlements of labor law, except PF and ESI that is permanent from an employee state insurance. The labor laws speak about what is known as principal employer. Now, the PF and ESI rule is basically as social security measure, because the independent contractor and his employees will be working on the mentioned site. They must be given some kind of Provident Fund, which is a social security measure as it is compulsory same to get the cover of the employee state insurance in case of an accident or an incident on site, including the medical cover.

That is the reason ESI law has been brought into place. But otherwise, he is independent in the context that there is no industrial dispute law or any other law to be applicable to the employees of an independent contractor. They are totally working under the rules of a contract. They do not serve full time neither do they represent the Principal towards third parties, which means they are not even agents.

Agency comes when the person makes a contract with a third party, an independent contractor just executing work, as you say, I have said, but they do not represent to any third party. So, independent contractors are responsible and liable for any deficiency of work or service that they give me provide for. But it is not that they can have the vicarious

responsibility or liability principle simply because vicarious responsibility and liability principle applies to agents and servants, but does not apply to independent contractor.

So, an independent contractor is like any other contracting party who has independent responsibilities, independent liabilities and his rights arise from the contract. It is not something that is defined as labor law or under the contract. At the same time, I think one can see the types of agency that we have seen we have discussed this in the past but one of the critical aspects that one we have to understand is how escrow agents are very relevant in today's context. The Real Estate Act of 2016 has now looked at making escrow kind of a compulsory modality in the real estate sector. The money that the allottee is given a project, nearly 70 percent of that money has to be deposited in an escrow account by the builders, and they can only withdraw it in stages for the completion of the work. The idea of the escrow account in the real estate sector is that this will not be diverted for other projects, which usually happens with builders and many of these projects are not completed on time, or they are abandoned by the builders when they sometimes go insolvent.

To be aware and avoid all those situations and in order to have financial stability of projects, any money that is collected with already 70 percent of the cost gets deposited into an escrow account. This is how the escrow becomes then an agent. He becomes someone who is the trustee of the money and in an agency capacity because he represents the allottee and the builders as well. The money can be withdrawn in stages, after an adjudication with RERA authority wherein he can either give permission or not give permission for withdrawing the money at the escrow agent.

Escrow has become a very critical aspect of agency today, especially in international contracts and international transactions as well. Escrow account can be applied to a neutral country with independent bank. Mostly banks play as escrow agent, this is an additional service. They also provide for in PPP projects (public private partnership projects) the toll money that is collected goes to an escrow account. It held in trust before it can be finally be withdrawn and distributed among the PPP partners as well.

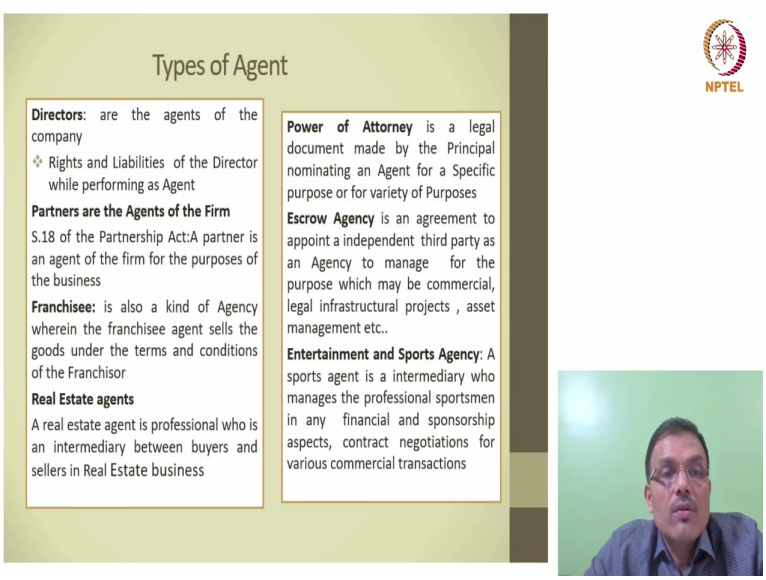
This is how a kind of brokerage aspect has been introduced in escrow account or an agency where the representation is there for both the contracting parties. But interestingly the Supreme Court has already laid down in one of the cases that an escrow agent cannot be an arbitrator. He is a trustee of the money, he holds the money as an agency capacity, but he

cannot decide dispute but because that could be conflict of interest. When an escrow agent; has a fiduciary capacity then the escrow agent cannot sit as an arbitrator in that sense.

