CONFIDENTIALITY AGREEMENTS AND LETTERS OF INTENT

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NOTE:

AS A BASIS FOR SOME OF THE MATERIALS IN THE APPENDICES INCLUDED HEREIN, THE AUTHOR HAS UTILIZED PORTIONS OF A PRE-PUBLICATION DRAFT OF THE MODEL ASSET PURCHASE AGREEMENT WITH COMMENTARY PREPARED PRIOR TO 2001 BY THE ASSET ACQUISITION AGREEMENT TASK FORCE OF THE MERGERS & ACQUISITIONS COMMITTEE OF THE AMERICAN BAR ASSOCIATION, TOGETHER WITH CERTAIN OTHER MATERIALS PREPARED FOR COMMITTEE PROGRAMS. THE MODEL ASSET PURCHASE AGREEMENT, AS FIRST PUBLISHED BY THE AMERICAN BAR ASSOCIATION, DIFFERS IN A NUMBER OF RESPECTS FROM THE DRAFT ON WHICH THESE MATERIALS WERE BASED. FURTHER, AS THE AUTHOR HAS UPDATED THESE MATERIALS TO REFLECT CASES, LEGISLATION, MARKET CHANGES AND OTHER DEVELOPMENTS SUBSEQUENT TO THE PUBLICATION OF THE MODEL ASSET PURCHASE AGREEMENT, THE DIVERGENCE OF THESE MATERIALS FROM THE MODEL ASSET PURCHASE AGREEMENT HAS INCREASED. THE AUTHOR EXPRESSES APPRECIATION TO THE MANY MEMBERS OF THE MERGERS & ACQUISITIONS COMMITTEE WHOSE CONTRIBUTIONS HAVE MADE THESE MATERIALS POSSIBLE. THESE MATERIALS, HOWEVER, ARE SOLELY THE RESPONSIBILITY OF THE AUTHOR AND HAVE NOT BEEN REVIEWED OR APPROVED BY THE MERGERS & ACQUISITIONS COMMITTEE.

CONFIDENTIALITY AGREEMENTS AND LETTERS OF INTENT

By

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I. CONFIDENTIALITY AGREEMENT

A confidentiality agreement (***"Confidentiality Agreement"***), also sometimes called a non-disclosure agreement (***"NDA"***), is typically the first stage for the due diligence process as parties generally are reluctant to provide confidential information to the other side without having the protection of a confidentiality agreement.[1] The target typically proposes its form of confidentiality agreement, and a negotiation of the confidentiality agreement ensues.[2] A seller's form of confidentiality agreement is attached as **Appendix A**.[3]

A. NDA As Effective Standstill Agreement. In *Martin Marietta Materials, Inc. v. Vulcan Materials Co.*,[4] the Delaware Supreme Court upheld a pair of confidentiality agreements and temporarily enjoined Martin Marietta Materials from prosecuting a proxy contest and proceeding with a hostile bid for its industry rival Vulcan Materials Company. After years of

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Further information relevant to the topics discussed herein can be found in Byron F. Egan, EGAN ON ENTITIES: *Corporations, Partnerships and Limited Liability Companies in Texas* available on Amazon.com. You can CLICK HERE to purchase EGAN ON ENTITIES.

1 Byron F. Egan, *Confidentiality Agreements Are Contracts With Long Teeth*, 46 Tex. J. Bus. Law 1 (Fall 2014).

2 Some confidentiality agreements contain covenants restricting activities of the buyer after receipt of confidential information. *See, e.g., Goodrich Capital, LLC and Windsor Sheffield & Co., Inc. v. Vector Capital Corporation*, 11 Civ. 9247 (JSR), 2012 U.S. Dist. Lexis 92242, at *2 (S.D.N.Y. June 26, 2012) (NDA required use of confidential information solely to explore the contemplated business arrangement and not to minimize broker's role or avoid payment of its fees; a prospective bidder used information provided about other comparable companies to acquire one of the other companies; broker's lawsuit against that prospective bidder for breach of contract for misusing confidential information survived motion to dismiss); *In re Del Monte Foods Company Shareholders Litigation*, 25 A.3d 813 (Del. Ch. 2011) (NDA restricted bidders from entering into discussions or arrangements with other potential bidders; in temporarily enjoining stockholder vote on merger because target was unduly manipulated by its financial adviser, Delaware Vice Chancellor Laster faulted bidders' violation of the "no teaming" provision in the confidentiality agreement and the target's Board for allowing them to do so); *see* discussion of *Del Monte* case in Byron F. Egan, *How Recent Fiduciary Duty Cases Affect Advice to Directors and Officers of Delaware and Texas Corporations*, pp. 289-297 (Feb. 13, 2015), http://www.jw.com/publications/article/2033.

