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WORKING GROUP FOR THE PREPARATION OF
PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS

Chapter [...]

AUTHORITY OF AGENTS

(Revised draft prepared by Professor M.J. Bonell)

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Article 1
(Scope of the chapter)

(1) This chapter governs the authority of a person, the agent, to affect the legal relations of another person, the principal, by or with respect to a contract with a third party, whether the agent acts in its own name or in that of the principal.

(2) It governs only the relations between the principal or the agent on the one hand, and the third party on the other.

(3) It does not govern an agent's authority conferred by law or the authority of an agent appointed by a public or judicial authority.

COMMENT

1. Scope of the Chapter

The Chapter governs the authority of an agent to affect the legal relations between its principal and a third party. In other words it focuses on the external relations between the principal or the agent on the one hand and the third party on the other, and is not concerned with the internal relations between the principal and the agent. Even those provisions which deal with issues affecting both the internal and the external relations (see, e.g., Articles 2 and 10 on the establishment and termination of the agent's authority, Article 7 on conflict of interests and Article 8 on subagency), consider those issues only with respect to their effects on the third party.

The rights and duties as between principal and agent are governed by their agreement and the applicable law which, with respect to specific types of agency relationships such as those concerning so-called commercial agents, may provide mandatory rules for the protection of the agent.

2. Authority to contract

The Chapter deals only with agents having authority to conclude contracts on behalf of their principals. Intermediaries whose task it is merely to introduce two parties to one another with a view their concluding a contract (e.g. real estate agents) or to negotiate contracts on behalf of a principal but having no authority to bind the principal (as may be the case of so-called commercial agents) are outside the scope of the Chapter.

On the other hand, the wording "the authority [...] to affect the legal relations of [...] the principal by or with respect to a contract with a third party" used in paragraph 1 is to be understood in a broad sense so as to comprise any act by the agent for the purpose of concluding a contract or relating to its performance, including giving a notice to, or receiving it from, the third party.

3. Whether agent acts in its own name or in that of its principal irrelevant

Contrary to a number of legal systems which distinguish between “direct representation” and “indirect representation” depending on whether the agent acts in the principal’s name or in its own name, no such distinction is made in this Chapter. As to the distinction between “disclosed” and “undisclosed” agency see Articles 3 and 4.

4. Voluntary nature of the relationship between principal and agent

A further condition for the application of this Chapter is the voluntary nature of the relationship between principal and agent. Cases where the agent’s authority is conferred by law (e.g. in the field of family law, matrimonial property and succession) or arises from judicial authorisation (e.g. to act for a person without capacity to act) are outside the scope of this Chapter.

5. Agents of companies

The authority of organs, officers or partners of a corporation, partnership or other entity, whether or not possessing legal personality, is traditionally governed by special rules, sometimes even of a mandatory character, which by virtue of their specific scope necessarily prevail over the rules on the authority of agents in general as laid down in this Chapter. Thus, for instance, if under the special rules governing the authority of its organs or officers a corporation is prevented from invoking against third parties any limitation to their authority, that corporation may not rely on Article 5(1) of this Chapter to claim that it is not bound by an act of its organs or officers which falls outside the scope of their authority.

On the other hand, as long as the general rules laid down in this Chapter do not conflict with the above-mentioned special rules on the authority of organs, officers or partners, they may well be applied in lieu of the latter. Thus, for instance, a third party seeking to establish that the contract it has concluded with an officer of a corporation binds that corporation, may invoke either the special rules governing the authority of that corporation’s organs or officers or, as the case may be, the general rules on apparent authority as laid down in Article 5 (2) of this Chapter.

