

Letters of Intent

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What is a letter of intent (“LOI”)

There are different names, but they mean the same thing:

Memorandum of Understanding (MOU)

Gentleman’s Agreement

Agreement in Principle

Term Sheet

What is an LOI?

It depends on what you intend.

The most common understanding—a nonbinding listing of preliminary deal points to establish the outlines of a final agreement.

Purposes of an LOI

1. Provide a skeleton for a final agreement.
2. Identifies what's been agreed to and what's still open.
3. Forces parties to consider the deal and identify fatal flaws.
4. Announces to 3rd parties (such as lenders) that a deal is pending.

Types of LOIs

1. Nonbinding
2. Binding
3. Partially binding.

Nonbinding LOI

What can go wrong

(how what someone thought was a nonbinding LOI can be interpreted to be binding)

Nonbinding LOI

What's required to make a document a binding agreement?

1. Identity of the parties.
2. Key terms are stated (or can be implied)--
Such terms include price and duration.

Nonbinding LOI—What can go wrong

1. The language of the LOI suggests the parties intended that there be binding agreement.

Examples:

“Please indicate your acceptance on the enclosed copy of this letter and return it to us.”

“The parties will execute a definitive lease in the usual standard form of business lease in this community.”

Nonbinding LOI—What can go wrong

Examples (cont.)

“Please acknowledge your intent to proceed with the leasing of the captioned store under the above terms, conditions, and understandings by signing the enclosed copy of this letter and returning it within 10 days from the date hereof.”

“This letter is intended to set forth the terms upon which we and our nominee intend to negotiate and consummate an agreement.”

Nonbinding LOI—What can go wrong

2. The behavior of the parties can be used as evidence of intent that the LOI is binding.

Examples:

Press releases (see Pennzoil case).

“Signing ceremony” statements.

Nonbinding LOI—What can go wrong (with apologies to Gary Larson)

What a lawyer says to John, from the senior staff:

“John, I think this can be very dangerous. Under no circumstances, John, should there be a press conference. Make sure, John, that any public statements are reviewed by Legal...” etc., etc.

What the client John actually hears:

“**John**, (blah, blah, blah, blah). (Blah blah blah blah blah blah blah), **John**, (blah blah blah blah blah blah). (Blah blah blah), **John**, (blah blah blah blah)...” etc. etc.

Nonbinding LOI—What can go wrong

(behavior evidencing intent to be bound, cont.)

Handing over the keys to the property after LOI signed.

General behavior suggesting the deal is done.

Nonbinding LOI—What can go wrong

3. The language might suggest the parties must negotiate in good faith.

Why is this bad?

If you intend for this to be nonbinding, it opens the door to arguments that you failed to act in good faith if the deal falls through.

Nonbinding LOI—What can go wrong

4. One side acts in reliance on the LOI and creates the argument for a claim of detrimental reliance.

Technically, this means that if a party claims the LOI is unenforceable because there was no consideration, that defense can be defeated through a showing of detrimental reliance.

Drafting a nonbinding LOI

1. Have a strong statement that the LOI is nonbinding.

“This LOI is only a proposal that may or may not become part of a final agreement. The parties acknowledge that there is currently no agreement between them and no agreement will be in effect until both parties agree to and execute a subsequent contract. This LOI does not impose any obligation on either party to negotiate in good faith. The parties may not rely on any promises or statements made outside this LOI or actions that are inconsistent with this paragraph. This paragraph supersedes all other conflicting language. The parties may withdraw from further negotiations at any time and for any reason. Each party is responsible for any costs it may incur arising out of the subject matter of this LOI.”

Drafting a nonbinding LOI

1. State that the parties can withdraw at any time from negotiations.
2. Never use language that suggests the LOI is a formal contract—avoid using “contract,” “agreement,” or “lease” to describe the document.

Drafting a nonbinding LOI

3. Never use terms such as “good faith” or “best efforts.”
4. Avoid putting in items such as non-refundable fees—this might be considered consideration and add to the argument that the LOI is binding.

Drafting a nonbinding LOI

5. State that each party is responsible for any fees they incur arising out of the subject matter of the LOI.
6. Avoid public signing ceremonies or anything which suggests a deal has been reached.
7. Do not issue press releases or allow statements by your client that suggest a “deal” has been completed.

Drafting a nonbinding LOI

8. Be careful how you act after LOI is signed—don't behave as if there is a deal in place.

Partially binding LOIs

There are good reasons that you might want some portions of the LOI to be enforceable:

1. Access to the property and business records.
2. Provide for enforceable indemnities as necessary.

Partially binding LOIs

3. Enforce confidentiality of information provided to the other side.
4. “Lock-up” promises—prevent the other side from shopping your proposals to others.
5. Identify brokers and who pays commissions.

Partially binding LOIs

6. Provide for a defined period of exclusive negotiations.
7. Conditions surrounding press releases and publicity.

Partially binding LOIs

When preparing a partially binding LOI, it's important to keep the binding and nonbinding portions separate.

When citing consideration for the binding portions, make clear what the consideration is for.