3 *See* **Appendix B**, *infra*. *See also* Article 12 of the ABA Model Asset Purchase Agreement and the Model Confidentiality Agreement accompanying the ABA Model Public Company Merger Agreement.

4 68 A.3d 1208, 1212 (Del. 2012), affirming *Martin Marietta Materials, Inc. v. Vulcan Materials Co.*, 56 A.3d 1072 (Del. Ch. 2012). *See* XVII Deal Points (The Newsletter of the Mergers and Acquisitions Committee of the ABA Bus. L. Sec.) at 23-26 (Summer 2012).

communications regarding interest in a friendly transaction, Vulcan and Martin Marietta in the spring of 2010 executed two confidentiality agreements to enable their merger and antitrust discussions, each governed by Delaware law:

- A general non-disclosure agreement requiring each party to use the other's confidential information "solely for the purpose of evaluating a Transaction," which was defined as "a possible business combination transaction . . . between" the two companies, and prohibiting disclosure of the other party's evaluation material and of the parties' negotiations except as provided in the agreement, which had a term of two years.

- A joint defense and confidentiality agreement, intended to facilitate antitrust review signed about two weeks after the non-disclosure agreement requiring each party to use the other's confidential information "solely for the purposes of pursuing and completing the Transaction," which was defined as "a potential transaction being discussed by" the parties, and restricting disclosure of confidential materials.

Neither agreement contained an express standstill provision. When the agreements were signed, both parties were seeking to avoid being the target of an unsolicited offer by the other or by another buyer. Accordingly, the agreements protected from disclosure the companies' confidential information as well as the fact that the parties had merger discussions.

After negotiations for a consensual transaction had floundered and Martin Marietta's economic position had improved relative to Vulcan, Martin Marietta decided to make a hostile bid for Vulcan and also launched a proxy contest designed to make Vulcan more receptive to its offer. The Court found that Martin Marietta used protected confidential material in making and launching its hostile bid and proxy contest.

The Court then construed the language of the confidentiality agreements to determine that Martin Marietta had breached those agreements by (1) using protected information in formulating a hostile bid, since the information was only to be used in an agreed-to business combination; (2) selectively disclosing protected information in one-sided securities filings related to its hostile bid, when such information was not disclosed in response to a third-party demand and when Martin Marietta failed to comply with the agreements' notice and consent process; and (3) disclosing protected information in non-SEC communications in an effort to "sell" its hostile bid. The Court emphasized that its decision was based entirely on contract law, and its reasoning did not rely on any fiduciary principles.

The Court held that, although the confidentiality agreements did not expressly include a standstill provision, Martin Marietta's breaches entitled Vulcan to specific performance of the agreements and an injunction. The Court therefore enjoined Martin Marietta, for four months, from prosecuting a proxy contest, making an exchange or tender offer, or otherwise taking steps to acquire control of Vulcan's shares or assets.

B. <u>"Don't Ask, Don't Waive" Provisions</u>. Some NDAs do contain express standstill provisions that (i) prohibit the bidder from making an offer for the target without an express invitation from its board of directors (***"Board"***) and (ii) preclude the bidder from publicly or

privately asking the Board to waive the restriction.[5] Such provisions in NDAs, which are sometimes referred to as "Don't Ask, Don't Waive" provisions, are designed to extract the highest possible offer from the bidder because the bidder only has one opportunity to make an offer for the target unless the target invites the bidder to make another offer *sua sponte*.[6] Bidders who do not execute NDAs with "Don't Ask, Don't Waive" provisions generally are not precluded from submitting multiple offers for the company, even after a winning bidder emerges from an auction.[7]

The legitimacy of "Don't Ask, Don't Waive" provisions was recognized in *In re Topps Co. Shareholders Litigation*,[8] in which then Vice Chancellor (now Chief Justice) Strine enjoined a stockholder vote on a merger until the target waived a standstill agreement. The target's Board had refused to waive the standstill in order to permit a strategic rival to make a tender offer on the same terms it had proposed to the Board and to communicate with Topps stockholders in connection with the vote on the proposed transaction the Board had approved with a private equity investor. In holding that the Board was misusing the standstill agreement solely in order to deny its stockholders the opportunity to accept an arguably more attractive deal and to preclude them from receiving additional information about rival's version of events, the Court wrote that standstill agreements can have legitimate purposes, including in the final round of an auction where a Board in good faith seeks to extract the last dollar from the remaining bidders, but can be subject to abuse:

> Standstills serve legitimate purposes. When a corporation is running a sale process, it is responsible, if not mandated, for the board to ensure that confidential information is not misused by bidders and advisors whose interests are not aligned with the corporation, to establish rules of the game that promote an orderly auction, and to give the corporation leverage to extract concessions from the parties who seek to make a bid.
>
> But standstills are also subject to abuse. Parties like Eisner often, as was done here, insist on a standstill as a deal protection. Furthermore, a standstill can be used by a target improperly to favor one bidder over another, not for reasons consistent with stockholder interest, but because managers prefer one bidder for their own motives.[9]

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5 Peter J. Walsh, Jr., Janine M. Salomone and David B. DiDonato, *"Don't Ask, Don't Waive" Standstill Provisions: Impermissible Limitation on Director Fiduciary Obligations or Legitimate, Value-Maximizing Tool?*, ABA Business Law Section, Business Law Today (January 23, 2013), http://apps.americanbar.org/buslaw/blt/content/2013/01/delawareinsider.shtml.

6 *Id.*

7 *Id.*

8 *In re Topps Company Shareholders Litigation*, 926 A.2d 58, 94-95 (Del. Ch. 2007); *see also* Byron F. Egan, *How Recent Fiduciary Duty Cases Affect Advice to Directors and Officers of Delaware and Texas Corporations*, University of Texas School of Law 37th Annual Conference on Securities Regulation and Business Law, Dallas, TX, Feb. 13, 2015, 277-282, http://www.jw.com/publications/article/2033.

9 926 A.2d at 91 (Del. Ch. 2007).

Subsequent Delaware Chancery Court decisions show that "Don't Ask, Don't Waive" provisions are subject to judicial scrutiny which can change the course of a transaction.[10]

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[10] *In re Celera Corp. Shareholder Litigation*, C.A. No. 6304-VCP, 2012 Del. Ch. Lexis 66, at *79 (Del. Ch. Mar. 23, 2012) (Transcript), *aff'd in part rev'd in part on other grounds*, 59 A.3d 418 (Del. Dec. 27, 2012), Vice Chancellor Parsons held that although in isolation the "Don't Ask, Don't Waive" provisions arguably fostered the legitimate objectives set forth in *Topps*, when viewed with the no-solicitation provision in the merger agreement, a colorable argument existed that the collective effect created an informational vacuum, increased the risk that directors would lack adequate information, and constituted a breach of fiduciary duty. The Court commented that the "Don't Ask, Don't Waive" standstill provisions blocked certain bidders from notifying the Board of their willingness to bid, while the no-solicitation provision in the merger agreement contemporaneously blocked the Board from inquiring further into those parties' interests, and, thus, diminished the benefits of the Board's fiduciary-out in the no-solicitation provision and created the possibility that the Board would lack the information necessary to determine whether continued compliance with the merger agreement would violate its fiduciary duty to consider superior offers.

In late 2012, two Chancery Court opinions, *In re Complete Genomics, Inc. S'holder Litig.*, C.A. No. 7888-VCL (Del. Ch. Nov. 27, 2012) (Telephonic Oral Argument and the Court's Ruling), and *In re Ancestry.com Inc. S'holder Litig.*, C.A. No. 7988-CS (Del. Ch. Dec. 17, 2012) (The Court's Ruling on Plaintiffs' Motion for Preliminary Injunction), considered the propriety of a target company's inclusion in standstill agreements of a "Don't Ask, Don't Waive" provision which became the "emerging issue of December of 2012," in the words of Chancellor Strine. In *Complete Genomics* the Board of a company in financial straits decided to explore "all potential strategic alternatives," including initiation of a process to find a buyer. Prospective bidders were required to sign confidentiality agreements, some of which included standstill provisions that prohibited the bidders from launching a hostile takeover and prohibited the prospective bidders from *publicly* asking the Board to waive the standstill restrictions, but one also forbade the prospective bidder from making a *nonpublic* request for such a waiver. *See* Robert S. Reder, *Delaware Chancellor Weighs in on "Don't Ask, Don't Waive" Provision of Standstill Agreement*, Bloomberg BNA Corporate Practice Library, 28 CCW 24 (2013). In a bench ruling, Vice Chancellor Laster analogized the "Don't Ask, Don't Waive" provision (at least insofar as it prohibited *nonpublic* waiver requests) to "bidder-specific no-talk" clauses criticized by the Court of Chancery in previous cases as being violative of the Board's "duty to take care to be informed of all material information reasonably available," rendering it the "legal equivalent of willful blindness" to its fiduciary duties. The Vice Chancellor wrote:

> In my view, a Don't Ask, Don't Waive Standstill resembles a bidder-specific no-talk clause. *In Phelps Dodge Corporation v. Cyprus Amax* [C.A. No. 17398, 1999 WL 1054255, at *2 (Del. Ch. Sept. 27, 1999)], Chancellor Chandler considered whether a target board had breached its fiduciary duties by entering into a merger agreement containing a no-talk provision. Unlike a traditional no-shop clause, which permits a target board to communicate with acquirers under limited circumstances, a no-talk clause -- and here I'm quoting from the Chancellor -- "not only prevents a party from soliciting superior offers or providing information to third parties, but also from talking to or holding discussions with third parties."

The Vice Chancellor commented that while "a board doesn't necessarily have an obligation to negotiate," it "does have an ongoing statutory and fiduciary obligation to provide a current, candid and accurate merger recommendation," which encompasses "an ongoing fiduciary obligation to review and update its recommendation," and a "Don't Ask, Don't Waive" provision in a standstill is "impermissible" to the extent it limits a board's "ongoing statutory and fiduciary obligations to properly evaluate a competing offer, disclose material information, and make a meaningful merger recommendation to its stockholders." These are ongoing obligations no matter how pristine the process adopted by the Board in making its initial decision to approve a transaction and recommend it to stockholders.

In *Ancestry.com*, the bidders in an auction initiated by the target were required to sign confidentiality agreements containing standstill restrictions that included "Don't Ask, Don't Waive" provisions. The ultimate winner in this process was a private equity firm which did not "demand an assignment" of the provision in the merger agreement, thereby leaving it within the target's discretion whether or not to allow

In *Koehler v. NetSpend Holdings Inc.*,[11] the Delaware Chancery Court criticized a Board's sales process as "unreasonable," but nevertheless declined to enjoin a $1.4 billion sale which it found represented the stockholders' only opportunity to receive a premium for their shares. The case involved a merger price that was well below the low end of the share price implied by the bankers' discounted cash flow analysis, a 3.9% termination fee, matching rights, and no-shop clause, as well as voting agreements covering 40% of the vote (coterminous with the merger agreement), and a Board decision to trade a price increase for a go-shop provision. The Court was critical of the merger agreement's prohibition of the company from waiving "don't-ask-don't-waive" provisions in standstill agreements from a prior transaction. This prohibition was subject to the Board's fiduciary out, but the Court considered that protection "illusory" as the terms of the standstill agreements would deter private equity firms from even requesting a waiver. While commenting that *Revlon* does not preclude a single-bidder negotiated deal, the Court said that, "[w]here a board decides to forgo a market check," the Court may review the deal terms and process with greater scrutiny and was troubled by the fact that the fairness opinion showed discounted cash flow ranges far above the deal price (a "***weak fairness opinion***").[12] These concerns

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unsuccessful bidders to make unsolicited topping bids prior to receiving stockholder approval. Chancellor Strine generally praised the process followed by the Ancestry Board, noting that the Board was "trying to create a competitive dynamic" and the process "had a lot of vibrancy and integrity to it … ." With respect to the "Don't Ask, Don't Waive" provision, the Chancellor noted that while it "is a pretty potent provision," he was aware of "no statute" or "prior ruling of the Court" that rendered such provisions "per se invalid," and wrote that a "Don't Ask, Don't Waive" provision actually may be used by a "well-motivated seller … as a gavel" for "value-maximizing purposes" by communicating to bidders that "there really is an end to the auction for those who participate," creating an incentive for bidders to "bid your fullest because if you win, you have the confidence of knowing you actually won that auction at least against the other people in the process," which may attract prospective bidders to a process that has "credibility so that those final-round bidders know the winner is the winner, at least as to them." *See* Christina M. Sautter, *Promises Made to be Broken? Standstill Agreements in Change of Control Transactions*, 37 Del J. Corp. L. 965 (2013); Robert S. Reder, *Delaware Chancellor Weighs in on "Don't Ask, Don't Waive" Provision of Standstill Agreement*, Bloomberg BNA Corporate Practice Library, 28 CCW 24 (2013).