Illustrations

1. A, Chief Executive Officer of Ruritanian Company B, has under the company’s articles authority to carry out all transactions falling within the course of the company’s ordinary business. A enters into a contract with Third Party C which clearly falls outside the scope of B’s ordinary business. According to section 35A of the Ruritanian Companies Act “[i]n favour of a person dealing with a company in good faith, the power of the board of directors to bind the company, or authorise others to do so, shall be deemed to be free of any limitation under the company’s constitution” and “[...] a person shall not be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the company’s constitution

[...]”. B is bound by the contract between A and C even if C knew or ought to have known the limitations to A’s authority, and B may not rely on Article 5(1) of this Chapter to claim the contrary.

2. A, Managing Director of Ruritanian Company B, has been given by the Board of Directors the authority to carry out all transactions falling within the course of the company’s ordinary business except the hiring and dismissal of employees. A hires C as the new accountant of B’s branch in foreign country X. B refuses to be bound by this appointment on account of A’s lack of authority to hire employees. C may overcome B’s objection by invoking section 35A of the Ruritanian Companies Act. Yet C, who as a national of foreign country X may not be familiar with that special provision of the Ruritanian Companies Act, may equally rely on the general rule on apparent authority as laid down in Article 5(2) of this Chapter and claim that, in view of A’s position as Managing Director of B, it was reasonable for C to believe that A had the authority to hire employees.

Article 2

(Establishment and scope of the authority of the agent)

(1) The principal’s grant of authority to an agent may be express or implied.

(2) The agent has authority to perform all acts necessary in the circumstances to achieve the purposes for which the authority was granted.

COMMENT

1. Express or implied grant of authority

Paragraph 1 makes it clear that the granting of the agent’s authority by the principal is not subject to any particular requirements of form and that it may be either express or implied.

The most common case of an express authority is a power of attorney, but the principal may also confer the authority on the agent in an oral statement or written communication or, in the case of a corporate entity, in a resolution by its board of directors. The granting of an express authority in writing has the obvious advantage of providing clear evidence to all parties concerned (principal, agent and third parties) of the existence and precise scope of the agent’s authority.

An implied authority exists whenever the principal’s intention to confer the authority on an agent can be inferred from the terms of the express authority or the principal’s conduct (e.g. the conferment on the agent of a particular task) or other circumstances of the case (e.g. the terms of an express authority; a particular course of dealing between the two parties or a general trade usage).

Illustration

1. B appoints A as manager of B's apartment building. A has implied authority to conclude short term lease contracts relating to the individual apartments.

2. Scope of the authority

The broader the mandate conferred on the agent, the wider the scope of its authority. Accordingly, paragraph 2 makes it clear that the agent's authority, unless otherwise provided by the principal in its authorisation, is not limited to its express terms but extends to all acts necessary in the circumstances to achieve the purposes for which the authority was granted.

Illustration

2. Owner B consigns to Shipmaster A a cargo to be transported to Country X within 10 days. With 3 days of navigation remaining, the ship is damaged and must stop in the nearest port for repairs. A has implied authority to unload the cargo and consign it to another shipmaster to be transported to destination on another ship.

Article 3 (Agency disclosed)

(1) Where an agent acts within the scope of its authority and the third party knew or ought to have known that the agent was acting as an agent, the acts of the agent shall directly affect the legal relations between the principal and the third party and no legal relation is created between the agent and the third party.

(2) However, the acts of the agent shall affect only the relations between the agent and the third party, where the agent with the consent of the principal undertakes to become the party to the contract.

COMMENT

1. "Disclosed" agency

With respect to the effects of the acts of the agent, this Chapter distinguishes between two basic situations: one in which the agent acts on behalf of a principal within the scope of its authority and the third party knows or ought to know that the agent is acting as an agent, and another in which the agent acts on behalf of a principal within the scope of its authority but the third party neither knows nor ought to know that the agent is acting as an agent. The first situation, which is the normal one, may be referred to as "disclosed" agency and is dealt with in the present Article.

2. Agent's acts directly affecting legal relations between principal and third party

In the case of a “disclosed” agency, the rule is that the agent's acts directly affect the principal's legal position vis-à-vis the third party (paragraph 1). Thus a contract made by the agent directly binds the principal and the third party. Likewise any communication of intention the agent makes to, or receives from, the third party affects the principal's legal position as if the principal itself had made or received it.

