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COMMERCIAL LOAN OFFICERS' AUTHORITY TO BIND A BANK

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The author believes that banks need to be cautious about actions taken without actual authority which could bind a bank. If an agent's actions can be construed as being taken with the approval of a bank or the bank has manifested some indication that such action was authorized, a bank could find itself liable for such agent's actions. Also, if a bank ratifies actions, even if unauthorized, the bank will be held responsible.

Every bank has lending policies and procedures, part of which identify and define a commercial lending officer's authority to make loans and to extend credit. That is known as actual authority and is based upon parameters that have been memorialized and approved by the bank's management and board of directors. Actual authority defines the extent to which a commercial lending officer is authorized to bind the bank. However, even in the absence of actual authority, a commercial lending officer's actions might still bind a bank under the doctrines of apparent authority, implied authority, agency by estoppel, or ratification.¹ While the common theme in each of these approaches is that an agent cannot expand his own authority, courts have found that institutions can be bound by an agent's unauthorized actions if third parties have been led to believe that such bank officer had authority. Agency by estoppel and ratification also require that the third party's reliance on such actions be reasonable.

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ACTUAL AUTHORITY

One way to create an agency relationship² is for the principal to confer actual authority on the agent.³ Actual “authority to do an act can be created by written or spoken words or other conduct of the principal which, reasonably interpreted, causes the agent to believe that the principal desires him so to act on the principal’s account.”⁴

Actual authority is that which is “actually granted by the principal, and it may be express or implied.”⁵ In *Progressive Cas. Ins. v. Ehrhardt*, the appellees contended that Progressive was obligated to cover losses under an insurance policy because Progressive’s chief underwriter backdated an insurance policy and in doing so waived Progressive’s ability to not cover losses.⁶ The court explained that in order to find that Progressive waived its right to not cover losses, the chief underwriter must have been authorized by Progressive to backdate the policy.⁷ The court noted that Progressive did in fact authorize *some* underwriters to backdate policies.⁸ However, these underwriters could only do so upon the explicit approval of an office supervisor after the insured had provided a written declaration of no loss, and when the renewal payment was received within five days of the policy expiration.⁹ In *Progressive*, the chief underwriter failed to get the approval of the office supervisor or written declaration of no loss, and the renewal payment was not received on time.¹⁰ Therefore, the chief underwriter did not have the actual authority to backdate the insurance policy, and the act of doing so was unauthorized so it could not serve as the reason to bind Progressive.¹¹

Agri Export Cooperative v. Universal Savings Association,¹² involved a lawsuit to enforce a letter of credit issued by the defendant bank. The bank president, who was expressly authorized to make loans without further approval from the board of directors, issued a \$1 million letter of credit.¹³ Upon a demand for payment, the bank refused to honor the letter of credit without providing any reason.¹⁴ The court inferred from the evidence that the president had actual authority to issue the letter of credit.¹⁵

Similarly in *First Interstate Bank of Texas, N.A. v. First National Bank of Jefferson*,¹⁶ the issue was whether a senior vice president had authority to execute a bond purchase agreement for the defendant. The Fifth Circuit noted that actual authority can be implied or express.¹⁷ The court added that a principal can confer actual authority orally; there need not be a corporate

resolution or by-law specifically authorizing a transaction.¹⁸ Because of his status as a senior vice president and his responsibilities, together with corroborating testimony about defendant's authorization that he could sign the bond agreement, the Fifth Circuit concluded that whether he had express actual authority was a jury question.¹⁹

APPARENT AUTHORITY

Under the doctrine of apparent authority, a principal will be bound by a person purporting to act for him only where the principal's words or conduct cause the third party to believe that the principal consents or has authorized the agent's conduct.²⁰ In *Iceland Telecom*, the alleged agent shared office space and phone service with the principal and used the principal's fax cover sheet.²¹ The court concluded that, notwithstanding these facts, nothing in the record had established a principal-agent relationship between the two; their actions did not manifest any intent to create such a relationship.²²

"The apparent power of an agent is to be determined by the *acts of the principal*, and not by the acts of the agent." (Emphasis added.) In *Homa v. Friendly Mobile Manor, Inc.*,²³ despite that fact that there was a piece of correspondence on the principal's letterhead, and the purported agent shared office space with the principal, the court concluded that there was "no evidence that [the principal] knew or should have known about this particular transaction."²⁴ The court held that a principal is responsible for the acts of an agent within his apparent authority "only where the principal by his acts of conduct has clothed the agent with the appearance of authority, and not where the agent's own conduct and statements have created the apparent authority."²⁵ The court upheld the trial court's determination that the plaintiff had failed to show reliance on agency based on apparent authority.²⁶

