THE EFFECT OF INSANITY ON AGENCY TRANSACTIONS

By P. F. P. HIGGINS*

The law relating to the effect of a principal's insanity on the relationship between principal and agent does not appear to be settled and, as a result, his liability and that of his agent to third parties is in considerable doubt.

The present confusion stems largely from two Court of Appeal decisions, *Drew* v. *Nunn*[1] and *Yonge* v. *Toynbee*,[2] and the attempts to reconcile them have, if anything, added to the confusion.

The purpose of this article is not to attempt a reconciliation but to review those two cases in the light of other cases touching on the same subject, changes in the general law since the decisions, and modern trends of thought with regard to the authority and power of agents. It is hoped to show that each case can be confined to its special facts, thus leaving the way open for the evolution of a reasonable rule to cover all cases where the principal becomes insane after the creation of the agency relationship.

Many writers[3] on the subject of agency have demonstrated that much of the difficulty encountered in trying to extract the rationes of the cases is attributable to the practice of confusing the agent's authority to act on behalf of his principal with his power to create legal relationships between the principal and third parties. Professor Powell has examined and summarised most of the writing on this topic,[4] and concludes:

> If the agent has the authority of his principal, then it follows as a matter of course that he also has the power to affect the legal relations of the principal with the third party. But, even if he has not the authority of his principal there are circumstances in which he may yet have this power.
>
> It is important, therefore—
>
> 1. Not to confuse *authority* and *power* . . .
> 2. To realise that the agent's *power* may be and often is wider than his *authority*.[5]

---

* LL.B. (London). Senior Lecturer in Law, University of Tasmania.

1 [1879] 4 Q.B.D. 661; 48 L.J.Q.B. 591; 40 L.T. 671.

2 [1910] 1 K.B. 215; 79 L.J.K.B. 208; 102 L.T. 57; 26 T.L.R. 211.

3 J. L. Montrose in *Can.B.Rev.* 16 (1938), 757; Warren A Seavey in *Yale L.J.* 29 (1919), 861; John D. Falconbridge in *Can.B.Rev.* 17 (1939), 248; Cecil A. Wright in *Can.B.Rev.* 15 (1937), 197.

4 *The Law of Agency* (1952) at 5-6 and 48-50.

5 Powell, *op. cit.*, 5-6.

A simple example may help to illustrate this distinction. P, a connoisseur of antique furniture, knows that a Sheraton table is to be offered at an auction in Hobart but realises that he will be away in Melbourne on the day of the sale. He accordingly authorises his friend, A, to attend the auction on his behalf and to bid up to seventy-five pounds. He writes to the auctioneers informing them of this arrangement. The day before the auction A receives a letter from P withdrawing the instructions and informing A that he has just managed to buy a similar table in Melbourne for fifty pounds. A attends the auction and buys the table in P's name for forty pounds, thinking that P will be happy to have it at such a low price.

It is quite clear that A had no authority to bid on P's behalf, but seeing that P did not inform the auctioneer of his revocation of the authority P will be liable to pay the forty pounds. The reason being that although A's authority had ceased, his power to create legal relationships between P and the vendor of the table continued until the auctioneer, as agent for the vendor, was informed of the revocation of the authority. Some writers prefer to describe the position as one in which the agent had an apparent or an ostensible authority but, with respect, it is submitted that confusion is avoided if Professor Seavey's view is adopted. He would confine the use of the word 'authority' to those cases where the agent has actual or real authority as distinct from those cases where in spite of the absence of such authority the agent has power to create legal relations between his principal and a third party.[6]

In the two cases, *Drew* v. *Nunn* and *Yonge* v. *Toynbee*, this confusion between power and authority appears in nearly all the judgments and largely as a result of it the effect of the principal's insanity both on the agency relationship itself and on the transaction purportedly entered into by the agent with the third party remains shrouded in doubt. In each case the Court of Appeal to some extent, either expressly or by implication, deals with the four questions involved:

1. Does the principal's insanity terminate the relationship between him and his agent, *i.e.*, terminate the agent's authority?
2. Does the principal's insanity deprive the agent of his ability to create legal relations between his principal and third parties, *i.e.*, divest the agent of power?
3. Has the agent any liability to third parties?
4. Has the principal any liability to third parties?