Illustrations

1. A, Sales Representative for Computer Manufacturer B, accepts the order placed by University C for the purchase of a certain number of computers. The sales contract directly binds B vis-à-vis C with the result that it is B, and not A, who is under the obligation to deliver the goods to C and who is entitled to payment by C.
2. The facts are the same as in Illustration 1, the difference being that one of the computers delivered is defective. The notice of such defects given by C to A directly affects B.

3. Acting in the principal's name not necessary

For the establishment of a direct relationship between the principal and the third party it is sufficient that the agent acts within the scope of its authority and that the third party knows or ought to know that the latter acts on behalf of another person. By contrast, it is as a rule not necessary for the agent to act in the principal's name (see also Article 1, paragraph 1).

In practice however there might be cases where it is in the agent's own interest to indicate expressly the identity of the person on whose behalf it is acting. Thus, whenever the contract requires the parties' signature, the agent is well advised not simply to sign in its own name, but to add language such as “for and on behalf of (followed by the principal's name)”, so as to avoid any risk of being held personally liable under the contract.

Illustrations

3. The facts are the same as in Illustration 1. For the sales contract directly binding B vis-à-vis C it is irrelevant whether A, when accepting C's order over the telephone, acts in its own name or expressly states that it is accepting in the name of B.
4. Computer Specialist A is contacted by Research Center C with a view to creating a computer programme for a special database on international case law. A, when signing the contract in its capacity as employee of Software Company B, should expressly state that it is acting on behalf of B. If A merely signs the contract without indicating B, A may be held personally liable under the contract by C.

4. Agent undertaking to become party to the contract

An agent, though openly acting on behalf of a principal, may exceptionally become itself party to the contract with the third party (paragraph 2). This is the case, in particular, where the principal, who wants to remain anonymous, instructs the agent to act as a so-called commission agent, i.e. to deal with the third party in its own name without establishing any direct relation between the principal and the third party. This is also the case where the third party makes it clear that it does not intend to contract with anyone other than the agent and the agent, with the consent of the principal, agrees that it alone and not the principal will be bound by the contract. In both cases it will follow from the terms of the agreement between the principal and the agent that, once the agent has acquired its rights under the contract with the third party, it will have to transfer them to the principal.

Entirely different is the case where the agent steps in and decides to become party to the contract with the third party in violation of its agreement with the principal. In so doing the agent no longer acts as an agent, and therefore the case falls outside the scope of this Chapter.

Illustrations

5. Dealer B, expecting a substantial increase in the price of wheat, decides to purchase a large quantity of wheat. B, wishing to remain anonymous, entrusts Commission Agent A with this task. Even though Supplier C knows that A is purchasing on behalf of a principal, the purchase contract is binding on A and C and does not directly affect B's legal position.

6. Confirming House A, acting on behalf of Overseas Buyer B, places an order with Supplier C for the purchase of certain goods. Since C, who does not know B, insists on A's confirmation of B's order, A accepts to be held itself liable vis-à-vis C. Even though C knows that A is purchasing on behalf of B, the purchase contract is binding on A and C and does not directly affect B's legal position.

7. Dealer B instructs Agent A to purchase on its behalf a certain quantity of oil. When A is about to conclude the contract with Supplier C, the news arrives that the oil producing countries intend to reduce substantially their production. A, expecting a rise in oil prices, decides to purchase the oil for itself and enters into the contract with C as the only other party. In so doing A has ceased to act as agent for the principal and the consequences of its acts are no longer governed by this Chapter.

Article 4
(Agency undisclosed)

(1) Where an agent acts within the scope of its authority and the third party neither knew nor ought to have known that the agent was acting as an agent, the acts of the agent shall affect only the relations between the agent and the third party.

(2) However, where such an agent, when contracting with the third party on behalf of a business, represents itself to be the owner of that business, the third party, upon discovery of the real owner of the business, may exercise also against the latter the rights it has against the agent.