When an Escrow is like an arbitrator, but court has already said they should not be. The arbitration is a separate clause, it is a separate process of dispute resolution and this is only the financial trust of the money. They cannot sit in adjudication of the right or wrong about the distribution of money, they just have to abide by the directions issued by the contracting parties.

Whether who can be escrow agents there can be minor be an agent. Minor can be an agent for beneficiaries, he cannot be for liability. The principal has to take the entire benefit, though agent but the minor cannot be made personally held responsible. A minor is allowed under various legislations under the Partnership Act of 1932. Under Section 30, minors can be members of a trade union at the age of 14 years. Minors can be employed as child artists; this is also permitted by labor law. So, minors are permitted to enter into contractual relationship with the aspect is that till they are 18 years of age, they can enter into this contract only for their benefit without any responsibility of liability that can be fixed by law.

The liability then is of the adult partners, they have to take the complete responsibility as they cannot make this minor personally responsible and liable for any of those actions. That is how a minor can definitely become an agent though the principal takes the entire responsibility of liability.



There are different types of agents. The directors in the company perform a very important duty of representing the company as agents. Interestingly, companies rule or law as the case may be, there is a very interesting rule called the Turquand rule. This was decided in the British bank versus to Turquand case where the indoor management doctrine was applied

Generally, when a director acts he must act within the scope of his authority of that company. But how does a third party know whether a director works within the scope of authority. He is innocent, he is acting in good faith and also the third party being innocent and acting in good faith probably under a contract with the director, supplies goods to the company. Later on it is found that the director did not have the authority to meet the contract or make that purchase order or did not have the authority to represent the company. Under these circumstances what happens to the right of the third party? Interestingly one of the matters in such cases was, there was supposed to be some kind of a constructive notice to third parties. So, third parties must be notified about who are these directors, the independent directors, the executive directors, the directors in a non-executive capacity. They should have some constructive notice and that is something that all companies have a duty to perform.

To understand what powers the directors have, whether the managing director has certain powers or the directors have certain powers, the third parties the Articles of Association AOA has to be read. There are two incorporating documents in a company called the memorandum of association and articles of association. The Articles of Association prescribes the powers and functions of individuals who can actually represent the company.

The Board of Directors or collective organizations of Directors have independent responsibilities as the case may be for the company to represent the company. Ideally there is something that is laid down under the company's law. However, while third parties must have notice about the powers, it is understood that there are two concepts called the “intra virus” which is within the scope of authority while Ultra viruses is beyond the scope of authority.

In an unauthorized or an ultra-virus act is based on what is known as the object clause that is registered under the memorandum of association. An MOE is an incorporating document, which has the name clause, the liability clause, the object clause. Now, what is the object of a company supposed to be is hardware, but the company later on enters into the business of software, such a business can be considered as ultra-virus as the object of the company. Secondly once the company is within the hardware business, then which are the directors who can represent the company in the hardware business is something that the articles of

association will actually represent 5 crores 10 crores that it should be done through a special resolution of the board and of the shareholders.

When everything will be prescribed, how decisions have to be taken, who are to be involved in that kind of decision, the articles of association will lay down the same. Now, if that is not followed by either individual Directors or by the Board of Directors or by the representatives of the company, as the case may be, then it becomes Ultra virus. The director or that agent, beyond the scope of that director has entered into a contract, which will then be called "beyond the powers of the director" in that sense. All of these are something that third parties must view before they enter into contract. But it is often done in trust and on third parties cannot always check these documents before they actually enter into a contract or supply goods, or give the services to these kinds of companies, now in the UK and in common law, they developed this very interesting doctrine called the doctrine of indoor management.

When the burden of proof on the company itself to manage its own affairs, why should a third party be blamed, if there is an ultra-virus action. Indoor management means that the companies must manage its affairs in such a manner that no agent of the company actually acts in an ultra-virus capacity. Manage the affairs in such a way that third party rights are not going to be adversely affected, especially when they are in contract with the organization. If there is any alternative action, it is for the complete result, if there is any antivirus action is for the company to take responsibility.

If there is an ultra-virus, then not to forget that an agency can be created by ratification. So, where there was no authority, an agency by ratification given antecedent and retrospective authority as well. So, it is for the company to manage its internal affairs. The company has to take responsibility because the director has acted in the capacity of a director. He has acted as an agent. He has disclosed that he has acted as an agent, though ultra-virus. So, this is for the principal which is the company to take responsibility to ratify that action. The third parties right should not be adversely affected that the third party acted in good faith and without any knowledge of that authority and he has performed in the best interest of the contract.