In *Drew* v. *Nunn* the defendant, when sane, held his wife out as having authority to order goods on credit from the plaintiff on the basis that he, the defendant, would pay for them. Prior to his insanity the defendant was ill, and at that time assigned the whole of his income to his wife at the same time empowering her to draw on his bank account. After the defendant had become insane, and while he was in a mental home, his

6 *Yale L.J.* 29 (1919), 859.

wife ordered goods from the plaintiff and did not pay for them. When the defendant recovered his sanity the plaintiff sued him for the price of boots and shoes delivered to the wife. At first instance Mellor J. held the defendant to be liable. The appeal proceeded on the basis that the boots and shoes were not necessaries so that no question of a wife's agency of necessity arose. The defendant relied solely on his insanity at the time of the transaction. The Court of Appeal affirmed the decision of the court below.

Brett L.J. found that the wife's authority had been revoked by the defendant's insanity and stated that but for the circumstance that she was a married woman she would have been personally liable to compensate the plaintiff.[7] This means that, in his view, a wife in similar circumstances today, since she can contract as a feme sole, will be personally liable. This accords with the rule in *Collen* v. *Wright*[8] which was approved unanimously by the House of Lords in *Starkey* v. *Bank of England*.[9] The rule as stated by Willes J. in *Collen* v. *Wright* is that 'a person professing to contract as agent for another, impliedly, if not expressly, undertakes to or promises the person who enters into such contract, upon the faith of the professed person being duly authorised, that the authority which he professes to have does in point of fact exist. The fact of entering into the transaction with the professed agent, as such, is good consideration for the promise.' Willes J. further makes it quite clear that the rule operates regardless of the agent's knowledge of his lack of authority. With respect, it is submitted that the word 'authority' was used throughout to indicate 'power,' as conceived by Professor Seavey.[10] If the agent merely lacked authority whilst retaining power then the principal would have been liable to the third party so that no question of the agent's liability to anyone other than his principal would have arisen.

Because of this contractual view of the agent's liability it was impossible in *Drew* v. *Nunn* to fix liability on the wife who, in the then state of the law, had no contractual capacity. Moreover, as a husband was only contractually liable for his wife's necessaries it was impossible to base his liability on contract. In addition, as a married woman was incapable of binding herself in contract, neither she nor her husband could be sued for the wife's tort if it was immediately connected with a contract purported to be entered into by her.[11] Had Brett L.J. distinguished between authority and power he would have been able to say that although the wife's authority had been revoked she still retained the power to bind her husband to the plaintiff until such time as the plaintiff had notice of the revocation of her authority. As things stood he was driven into basing the husband's liability on the very wide proposition that 'where one of two persons both innocent must suffer by the wrongful act of a third

---

7 [1897] 4 Q.B.D. at 666.

8 (1857) 8 E. & B. 647.

9 [1903] A.C. 114.

10 *Op. cit.*

11 *Liverpool Adelphi Loan Association v. Fairhurst* 9 Exch. 422.

person, that person making the representation which, as between the two, was the original cause of the mischief, must be the sufferer and bear the loss.'[12] This comes very near to basing a cause of action, sounding in damages, on innocent misrepresentation. In *Starkey* v. *Bank of England* it was stressed that the rule in *Collen* v. *Wright* was not an exception to the rule of no damages for financial loss caused by innocent misrepresentation but was based solely on breach of an implied contract.[13]

Cotton L.J. considered it unnecessary to decide whether or not the defendant's insanity revoked the wife's authority and based his judgment on the principle that even if insanity did revoke the authority the defendant remained liable on transactions entered into by the wife with the plaintiff before the plaintiff received notice of the defendant's insanity.[14] It is submitted that this view implicitly distinguishes authority from power.

Bramwell L.J. considered that insanity short of dementia did not revoke the agent's authority and that as there was no evidence of dementia the defendant remained liable on all transactions effected by his wife, as his agent, during his insanity.[15]

It is difficult to abstract any firm principles from these varying judgments as they tend to give different answers to three of the four questions involved and only agree in giving an affirmative answer to the fourth, namely, 'Has the principal any liability to third parties?'