A principal needs to act in some affirmative way to confer apparent authority which cannot be founded solely upon the agent's acts or statements.²⁷ In *Roberston's Crab House*, the restaurant sued the bank for improper payment of checks deposited by an accountant who had done work for the restaurant for 21 years and who was authorized to deposit checks but not to his own account. The bank argued that the accountant was the restaurant's agent by virtue of apparent authority and that it was justified in relying on this au-

thority.²⁸ However, the court found that “it is clear that Hanson had no actual or apparent authority to receive the proceeds of the eleven checks here involved.”²⁹

Also, as the Maryland Court of Special Appeals noted in *Robertson's Crab House, Inc.*, “[a] third person dealing with a purported agent should communicate with the principal to verify the agent's authority to sign.”³⁰ Nobody from Robertson's restaurant made any manifestation to the bank that the accountant was authorized to divert checks to his own account.³¹ The court also determined that the bank had been misled by an appearance of authority not known and acquiesced by the principal and not by apparent authority.³²

One fact a party seeking to rely on agency relationship based on apparent authority must establish is that the third party knew of the facts and, acting in good faith, had reason to believe, and did actually believe, that the agent possessed such authority. The U.S. Court of Appeals for the Fourth Circuit has explained that under Maryland law the “mere fact that one is dealing with an agent, whether the agency be general or special, should be a danger signal, and like a railroad crossing, suggests the duty to ‘stop, look and listen,’ and he who would bind the principal is bound to ascertain, not only the fact of agency, but the nature and extent of authority....” (citation omitted.)³³ The court criticized the plaintiff for not availing itself of its right to determine the exact scope of the alleged agent's duties.³⁴ Finding insufficient evidence of actual or apparent authority, the court rejected the breach of contract claim.³⁵

IMPLIED AUTHORITY

Some courts have recognized that an agent with implied authority may bind its principals. For example, “the responsibility of the principal to third persons is not confined to cases where the contract has been actually made under express or implied authority. It extends further and binds the principal in all cases where the agent is acting within the scope of his usual employment, or is held out to the public, or to the other party, as having competent authority, although, in fact, he has, in the particular instance, exceeded or violated his authority...for in all such instances, where one or two innocent persons is to suffer, he ought to suffer who misled the other into the contract, by holding out the agent as competent to act, and as enjoying his confidence.”³⁶

The U.S. District Court for New Jersey recently described implied authority as follows: "...implied authority — that is to do all that is proper, customarily incidental and reasonably appropriate to the exercise of the authority granted. The New Jersey Supreme Court has explained that implied authority rests upon the nature or extent of the function to be performed, the general course of conducting the business, or from the particular circumstances in the case."³⁷

In *First Interstate Bank of Texas, N.A. v. First National Bank of Jefferson*,³⁸ the Fifth Circuit defined implied authority as "actual authority" which is inferred from the circumstances and notice of the agency. The agent is vested with the implied authority to do everything necessary or incidental to the agency assignment.³⁹ Implied authority connotes permission from the principal for the agent to act, even though permission is not expressly set forth orally or in writing.⁴⁰ In light of a Louisiana statute requiring express actual authority, the Fifth Circuit held that plaintiff could not state a claim for implied authority.⁴¹

AGENCY BY ESTOPPEL

The Maryland Court of Special Appeals has held that: "Like apparent authority, an agency by estoppel can arise only where the principal, through words or conduct, represents that the agent has authority to act and the third party *reasonably* relies on those representations" (emphasis in the original).⁴² The Court of Special Appeals emphasized that "reasonable reliance is a critical element."⁴³ In that case, the court found that, as a matter of law, it was clearly not reasonable for the plaintiff to believe that the agent had any authority.⁴⁴

Other courts have also recognized the principle of agency by estoppel. For example, in *Jackson v. 2109 Brandywine, LLC*,⁴⁵ the court stated: "An agency by estoppel can arise only where the principal, through words or conduct, represents that the agent has authority to act and the third party reasonably relies on those representations." In *Wailes & Edwards, Inc.*,⁴⁶ the court noted as follows: "... [A] permissible finding of apparent authority often is based on elements of estoppel: 'like apparent authority [estoppel] is based on the idea that one should be bound by what he manifests irrespective of fault; but it operates only to compensate for loss to those relying upon the words and not to create

rights in the speaker. It follows, therefore, that one basing his claim on the rules of estoppel must show not merely reliance, which is required when the claim is based upon apparent authority, but also such a change in position that it would be unjust for the speaker to deny the truth of his words.”