COMMENT

1. “Undisclosed” agency

This article deals with what may be referred to as “undisclosed” agency, i.e. the situation in which an agent acts on behalf of a principal within the scope of its authority but the third party neither knows nor ought to know that the agent is acting as an agent.

2. Agent’s acts directly affecting only the relations between agent and third party

Paragraph 1 provides that in the case of an “undisclosed” agency the agent’s acts affect only the relations between the agent and the third party and do not directly bind the principal vis-à-vis the third party.

Illustration

1. Art Dealer A, purchases a painting from Artist C. When entering into the contract A does not disclose the fact that it is acting on behalf of Client B, nor has C any reason to believe that A is not acting on its own behalf. The contract is binding on A and C only and does not give rise to a direct relationship between Client B and Artist C.

3. Third party’s right of action against principal

Notwithstanding the rule laid down in paragraph 1, the third party may exceptionally have a right of direct action also against the principal. More precisely, according to paragraph 2, if the third party believes that it is dealing with the owner of a business, while in fact it is dealing with the owner’s agent, it may, upon discovery of the real owner, exercise also against the latter the rights it has against the agent.

Illustration

2. Manufacturer A, after having transferred his assets to a newly formed company, continues to contract in his own name without disclosing to Supplier B that he is in fact acting only as the managing director of the company. Upon discovery of the existence of the company, Supplier B has a right of action also against the company.

Article 5

(Agent acting without or exceeding its authority)

(1) Where an agent acts without authority or exceeds its authority, its acts do not affect the legal relations between the principal and the third party.

(2) However, where the principal causes the third party reasonably and in good faith to believe that the agent has authority to act on behalf of the principal and that the agent is acting within the scope of that authority, the principal may not invoke against the third party the lack of authority of the agent.

COMMENTS

1. Lack of authority

Paragraph 1 expressly states that where an agent acts without authority, its acts do not bind the principal and the third party to each other. The same applies to the case where the agent has been granted authority of limited scope and acts exceeding its authority.

As to the liability of the false agent vis-à-vis the third party, see Article 6.

Illustration

1. Principal B authorises Agent A to buy on its behalf a specific quantity of grain with a price limit. A enters into a contract with Seller C for the purchase of a greater quantity of grain and at a higher price than authorised by B. On account of A's lack of authority, the contract between A and C does not bind B, nor does it become effective between A and C.

2. Apparent authority

There are two cases in which an agent, though acting without authority or exceeding its authority, may bind the principal vis-à-vis the third party.

The first case occurs whenever the principal ratifies the agent's act and is dealt with in Article 9.

The second case is that of so-called apparent authority and is dealt with in paragraph 2 of the present article. According to this provision a principal, whose conduct leads a third party reasonably to believe that the agent has authority to act on its behalf, is prevented from invoking against the third party the lack of authority of the agent and is therefore bound by the latter's act.

Apparent authority, which is an application of the general principle of good faith (see Article 1.7) and of the prohibition of *venire contra factum proprium* (see, e.g., Articles 2.4(2)(b), 2.18 and 3.12), is especially important where the principal is not an individual but an organisation. In dealing with a corporation, partnership or other business association a third party may find it difficult to determine whether the persons acting for the organisation have actual authority to do so and may therefore prefer, whenever possible, to rely on their apparent authority. For this purpose the third party only has to demonstrate it was reasonable for it to believe that the person purporting to represent the organisation was authorised to do so, and this belief was caused by the conduct of those actually authorised to represent the organisation (board of directors; executive officers; partners; etc.). Whether or not the third party's belief was reasonable will depend on the circumstances of the case (position occupied by the apparent agent in the organisation's hierarchy; type of transaction involved; acquiescence of the organisation's representatives in the past; etc.).