Today, if the wife's power ceases on her husband's insanity then in a similar case to *Drew* v. *Nunn*, if her relationship with her husband was in fact one of principal and agent, she will be personally liable to the third party for breach of contract under the rule in *Collen v. Wright*. This seems to be a reasonably just solution unless the husband has received a material benefit from the transaction purportedly entered into by his wife with the third party. In such a case it would be manifestly unjust for his wife to be saddled with full liability and, indeed, if she were without means the third party would be gravely prejudiced. A possible and fair solution was adumbrated by the High Court of Australia in *McLaughlin* v. *Daily Telegraph*.[16] In that case the wife of an insane husband under a void power of attorney sold and transferred certain of her husband's shares in the defendant companies. On recovering his sanity the husband brought suit in Equity to compel the defendants to rectify their registers by entering his name as holder of a number of shares equal to the number sold, and also as holder of certain other shares to which he would

---

12 [1897] 4 Q.B.D. at 667, 668.

13 [1903] A.C. 114, *per* Halsbury L.C.J. at 118: 'That which does enforce the liability is this—that under the circumstances of this document being presented to the bank for the purpose of being acted upon, and being acted upon on the representation that the agent had the authority of the principal, which he had not, that does import an obligation—the contract being for good consideration—an undertaking on the part of the agent that the thing which he represented to be genuine was genuine.'

14 [1879] 4 Q.B.D. at 669.

15 *Ibid.*

16 (1904) 1 C.L.R. 243, at 280, 281; affirmed *sub nom. Daily Telegraph* v. *McLaughlin* [1904] A.C. 776.

have been entitled by way of bonus issues had he remained the registered holder of the original shares. In holding that the husband was entitled to the relief prayed Griffith C.J. considered that the defendants, on the authority of *Starkey* v. *Bank of England*, would be entitled to an indemnity from the plaintiff's wife and that she in her turn would be entitled to recover from her husband to the extent of any benefit he had derived from the unauthorised transaction. In fact, the husband had agreed to account for any such benefits direct to the defendants so that the question did not arise. But the Chief Justice did venture an opinion to the effect that had the husband not agreed, the defendants, to avoid circuity of action, might have been enabled to sue the husband direct for the return of such benefits, they being subrogated to the wife's rights in the matter.[17]

In cases where necessaries are not involved and the husband receives no material benefit from the transaction it may well be that the transaction is not one of agency at all. In *Drew* v. *Nunn*, Bramwell L.J. indicated what the true position may be when he said that 'the facts before us resemble the case of a guarantee.'[18] Of course, because at that time a wife had no contractual capacity she was not a debtor so that her husband could not have been her guarantor.[19] Today when the goods are not necessaries and are intended solely for the wife's use the equitable presumption of advancement in her favour would vest the property in her. Thus, in effect what the husband is representing to the third party, either in words or by his conduct, is, 'Provide my wife with the goods and I will pay you for them' or, possibly, a very unlikely case, 'Provide my wife with the goods and if she does not pay you for them I will.' In such cases it would appear that the transaction is not one of agency at all but either an indemnity or a guarantee. It is then relevant to consider the legal effect of the supervening insanity of the indemnifier or guarantor on such contracts when they are of a continuing nature.

In Chitty on Contracts[20] the view is taken that the surety in a continuing contract of either indemnity or guarantee remains liable for advances made after his insanity until the creditor becomes aware of the incapacity. The only case directly in point seems to be *Bradford Old Bank* v. *Sutcliffe*.[21] In that case, at first instance, Lawrence J. held that the continuing guarantee ceased only when the creditor had notice of the guarantor's insanity. This was accepted by the parties so that the question was not really considered by the Court of Appeal. In *Imperial Loan Co.* v. *Stone*[22] the question was whether an insane person, not so found,[23] can enter into a contract of guarantee. It was held by the Court of Appeal that he can and that he can avoid the contract only if he is able to prove both the existence of the incapacity and the creditor's knowledge of it.

17 *Ibid.* at 280.
18 [1879] 4 Q.B.D. at 669.
19 *Coutts & Co. v. Browne Lecky* [1947] K.B. 104.
20 21st ed., vol. 2 at 475.
21 [1918] 2 K.B. 833.
22 [1892] 1 Q.B. 599.
23 *I.e.*, not so found by inquisition, a practice which has fallen into disuse.