Sample language comparison

- Dear PPT:
 -
 - Re: Proposed One-Year Lease Agreement between the Port of Pâté (“the Port) and PPT, LLC (“Lessee”) for Terminals Y and Z
 -
 - The purpose of this non-binding letter of intent (“Letter of Intent”) is to set forth the basic terms and conditions upon which Lessee and the Port propose to negotiate and enter into a proposed one-year lease (“Lease”) for the Premises described below.
- Dear PPT:
 -
 - Re: Proposed One-Year Lease Agreement between the Port of Pâté (“the Port) and PPT, LLC (“Lessee”) for Terminals Y and Z
 -
 - The purpose of this non-binding letter of intent (“Letter of Intent”) is to set forth the basic terms and conditions upon which Lessee and the Port propose to negotiate and enter into a proposed one-year lease (“Lease”) for the Premises described below.

Sample language comparison

The Port and Lessee have agreed that the proposed Lease is an interim one-year agreement commencing effective _____, 2013, upon termination of the existing lease (dated April 10, 2008). This proposed Lease will give Lessee and the Port additional time to discuss and finalize the terms of a new long-term agreement.

The Port and Lessee have discussed but not agreed to ~~that the~~ a proposed Lease ~~is an~~ for an interim one-year ~~agreement~~ term commencing effective _____, 2013, upon termination of the existing lease (dated April 10, 2008). This proposed Lease will give Lessee and the Port additional time to discuss and finalize the terms of a new long-term agreement.

Sample language comparison

Acceptance of Premises:

Lessee accepts the Premises in its present “as-is” condition.

Acceptance of Premises:

Lessee would accepts the Premises in its present “as-is” condition.

Sample language comparison

Use of Premises: Lessee will use the Premises for receiving and dispatching empty cargo containers and truck chassis; storage, repair, leasing, and sale of cargo containers and chassis; and activities related to this business operation.

Use of Premises: Lessee ~~will~~ would use the Premises for receiving and dispatching empty cargo containers and truck chassis; storage, repair, leasing, and sale of cargo containers and chassis; and activities related to this business operation.

Sample language comparison

Lease Term: The Lease will be for an initial term of one (1) year beginning April 1, 2013 and ending on March 31, 2014, or upon execution of a new long-term agreement.

Lease Term: The Lease ~~will~~ would be for an initial term of one (1) year beginning April 1, 2013 and ending on March 31, 2014, or upon execution of a new long-term agreement.

Sample language comparison

Base Rent: In consideration of the parties negotiating in good faith for a new long-term agreement, the base rent will be as follows:

Base Rent: ~~In consideration of~~ ~~the~~ ~~parties negotiating in good faith~~ propose to negotiate for a new long-term agreement, ~~for which~~ and the base rent ~~will~~ in a final agreement would be as follows:

Sample language comparison

Utilities: Lessee shall be responsible for timely payment of all utility fees, charges, and assessments for all utility services provided to the Premises.

Utilities: Lessee ~~shall~~ would be responsible for timely payment of all utility fees, charges, and assessments for all utility services provided to the Premises.

Sample language comparison

Maintenance and Repair: The Premises, together with all alterations or improvements, equipment and installations therein and the appurtenances thereto, shall be put and kept in good order, maintenance and repair by Lessee at Lessee's sole cost and expense, and, subject to provisions in the Lease regarding capital improvements, casualty and condemnation, Lessee shall undertake all maintenance and make all repairs and replacements, ordinary, as well as extraordinary, foreseen and unforeseen, structural or otherwise, which may be necessary or required so that at all times the Premises and all Improvements, equipment, installations and appurtenances shall be in good order, condition and repair.

Maintenance and Repair: The Premises, together with all alterations or improvements, equipment and installations therein and the appurtenances thereto, ~~shall~~ would be put and kept in good order, maintenance and repair by Lessee at Lessee's sole cost and expense, and, subject to provisions in the Lease regarding capital improvements, casualty and condemnation, Lessee ~~shall~~ would undertake all maintenance and make all repairs and replacements, ordinary, as well as extraordinary, foreseen and unforeseen, structural or otherwise, which may be necessary or required so that at all times the Premises and all Improvements, equipment, installations and appurtenances shall be in good order, condition and repair.

Sample language comparison

- **Insurance**: Lessee shall maintain the following insurance:
 - General Liability: \$2 Million – Port as Additional Insured
 - Automobile Liability: \$2 Million – Port as Additional Insured
- **Insurance**: Lessee ~~shall~~ would maintain the following insurance:
 - General Liability: \$2 Million – Port as Additional Insured
 - Automobile Liability: \$2 Million – Port as Additional Insured

Sample language comparison

Assignment: Lessee shall not have the right to assign or sublet the Premises in whole or in part, without the prior written consent of the Port, which consent shall not be unreasonably withheld, conditioned or delayed.

Assignment: Lessee ~~shall~~ would not have the right to assign or sublet the Premises in whole or in part, without the prior written consent of the Port, which consent shall not be unreasonably withheld, conditioned or delayed.

Questions?