RATIFICATION

Ratification occurs when a principal later adopts an agent's unauthorized act, giving it the same effect as if it had originally been authorized.⁴⁷ The principal ratifies by simply indicating the intention to treat the act as authorized.⁴⁸ Ratification requires an intention to ratify and knowledge of all material facts.⁴⁹ In *Integrated Consulting*, the court found no evidence of an intention to ratify. “Inasmuch as knowledge of the material facts is an essential element of ratification, this claim must be rejected.”⁵⁰ Ratification also requires a knowledge of and acceptance of a benefit without taking steps to disavow it.⁵¹ In *Kuwait Airways Corp. v. American Security Bank, N.A.*,⁵² the jury found that the agent's conduct was implicit with apparent authority and the bank asserted a defense of ratification. On appeal, the U.S. Court of Appeals for the D.C. Circuit held that facts did not compel a finding of ratification.⁵³ The court noted that to ratify an unauthorized act, a principal must have knowledge of the act and may ratify the act implied by, but the conduct implying ratification must be an act that is inconsistent with any other hypothetical.⁵⁴

CONCLUSION

When an agent acts with actual authority, a bank is aware of the scope of his or her actions. Banks need to be cautious about actions taken without actual authority which could bind a bank. If an agent's actions can be construed as being taken with the approval of a bank or the bank has manifested some indication that such action was authorized, a bank could find itself liable for such agent's actions. Also, if a bank ratifies actions, even if unauthorized, the bank will be held responsible. Upon discovery of unauthorized actions, it is imperative that a bank disavow any authority to eliminate any ratification argument.

NOTES

¹ *Agri Export Cooperative v. Universal Savings Association*, 767 F. Supp. 824, 829 (S.D. Tex. 1991) (elementary that bank is bound by acts of its officers while acting within the scope of their authority, either actual or apparent); *see also In re Canal Refining Co.*, 2008 WL 5157458, at *3 (Bankr. W.D. La. June 13, 2008) (corporate officers' actions bind corporation in same way that acts of any agent would bind corporation through actual authority, apparent authority or ratification).

² The cases are uniform that agency is a question of fact and that the party seeking to demonstrate agency relationship has the burden of proof. *See, e.g., Bouffard v. State Farm Fire & Casualty Company*, 162 N.H. 305, 27 A.3d 682, 687 (2011) (agency relationship is question of fact); *National Mortgage Warehouse, LLC v. Bankers First Mortgage Co., Inc.*, 190 F. Supp. 2d 774, 779 (D. Md. 2002) (Question of agency in factual one); *First Union National Bank v. Brown*, 186 N.C. App. 519, 603 S.E. 2d 808, 815 (2004) (where evidence is conflicting, extent of agent's authority is question of fact); *Green Leaves Restaurant, Inc. v. 617 H Street Associates*, 974 A.2d 222, 230 (D.C. App. 2009) (agency is question of fact and party asserting agency has burden of proof).

³ *Citizens v. Maryland Indus.*, 338 Md. 448, 459, 659 A.2d 313, 318 (1995) (quoting Restatement (2nd) of Agency §26 (1958)).

⁴ *Id.* *See also Trip Mate, Inc. v. Stonebridge Casualty Insurance Co.*, 2013 WL 1628502, at *4 (W.D. Mo. April 16, 2013) (actual authority is created by written or spoken words or other conduct which reasonably causes agent to believe agent is authorized to act on principal's behalf); *Sarkes Tarzian, Inc. v. U.S. Trust Company of Florida Savings Bank*, 397 F.3d 577, 583 (7th Cir. 2005) (principal confers actual authority on agent when he objectively manifests to agent consent to agency).