It would be strange if the guarantor's subsequent insanity were to revoke a guarantee already validly subsisting in circumstances where it does not prevent the creation of a guarantee.

To summarise the position as it might be today. Where the relationship of principal and agent has been established prior to the principal's insanity:

1. (*a*) If the subsequent insanity of the principal does in fact revoke the agent's authority but without divesting the agent of power then the principal is fully liable to the third party. Of course, as between principal and agent, the latter will have to indemnify the former but this indemnity will be tempered by any material benefit received by the principal from the transaction.

   (*b*) If the subsequent insanity of the principal divests the agent of power then the agent will be liable to the third party on the principle laid down in *Collen* v. *Wright* but, if the position indicated in *McLaughlin* v. *Daily Telegraph* is accepted, then the principal must indemnify the agent to the extent of the material benefit that the principal has received from the transaction.

2. In cases where the person dealing with the third party enters into a transaction purely for his own benefit, but in circumstances where it is contemplated that another is to be liable to the third party, then it seems right to apply the law relating to contracts of indemnity and guarantee.

3. Where the transaction entered into is one for the purchase of necessaries then the position must now be considered in the light of the Sale of Goods Act 1893, section 2.[23a]

> Capacity to buy and sell is regulated by the general law concerning capacity to contract, and to transfer and acquire property:
>
> Provided that where necessaries are sold and delivered to . . . a person who by reason of mental incapacity . . . is incompetent to contract, he must pay a reasonable price therefor.
>
> Necessaries in this section . . .

It will be noted that the section only applies where the necessaries are delivered, *i.e.*, to executed contracts, so that the general law applicable to capacity to contract and to transfer and acquire property at the time of the passing of the Act is as stated by Patteson J. in the Court of Exchequer Chamber in *Molton* v. *Camroux*.[24]

> . . . the modern cases shew that when that state of mind was unknown to the other contracting party and no advantage was taken of the lunatic, the defence cannot prevail, especially where the contract is not merely executory but executed in whole or in part and the parties cannot be restored altogether to their original position.

It seems therefore that the section only applies when the seller is aware of the insanity of the buyer and that unless this is so the buyer will be

---

[23a] N.S.W., s.7; Vic., s.7; Q'ld., s.5; Tas., s.7; W.A., s.2; N.Z., s.4.

[24] (1849) 4 Exch. 17, at 19; 154 E.R. 1107 at 1108.

liable for the full price under the rule in *Molton* v. *Camroux*. Thus, when the transaction is entered into by an agent on behalf of an insane principal under conditions making the section applicable there seems to be no reason why the principal, who by definition will have received the benefit directly or indirectly, should not be liable to pay a reasonable price to the seller.

These possible solutions still leave unanswered the question as to the effect of the principal's insanity on his agent's authority, but it is submitted that the existence of authority is relevant only to the position as between principal and agent and that in considering the liability of either to the third party all that matters is whether or not the agent had power. As to revocation of authority *Drew* v. *Nunn* provides no answer and, indeed, if the method of indemnity outlined in *McLaughlin* v. *Daily Telegraph* is adopted the question becomes largely academic. On the facts of *Drew* v. *Nunn* it would be surprising if as between husband and wife her authority to pledge his credit had not been revoked prior to his insanity when he assigned his whole income to his wife thereby leaving no credit to pledge.

The widest ratio that can be extracted from *Drew* v. *Nunn*, if Professor Seavey's terminology is adopted, is that whether or not an agent's authority is revoked by the principal's insanity, the agent will not be divested of his power to create legal relations between the principal and third parties, to whom he has been held out by the principal as having such power, unless the third parties are aware of the insanity. Can such a ratio be reconciled with the later case of *Yonge* v. *Toynbee* or must either one or both of the cases be confined to its special facts?