Illustrations

2. A, Manager of one of Company B's branch offices, though lacking actual authority to do so, engages Construction Company C to renovate the branch's premises. In view of the fact that a branch manager normally would have authority to enter into such a contract, B is bound by the contract with C since it was reasonable for C to believe that A had actual authority to enter into the contract.

3. A, Chief Financial Officer of Company B, though lacking actual authority to do so, with the acquiescence of the Board of Directors repeatedly entered on behalf of B into financial transactions with Bank C. On the occasion of a new transaction which proves to be disadvantageous to B, B's Board of Directors raises vis-à-vis C the objection of A's lack of authority. C may defeat this objection by claiming that B is bound by A's apparent authority to enter into the financial transaction for B.

Article 6

(Liability of agent acting without or exceeding its authority)

(1) An agent that acts without authority or exceeds its authority is, failing ratification by the principal, liable for damages that will put the third party in the same position as if the agent had acted with authority and not exceeded its authority.

(2) However, the agent is not liable if the third party knew or ought to have known that the agent had no authority or was exceeding its authority.

COMMENT

1. Liability of false agent

It is generally recognised that an agent acting without authority or exceeding its authority shall, failing ratification by the principal, be liable for damages to the third party. Paragraph 1, in stating that the false agent shall be liable to pay the third party such compensation as will place the third party in the same position as it would have been in if the agent had acted with authority, makes it clear that the liability of the false agent is not limited to the so-called reliance or negative interest, but extends to the so-called expectation or positive interest. In other words the third party may recover the profit which would have resulted if the contract concluded with the false agent had been a valid one.

Illustration

1. Agent A, without being authorised by Principal B, enters into a contract with Third Party C for the sale of a cargo of oil belonging to B. Failing B's ratification of the contract, C may recover from A the difference between the contract price and the current market price.

2. Third party's knowledge of agent's lack of authority

The false agent is liable to the third party only to the extent that the third party, when entering into the contract with the false agent, neither knew nor ought to have known that the latter was acting without authority or exceeding its authority.

Illustration

2. A, Junior Employee of Company B, without actual authority to do so, engages Construction Company C to renovate B's premises. B refuses to ratify the contract. Nevertheless C may not request damages from A since it should have known that an employee of A's rank normally has no authority to enter into such a contract.

Article 7
(*Conflict of interests*)

(1) If a contract concluded by an agent involves the agent in a conflict of interests with the principal of which the third party knew or ought to have known, the principal may

avoid the contract. The right to avoid is subject to Articles 3.12 and 3.14 to 3.17.

(2) However, the principal may not avoid the contract

(a) if the principal had consented to, or knew or ought to have known, the agent's involvement in the conflict of interests; or

(b) if the agent had disclosed the conflict of interests to the principal and it had not objected within a reasonable time.

COMMENT

1. Conflict of interests between agent and principal

It is inherent in any agency relationship that the agent, in fulfilling its mandate, shall act in the interest of the principal to the exclusion of its own interest or that of anyone else if they conflict with one another.

The most frequent cases of potential conflict of interests are those where the agent acts for two principals and those where the agent concludes the contract with itself or with a firm in which it has an interest. However in practice even in such cases a real conflict of interests may not exist. Thus, for instance, the agent's acting for two principals may be in conformity with the usages of the trade sector concerned, or the principal has conferred on the agent a mandate which is so stringent as to leave no margin for manoeuvre.

2. Conflict of interests as ground for avoidance of the contract

Paragraph 1 of this Article lays down the rule that a contract concluded by an agent acting in a situation of a real conflict of interests may be avoided by the principal provided that the third party knew or ought to have known of the conflict of interests.

The requirement of the constructive knowledge of the third party is intended to protect the innocent third party's interest in preserving the contract. This requirement is obviously no longer relevant where the agent concludes the contract with itself and therefore is at one and the same time agent and third party.