⁵ *Progressive Cas. Ins. Co. v. Ehrhardt*, 69 Md. App. at 440, 518 A.2d 151, 155, quoting 3 Am. Jur.2d Agency §71, at 575 (1986) (footnotes omitted); *see also GGNOSC Omaha Oak Grove, LLC v. Pagich*, 2012 WL 2021868, at *6 (D. Neb., June 5, 2012) (actual authority is that which principal expressly grants to agent or that principal consents to); *Bouffard v. State Farm Fire and Casualty Co.*, 162 N.H. 305, 27 A.3d 682, 687 (2011) (actual authority arises when principal explicitly manifests authorization of agent's actions).

⁶ *Progressive Cas. Ins. v. Ehrhardt*, 518 A.2d at 155; *See also Three Minnows, LLC v. Cream, LLC*, 2013 WL 1453246, at *4 (Iowa App. April 10, 2013) (actual authority exists if principal has either expressly or by implication granted agent authority to act on principal's behalf).

⁷ 518 A.2d at 155.

⁸ *Id.*

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.*; See Also *Dickerson v. Longoria*, 995 A.2d 721, 735 (principal can be legally bound by agent's actions if principal confers actual authority).

¹² 767 F. Supp. 824 (S.D. Tex. 1991); see also *Municipality of Bremanger v. Citigroup Global Markets Inc.*, 201e WL 1294615, at * 20 (S.D.N.Y. March 28, 2013) (apparent authority created only by principal's representations to third party and agent cannot create apparent authority by his own actions or representations); *Farm & Ranch Services, Ltd. v. LT Farm & Ranch, LLC*, 779 F. Supp. 2d 949, 962 (S.D. Iowa 2011) (apparent authority is authority principal has knowingly permitted or held out agent as possessing).

¹³ 767 F. Supp. at 825.

¹⁴ *Id.* at 826.

¹⁵ *Id.* at 830.

¹⁶ 928 F.2d 153, 154 (5th Cir. 1991).

¹⁷ *Id.* at 156.

¹⁸ *Id.*

¹⁹ *Id.* at 157.

²⁰ *Iceland Telecom, Ltd. v. Information Systems and Networks Corp.*, 268 F. Supp.2d 585, 592 (D. Md. 2003); See also *Sarkes Tarzian, Inc. v. U.S. Trust Company of Florida Savings Bank*, 397 F.3d 577, 583 (7th Cir. 2005) (apparent authority is created by principal's words or conduct communicated to third party that give rise to appearance and belief that agent possesses authority to enter into transaction).

²¹ 288 F. Supp. 2d at 588.

²² *Id.* at 592. See also *Trip Mate, Inc. v. Stonebridge Casualty Insurance Co.*, 2013 WL 1628502, at *5 (W.D. Mo., April 16, 2013) (agent acts with apparent authority when principal manifests consent to exercise of authority, person relied on facts and had reason to believe and believed that agent possessed authority and acted to his detriment).

²³ 93 Md. App. 337, 363, 612 A.2d 322, 335 (1992); see also *Sarkes Tarzian, Inc. v. U.S. Trust Company of Florida Savings Bank* at 583 (agent cannot confer apparent authority on himself); *GGNSC Omaha Oak Grove LLC v. Pagich*, 2102 WL 2021868, at *6 (D. Neb. June 5, 2012) (apparent authority is based on principal's manifestations and cannot be established by agent's conduct).

²⁴ 612 A.2d at 364.

²⁵ *Id.*

²⁶ *Id.*; see Also *Jackson v. 2109 Brandywine, LLC*, 180 Md. App. 535, 568, 952 A.2d 304, 323 (2008) (apparent authority is based upon some action by principal that leads third party to believe that principal has authorized agent's acts); *Integrated*

Consulting Services, Inc. v. LLDS Communications, Inc., 996 F. Supp. 470, 476 (D. Md. 1998) (Maryland law is clear that agent's apparent power is to be determined by the acts of the principal and not by agent's acts) (citation omitted).

²⁷ *Bank of Southern Maryland v. Robertson's Crab House, Inc.*, 39 Md. App. 707, 713, 389 A.2d 388, 394 (1978).

²⁸ *Id.* at 715; *See also Mauldin Furniture Galleries, Inc. v. BB&T*, 2012 WL 3680426, at *9 (D.S.C. Aug. 27, 2012) (third party can rely on agent's apparent authority until something occurs that would cause reasonable person to inquire further into circumstances) (citations omitted).