In *Yonge* v. *Toynbee* the defendant when sane expressly authorised a firm of solicitors, Messrs. Wontner & Sons, to act for him as defendant in a defamation action, and he wrote to the plaintiff's solicitors expressly informing them of the appointment. Before the issue of a writ in the action the defendant became insane. In ignorance of their client's incapacity the defendant's solicitors accepted service of the writ, entered an appearance and filed a defence on his behalf. Some time later the defendant's solicitors became aware of their client's disability and informed the plaintiff's solicitors accordingly. After abortive negotiations with the defendant's solicitors for the appointment of a representative to carry on the action on the defendant's behalf, the plaintiff's solicitors applied to the Master for an order that the appearance in the action and all proceedings subsequent thereto should be struck out and that the defendant's solicitors should personally pay to the plaintiff her costs of the action. The Master made the order except in so far as it related to the solicitors' personal liability for costs and on appeal his order was affirmed by Sutton J. in chambers. The plaintiff appealed to the Court of Appeal against the refusal to order the defendant's solicitors to pay her costs.

Both Buckly L.J. and Swinfen Eady J. held that the solicitors' authority to act was terminated by the insanity of their client even though

they were unaware of his condition. Although *Drew* v. *Nunn* had been cited to them in argument the case is not referred to in their judgments and they give no reason why the 'authority' was terminated. Then, applying the rule in *Collen* v. *Wright*, they held the defendant's solicitors liable for the damage caused to the plaintiff, namely, her costs of the abortive action. Again, it is submitted that 'authority' was used in the sense of 'power.' It is true that it was decided in *Starkey* v. *Bank of England* that the rule in *Collen v. Wright* was not limited to cases of contracts purported to be made by an agent but extended to all transactions entered into by him without the principal's 'authority'.[25] To that extent the view of Buckley L.J. that 'the particular nature of the agency is not, I think, very material',[26] is, with respect, indisputable. But although the particular transaction entered into may not be relevant once the agent's lack of power has been established, it may well be the deciding factor in establishing whether or not it existed. If this view is accepted it would be reasonable to suppose that a principal's insanity does not terminate the agent's power to involve him in legally binding transactions of the type which he could effect in person despite his insanity unless the other party to the transaction is aware of the insanity. Once again the agent's knowledge of the insanity is not relevant when one considers the termination of his power. What would be relevant, as it is in the case of an insane person entering into a transaction without the intervention of an agent, is whether or not the other party to the transaction knows of the disability. On the other hand, it would again be reasonable to suppose that, if the transaction to be effected is of the kind which in any circumstances cannot be entered into by an insane person, both the agent's power and his authority will terminate automatically on the insanity of his principal regardless of either his or the third party's knowledge of the incapacity.

In contrast to Buckley L.J., Swinfen Eady J. placed great emphasis on the special position of solicitors in the conduct of proceedings on their clients' behalf before the Court.[27]

Vaughan Williams L.J. seems to have concurred mainly for the sake of conformity. 'Reluctantly, and not without doubt, I have yielded to the views expressed by my brethren'.[28]

Again it is not easy to extract a clear rule of law from the judgments. The widest ratio that the principal's insanity *ipso facto*, and regardless of the knowledge of either agent or third party, terminates the agent's authority and his power leaving him and not the principal liable to the third party is a flat contradiction of anything that can fairly be abstracted from *Drew* v. *Nunn*.

---

25 [1903] A.C. 114, *per* Lord Davey at 119: '. . . but it extends to every transaction of business into which a third party is induced to enter by a representation that the person with whom he is doing business has the authority of some other person.'

26 [1910] 1 K.B. at 228.

27 *Ibid.*, at 233, 234.

28 *Ibid.*, at 234.

Cheshire & Fifoot,[29] *Law of Contract*, and Wilson's *Principles of Contract*[30] take the view that even the above wide ratio of *Yonge* v. *Toynbee* can be reconciled with *Drew* v. *Nunn* on the basis that in the latter case the principal remained liable because of the estoppel arising from his having held out the agent to the third party, whereas the principal was not liable in *Yonge* v. *Toynbee* because the agency was not one by estoppel. It is submitted that this proposition cannot withstand examination and that it merely illustrates the danger inherent in the practice of describing an agency created by implied representation as an agency by estoppel, in an attempt to distinguish it from an agency created by an expressly conferred authority. In *Drew* v. *Nunn* the agent's power was represented to the third party by the conduct of the principal whereas in *Yonge* v. *Toynbee* the solicitors' authority was expressly conferred upon them by their client, who also wrote to the plaintiff's solicitors informing them that Messrs. Wontner & Sons were empowered to act on his behalf.[31] If, then, the cases can be reconciled on this basis it involves the curious proposition that a representation by conduct raises an estoppel whilst an express representation in writing does not.[32]