Illustrations

1. Solicitor A is requested by foreign Client B to purchase on its behalf an apartment in A's city. A buys the apartment Client C has requested A to sell on its behalf. B may avoid the contract if it can prove that C knew or ought to have known of A's conflict of interests. Likewise C may avoid the contract if it can prove that B knew or ought to have known of A's conflict of interests

2. Sales agent A, requested by Retailer B to purchase on its behalf certain goods, purchases the goods from Company C in which A is a majority

shareholder. B may avoid the contract if it can prove that C knew or ought to have known of A's conflict of interests.

3. Client B instructs Bank A to buy on its behalf one thousand shares of Company X at the closing price of the same day on the Stock Exchange of City Y. Even if A sells to B the requested shares from those it had in its own portfolio, there can be no conflict of interests because B's mandate leaves A no margin for manoeuvre.

4. A, Chief Executive Officer of Company B, has authority to appoint the company's counsel in the event of law suit brought by or against B. A appoints itself as B's counsel. B may avoid the contract.

3. Procedure for avoidance

As to the procedure for avoidance, the provisions laid down in Articles 3.12 (*Confirmation*), 3.14 (*Notice of avoidance*), 3.15 (*Time limits*), 3.16 (*Partial avoidance*) and 3.17 (*Retroactive effect of avoidance*) apply.

4. Avoidance excluded

According to paragraph 2 the principal loses its right to avoid the contract if it had agreed beforehand, or at any rate knew or ought to have known, that the agent would act in a situation of conflict of interests. The right of avoidance is likewise excluded if the principal, having been informed by the agent of the contract it had concluded in a conflict of interests, raises no objection.

Illustration

5. The facts are the same as in Illustration 1, the difference being that before concluding the contract A duly informs B that it is acting as agent also for C. If B does not object B loses its right to avoid the contract. Likewise if A duly informs C that it is acting as agent also for B and C does not object, C loses its right to avoid the contract.

5. Issues not covered by the present article

In conformity with the scope of this Chapter as set out in Article 1, the present article addresses only the impact the agent's involvement in a conflict of interests may have on the external relationship. Issues such as the agent's duty of full disclosure vis-à-vis the principal and the principal's right to damages from the agent may be settled on the basis of other provisions of these Principles (cf. Articles 1.7, 3.18, 7.4.1 *et seq.*) or otherwise are governed by the law applicable to the internal relationship between principal and agent.

Article 8
(*Subagency*)

An agent has implied authority to appoint a subagent to perform acts which it is not reasonable to expect the agent to perform itself. The rules of this chapter apply to the subagency.

COMMENTS

1. Role of subagents

In carrying out the mandate conferred on it by the principal, an agent may find it convenient or even necessary to avail itself of the services of other persons. This is the case for instance where certain tasks are to be performed in a place distant from the agent's place of business, or at any rate a more efficient performance of the agent's mandate requires distribution of work.

2. Implied authority to appoint subagents

Whether or not the agent is authorised to appoint one or more subagents depends on the terms of the authority granted by the principal. Thus the principal may expressly exclude the appointment of subagents or make it conditional upon its prior approval. If nothing is said in the authorisation as to the possibility of appointing subagents and the terms of the authority are not otherwise inconsistent with such possibility, the agent has the right under this article to appoint subagents. The only limitation is that the agent may not entrust the subagent(s) with tasks which it is reasonable to expect the agent itself to perform. This is the case in particular of acts requiring the agent's personal expertise.

Illustrations

1. Chinese Museum B instructs a London based Art Dealer A to buy a particular piece of Greek pottery on sale at a private auction in Germany. A has implied authority to appoint German subagent S to purchase that piece of pottery at the auction in Germany and to send it with insurance coverage to B.
2. The facts are the same as in Illustration 1, the difference being that B does not specify the particular piece of Greek pottery to be acquired at the auction in Germany as it relies on A's expertise to choose the most suitable item offered for sale. A itself is expected to make the purchase at the auction, but once it has purchased the piece of pottery, it may appoint subagent S to send it with insurance coverage to B.