²⁹ 389 A.2d at 716; *see also Dickerson v. Longoria*, 414 Md. 419, 441-442, 995 A.2d 721, 735 (2010) (agent cannot enlarge actual authority by own acts); *Frederick W. Berens, Inc. v. Fidelity Mut. Life Ins. Co.*, 257 Md. 168, 179, 262 A.2d 556, 562 (1970) (agent cannot enlarge actual authority without some measure of assent or acquiescence from principal whose rights and liabilities to third parties are not affected by any apparent authority agent has conferred on himself by his express or implied representations) (citation omitted).

³⁰ 389 A.2d at 394; *see also Green Leaves Restaurant, Inc. v. 617 H Street Associates*, 974 A.2d at 230 (apparent authority arises when principal places agent in position that causes third party to reasonably believe principal had consented to exercise of authority agent purports to hold).

³¹ 389 A.2d at 394.

³² *Id.* at 718; *see also Homa v. Friendly Mobile Manor, Inc.*, 612 A.2d at 363-64 (plaintiff presented no evidence of any contact with principal that would have established authorization for agent to act on principal's behalf or that would indicate any benefit to principal which received no fees); *First Union National Bank v. Brown*, 186 N.C. App. 519, 603 S.E. 2d 808, 815 (2004) (president of corporation had apparent authority to bind corporation to contracts that were within corporation's ordinary course of business) (citations omitted).

³³ *Integrated Consulting Services, Inc. v. LDDS Communications, Inc.*, 996 F. Supp. at 477.

³⁴ *Id.*

³⁵ *Id.* at 478. *See also Bullitt County Bank v. Publishers Printing Co., Inc.*, 684 S.W. 2d 289, 293 (Ky. 1985) (no apparent authority for check drawer because principals did not manifest any apparent authority).

³⁶ *Wailes & Edwards, Inc. v. Bach*, 265 Md. 274, 277-78 (1972) (citation omitted).

³⁷ *Derbia v. Access Wealth Management, LLC, et al.*, 2011 U.S. Dist. LEXIS 115992 (USDC NJ 2011).

³⁸ 928 F.2d 153, 157 (5th Cir. 1991).

³⁹ *Id.*; *see also Three Minnows, LLC v. Cream, LLC*, 2013 WL 1453246, at *5

(principal is liable under agency by estoppel if he causes third party to believe agent has authority to act or has notice that third party believes agent has authority to act and does nothing to notify third party about lack of authority).

⁴⁰ 928 F.2d at 157.

⁴¹ *Id.*

⁴² *The Johns Hopkins University v. Ritter*, 114 Md. App. 77, 689 A.2d 91, 96 (1997).

⁴³ *Id.*

⁴⁴ *Id.* at 101; *see also Integrated Consulting Services, Inc. v. LDDS Communications, Inc.*, 996 F. Supp. at 476 (denying estoppel claim because of insufficient evidence of reasonable reliance and holding that third party's reliance on principal's conduct is crucial factor in agency by estoppel).

⁴⁵ 180 Md. App. 535, 556 (2008).

⁴⁶ 265 Md. 274, 277-78 (1972).

⁴⁷ *Wood v. Walter*, 855 F. Supp. 2d 494, 503 (D. Md. 2012).

⁴⁸ *Id.* (citation omitted).

⁴⁹ *Integrated Consulting Services, Inc. v. LDDS Communications, Inc.*, 996 F. Supp. at 476.

⁵⁰ *Id.*; *see also Huppmann v. Tighe*, 100 Md. App. 655, 665, 642 A.2d 309 (1994) (authorities are crystal clear that party cannot be found to have ratified absent knowledge of material facts underlying transaction); *Frontier Leasing Corp. v. Links Engineering, LLC*, 781 N.W. 2d 772, 777 (Iowa 2010) (principal may be liable under ratification theory when he knowingly accepts benefits of transactions entered into by his agent).

⁵¹ *Bakery and Confectionery Union and Industry International Pension Fund v. New World Pasta Company*, 309 F. Supp.2d 716, 729 (D. Md. 2004); *see also Progressive Casualty Insurance Company v. Ehrhardt*, 518 A.2d at 156 (intent to ratify includes receipt and retention of benefits of unauthorized transaction).

⁵² 890 F.2s 456, 465 (U.S. App. D.C. 1990).

⁵³ *Id.*

⁵⁴ *Id.* (citation omitted).