It has also been suggested that the cases are reconcilable on the basis that had the principal in *Yonge* v. *Toynbee* been sued on the basis of estoppel he would have been held liable for the payment of the plaintiff's costs.[33] This does not accord with either the facts or the law. The principal was Toynbee, the defendant in the action, and Messrs. Wontner and Sons were made liable for the costs in pursuance of the Court's inherent disciplinary jurisdiction over solicitors.[34] The basic reason why Toynbee could not have been made liable is that under the Rules of the Supreme

---

29 5th ed. at 415: 'It is true that his lunacy does in fact revoke the authority of the agent (*Yonge* v. *Toynbee* and *Drew* v. *Nunn*) . . . , but if while sane he has held out his agent to third parties as having authority, then the authority is presumed to continue despite a change in his mental condition unless and until the third party receives notice of the revocation (*Drew* v. *Nunn*). In other words it determines the contract as between principal and agent, but the principal may still be liable to a third party on the ground of estoppel.'

30 At 231: 'Nevertheless the husband remained liable to the tradesman since "In this case the wife was held out as agent, and the plaintiff acted upon the defendant's representation as to her authority without notice that it had been withdrawn" (*Drew* v. *Nunn*). But in the absence of an agency by estoppel, the insanity will automatically terminate the agency. Thus in *Yonge* v. *Toynbee* . . . .'

31 [1910] 1 K.B. at 228, 229, *per* Buckley L.J.: 'On the other hand it must be borne in mind that after August 21, when the defendant Toynbee wrote to the plaintiff's solicitors, referring them to Messrs. Wontner & Sons, the plaintiff could not consistently with professional etiquette communicate personally with the defendant.'

32 A. H. Hudson in *Can.B.Rev.* 37 (1959), 497, appears to favour the estoppel solution (see 501, note 36, and his concluding sentence at 503): 'The ordinary holding out rules seem perfectly capable of giving a just and reasonable solution in this type of case.'

33 *Stephen' Commentaries* (19th edition), vol. 3, chapter on Agency by C. H. S. Fifoot, at 246: '2. AS REGARDS THIRD PARTIES. The general rule has been stated by Sir Frederick Pollock: "The termination of the authority of the agent does not take effect . . . so far as regards third parties, before it becomes known to them . . . . The case of *Yonge* v. *Toynbee, supra,* is not inconsistent with this rule. In that case, the question of a claim against the principal on the basis of estoppel was not raised".'

34 [1910] 1 K.B. at 235, *per* Vaughan Williams L.J.: '. . . I should have thought it a better course to leave the plaintiff to her action rather than dispose of the matter on a summary disciplinary order.'

Court a person of unsound mind is barred from action in the Courts[35] until application has been made on motion or by petition for the appointment of a guardian *ad litem*. As a result of this any proceedings by or against a lunatic before such appointment are a complete nullity. In other words, an action in the Courts is a transaction into which a lunatic cannot enter, either in person or through solicitors, until a guardian *ad litem* has been appointed by the Court.

As in *Drew* v. *Nunn* much of the difficulty in *Yonge* v. *Toynbee* stems from the confusion of authority and power. In the long history of agency law this confusion has been common enough, but it is surprising that it still survives in the face of all that has been written with a view to emphasising the distinction. As recently as 1957 it was stated in the New Brunswick Supreme Court, Appeal Division, that 'Unsoundness of mind . . . is . . . sufficient to determine a contract of agency, though the authority of the agent is not revoked with regard to a third person who has been dealing with the agent unless such third person has knowledge of the mental incompetency of the principal'.[36] Surely, a less confusing approach is to pose the two questions: 'Does the principal's insanity revoke the authority of the agent to act?', and, 'If so, does such revocation deprive the agent of power to bind his principal to third parties?'

The judgments in *Drew* v. *Nunn* give different answers to the first of these questions and a negative answer to the second, whereas *Yonge* v. *Toynbee* gives an affirmative answer to each. This renders the two cases irreconcilable in so far as each purports to set out a general proposition of law. Unless, therefore, one is to be adopted and the other disregarded they must either be distinguished by confining each to its special facts or combined to indicate a possible rule of law that will be valid in all situations.