3. Effects of a subagent's acts

The present Article expressly states that the rules of this Chapter apply to the subagency. In other words the acts of a subagent legitimately appointed by the agent bind the principal and the third party directly to each other, provided that those acts are both within the agent's authority and the authority conferred on the subagent by the agent which may be more limited.

Illustration

3. The facts are the same as in Illustration 1. The purchase of the piece of Greek pottery by S directly binds B provided that it is within both the authority which B has granted to A and the authority which A has granted to S.

Article 9 (*Ratification*)

(1) An act by an agent that acts without authority or exceeds its authority may be ratified by the principal. On ratification the act produces the same effects as if it had initially been carried out with authority.

(2) The third party may by notice to the principal specify a reasonable period of time for ratification. If the principal does not ratify within that period it can no longer do so.

[(3) Where, at the time of the agent's act, the third party neither knew nor ought to have known of the lack of authority, it may, at any time before ratification, by notice to the principal indicate its refusal to become bound by a ratification.] (*)

COMMENT

1. Notion of ratification

This article lays down the generally accepted principle whereby acts carried out by an agent holding itself out to have authority but actually without authority or exceeding its authority, and which therefore have no effect on the principal, may be authorised by the principal at a later stage. Such subsequent authorisation is known as ratification.

Like the original authorisation, ratification is not subject to any requirements as to form. Being a unilateral manifestation of intent, it may either be express or implied from words or conduct and, though normally communicated to the agent, to

the third party, or to both, it need not be communicated to anybody provided that it is manifested in some way and can therefore be ascertained by probative material.

Illustration

Agent A purchases on behalf of Principal B goods from Third Party C at a price higher than authorised by B. Upon receipt of C's bill, B makes no objection and pays it by bank transfer. The payment amounts to ratification of A's act even if B does not expressly declare its intention to ratify, fails to inform both A and C of the payment and C is only subsequently informed of the payment by its bank.

2. Effects of ratification

On ratification the agent's acts produce the same effect as if they had been carried out from the outset with authority (paragraph 1). It follows that the third party may refuse partial ratification as it amounts to a proposal by the principal to modify the contract the third party has concluded with the agent. [On its part the principal may no longer revoke ratification after it was brought to the attention of the third party. Otherwise the principal would be in a position to unilaterally withdraw from the contract with the third party.]

3. Time of ratification

The principal may in principle ratify at any time. The reason for this is that normally the third party does not even know that it had contracted with an agent without authority or exceeding its authority. Only if the third party knows from the outset or becomes aware subsequently that the agent was a false agent it has a legitimate interest not to be left in doubt indefinitely as to the ultimate fate of the contract with the false agent. Accordingly paragraph 2 grants the third party the right to set a reasonable time limit within which the principal must ratify if it intends to do so. It goes without saying that in such a case ratification has to be notified to the third party.

4. Third persons' rights not affected

This article deals only with the effects of ratification on the three parties directly involved in the agency relationship, i.e. the principal, the agent and the third party. In accordance with the scope of this Chapter as defined in Article 1 the rights of other third persons are not affected. For instance, if the same goods have been sold first by the false agent to C and subsequently by the principal to another person D, the conflict between C and D as a result of the principal's later ratification of the first sale will have to be solved by the applicable law.

(*) *Reporter's Note*

The preliminary draft discussed by the Working Group at its 2nd session in 1999 contained, instead of the present paragraph 2, two paragraphs which had been taken literally from Article 15 of the Geneva Convention and which read as follows:

“(2) Where, at the time of the agent’s act, the third party neither knew nor ought to have known of the lack of authority, the latter shall not be liable to the principal if at any time before ratification it gives notice of its refusal to become bound by a ratification. Where the principal ratifies but does not do so within a reasonable time, the third party may refuse to be bound by the ratification if it promptly notifies the principal.

(3) Where, however, the third party knew or ought to have known of the lack of authority of the agent, the third party may not refuse to become bound by a ratification before the expiration of any time agreed for ratification or, failing agreement, such reasonable time as the third party may specify.”

The two paragraphs addressed two basically different issues: the protection of the innocent third party (paragraph 2 first sentence) and the time limits for ratification irrespective of whether or not the third party knew or ought to have known of the agent’s lack of authority (paragraph 2 second sentence and paragraph 3).

When discussing the two paragraphs the Group had focussed mainly on the question of time limits (see Report on the 1999 session: paras. 201-208) and decided by a majority of 7:5 to delete paragraphs 2 and 3 of the draft and to add the present paragraph 2. Yet in so doing the question of the protection of the innocent third party was no longer addressed.

*The Group might wish to reconsider its decision and adopt a new paragraph 3 along the lines suggested in the above text in square brackets. By granting the innocent third party the possibility of preventing the principal from ratifying the act of the false agent the principal would no longer be the sole party in a position to speculate on the market and make its decision to ratify or not dependent on whether or not market developments are to its advantage or disadvantage. The proposed solution has been adopted in domestic laws: see, for further references H. KÖTZ, *European Contract Law* (1997), p.234; § 4.05 of the *Draft Restatement 3rd on Agency*; even with respect to English law, traditionally opposed to the idea of the third party being entitled to withdraw from the contract, doubts as to the appropriateness of such a solution have recently be expressed, see BOWSTEAD AND REYNOLDS ON AGENCY, 17th ed. (2001), p. 77.*

Article 10
(Termination of authority)

(1) Termination of authority is not effective in relation to the third party unless the third party knew or ought to have known of it.

(2) Notwithstanding the termination of its authority, an agent remains authorized to perform the acts that are necessary to prevent harm to the principal's interests.

COMMENT

1. Grounds for termination not covered by the present article

There are several grounds on which the agent's authority may be terminated: revocation by the principal, renunciation by the agent, completion of the act(s) for which authority had been granted, loss of capacity, bankruptcy, death or cessation of existence of the principal or the agent, etc. What exactly constitutes a ground for termination and the way it operates as between the principal and the agent falls outside the scope of the present article and is to be determined in accordance with the applicable laws (e.g. the law governing the internal relations between principal and agent; the law governing their legal status or personality; the law governing bankruptcy; etc.) which may vary considerably from one country to another.

2. Termination effective vis-à-vis the third party

Whatever the grounds for termination of the agent's authority, in relation to the third party termination is not effective unless the third party knew or ought to have known of it (paragraph 1). In other words, even if the agent's authority has been terminated for one reason or another, the agent's acts continue to affect the legal relationship between the principal and the third party as long as the third party is unaware of nor ought to know that the agent no longer has authority.

Obviously the situation is clear whenever the principal or the agent gives notice to the third party of the termination. In the absence of such notice it will depend on the circumstances of the case whether the third party ought to have known of the termination.

Illustrations

1. Principal B opens a branch office in City X. An advertisement published in the local newspaper indicates Managing Director A as having full authority to act on behalf of B. When B subsequently revokes A's authority, a similar notice thereof in the same newspaper is sufficient to make termination effective vis-à-vis B's customers in City X.

2. Retailer C has repeatedly placed orders with Sales Representative A for the purchase of goods sold by Principal B. A continues to accept orders from C

even after its authority had been terminated on account of B's bankruptcy. The mere fact that the bankruptcy proceeding was given the publicity required by the applicable law is not sufficient to make termination effective vis-à-vis C.

3. Authority of necessity

Even after termination of the agent's authority the circumstances of the case may make it necessary for the agent to perform additional acts in order to prevent the principal's interests from being harmed.

Illustration

3. Agent A had authority to purchase a certain quantity of perishable goods on behalf of Principal B. After the purchase of the goods A is informed of B's death. Notwithstanding the termination of its authority A continues to be authorised either to resell the goods or to store them in a suitable warehouse.

[4. Modification of authority also covered

The rules of this article apply not only to termination but, with appropriate modifications, also to subsequent restrictions to an agent's authority.]