It is, perhaps, trite law to state that the relationship of principal and agent exists primarily to bring about legal relations between the principal and a third party and that, as a general rule, once that has been achieved the agent drops out. In such cases the legal obligations of the principal and the third party, *inter se*, are determined by the law governing the

---

35 R.S.C., O. 16, p. 17, provides that 'Where lunatics and persons of unsound mind not so found by inquisition might respectively, immediately before November 1, 1875, have sued as plaintiffs or would have been liable to be sued as defendants in any action or suit, they may respectively sue as plaintiffs in any action by their committee or next friend, according to the practice of the Chancery Division, and may in like manner defend any action by their committees or guardians appointed for that purpose.' The practice of Chancery was described by James L.J. in *Beall* v. *Smith* (1873) L.R. 9 ch. 85 at 91: 'The law of the Court of Chancery undoubtedly is that in certain cases where there is a person of unsound mind, not found so by inquisition, *and therefore incapable of invoking the protection of the Court*, that protection may in proper cases, and if and so far as may be necessary & proper, be invoked by any person as his next friend.' This statement of the practice was approved after the Judicature Act 1873, by Sir George Jessel M.R. in *Jones* v. *Lloyd*, L.R. 18 Eq. 265, at 276, and the passage *underlined* is clear authority for the proposition that a person of unsound mind is incapable of conducting a legal action except through his committee or guardian.

It is interesting to note that in *Beall* v. *Smith*, at 97, the lunatic's solicitors were held liable for all the costs of the action.

36 *Re Parks, Canadian Permanent Trust Co.* v. *Parks* (1957) 8 D.L.R. (2d) 155, *per* Bridges J. at 162.

transaction effected. When, therefore, the capacity of the principal is in issue it seems relevant, in cases where the relationship of principal and agent came into being before the insanity of the principal, to consider the capacity of the principal to enter into the type of transaction purported to be entered into on his behalf by his agent subsequent to the supervening insanity. In the cases of ratification it has been held, *inter alia*, that the transaction to be ratified must be one which the principal could, at the time the agent acted, have entered into.[37] Similarly, one would expect to find that a lunatic on recovering sanity can ratify transactions entered into on his behalf during his insanity provided that the transactions are those that a person of unsound mind could enter into in person. Following from this, in cases where the agent has power, whether derived from authority or not, to act on behalf of his principal, there seems to be no valid reason why that power should be terminated by the principal's supervening insanity unless the transaction is one that a person of unsound mind could not enter into in person.

On this view *Drew* v. *Nunn* and *Yonge* v. *Toynbee* are clearly distinguishable in that a lunatic, not so found, can enter into a valid contract unless the other party was aware of the mental incompetence at the time of contracting, whereas a person of unsound mind cannot conduct a legal action in the Courts without the intervention of the Master in Lunacy. It is submitted that it is open to the Court of Appeal to distinguish the two cases on this basis and, furthermore, that it is possible to lay down a rule of law causing the minimum inconvenience to all concerned without being inconsistent with the findings in either of the two cases under review.

A short summary of the suggested rule and of the consequences of its application on the position of each party may be of assistance.

The Rule. Once the relationship of principal and agent has been established the subsequent insanity of the principal will only deprive the agent of his power to establish legal relations between the principal and third parties if either (*a*) the third party knows of the principal's insanity or (*b*) the transaction is one that a person of unsound mind could not have entered into in person.

1. If the transaction is binding on the principal then he is liable to the third party but to the extent that such liability exceeds the material benefit he has derived he may claim indemnity from the agent if the agent knew of the insanity.

2. If the transaction is void or voidable because the third party knew of the principal's insanity then it does not seem unfair that the third party should bear the loss.

3. If the transaction is one that an insane principal cannot enter into in person and provided that the third party has no knowledge of the principal's mental incompetence the liability will fall upon the agent but subject to an indemnity from his principal to the extent of any material benefit derived by the principal.

---

[37] *Ashbury Railway Carriage & Iron Co. v. Riche* (1875) L.R. 7 H.L. 653.