The Chancellor was, however, troubled by the target's failure to disclose in proxy materials sent to stockholders the potential impact of the "Don't Ask, Don't Waive" provision on the bidding process, warned that directors "better be darn careful" in running an auction process to be sure that "if you're going to use a powerful tool like that, are you using it consistently with your fiduciary duties, not just of loyalty, but of care." Chancellor Strine faulted the lack of proxy statement disclosures regarding the "Don't Ask, Don't Waive" provision as "probabilistically in violation of the duty of care" since the Board was "not informed about the potency of this clause," and it "was not used as an auction gavel." Once the winning bidder "did not demand an assignment of it," the Board did not "waive it in order to facilitate those bidders which had signed up the standstills being able to make a superior proposal." The Chancellor "enjoin[ed] the deal subject to those disclosures being promptly made."

[11] C.A. No. 8373-VCG, 2013 Del. Ch. LEXIS 131, at *2 (Del. Ch. May 21, 2013). *See* John K. Hughes, *Board Sales Processes: A 'Weak' Fairness Opinion Highlights the Importance of Identifying Strategic Inflection Points in Deals*, Deal Points: The Newsletter of the Committee on Mergers and Acquisitions Volume XVIII, Issue 3, at 14 (Summer 2013).

[12] In *In re BioClinica, Inc. Shareholder Litigation*, C.A. No. 8272-VCG, 2013 WL 5631233 (Del Ch. Oct. 16, 2013), a weak fairness opinion alone was insufficient to defeat a motion to dismiss where the target's Board had employed an auction canvass of twenty-one separate entities (Vice Chancellor Glasscock commented that it was reasonable for the Board to reach out initially only to financial buyers in order to minimize the risk of misuse of confidential information by competitors, although it ultimately reached out to four strategic companies it thought might be buyers) and a special committee of independent directors who were regularly advised by counsel as to their fiduciary duties.

led the Court to conclude that the Board had probably breached its duty of care, but it declined to enjoin the transaction, finding that the risks of a potential injunction would outweigh its benefits.

C. Non Reliance Provisions. In *RAA Management, LLC v. Savage Sports Holdings, Inc.*,[13] the Delaware Supreme Court held that non-reliance disclaimer language in a confidentiality agreement was effective to bar fraud claims by a prospective buyer. The prospective buyer had been told by seller during early discussions that seller had no significant unrecorded liabilities, but due diligence showed otherwise. The confidentiality agreement provided that seller made no representations regarding any information provided[14] and that buyer could only rely on express representations in a definitive acquisition agreement, which was never signed. After deciding not to pursue a transaction, the buyer sued seller to recover its due diligence and other deal costs. In affirming the Superior Court's dismissal of the buyer's complaint, the Delaware Supreme Court wrote:

> Before parties execute an agreement of sale or merger, the potential acquirer engages in due diligence and there are usually extensive precontractual negotiations between the parties. The purpose of a confidentiality agreement is to promote and to facilitate such precontractual negotiations. Non-reliance clauses in a confidentiality agreement are intended to limit or eliminate liability for misrepresentations during the due diligence process. The breadth and scope of the non-reliance clauses in a confidentiality agreement are defined by the parties to such preliminary contracts themselves. In this case, RAA and Savage did that, clearly and unambiguously, in the NDA.
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> * * *
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> The efficient operation of capital markets is dependent upon the uniform interpretation and application of the same language in contracts or other documents. The non-reliance and waiver clauses in the NDA preclude the fraud claims asserted by RAA against Savage. Under New York and Delaware law, the reasonable commercial expectations of the parties, as set forth in the non-reliance disclaimer clauses in Paragraph 7 and the waiver provisions in Paragraph 8 of the NDA, must be enforced. Accordingly, the Superior Court properly granted Savage's motion to dismiss RAA's Complaint.

II. LETTER OF INTENT

A letter of intent is often entered into between a buyer and a seller following the successful completion of the first phase of negotiations of an acquisition transaction. A letter of intent typically describes the purchase price (or a formula for determining the purchase price) and certain other key economic and procedural terms that form the basis for further negotiations. In most cases, the buyer and the seller do not yet intend to be legally bound to consummate the transaction and expect that the letter of intent will be superseded by a definitive written acquisition agreement.

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[13] 45 A.3d 107, 117 (Del. 2012).

[14] With respect to the effectiveness of non-reliance clauses to eliminate extra contractual liabilities, *see infra* the Comment to Section 13.7.

Alternatively, buyers and sellers may prefer a memorandum of understanding or a term sheet to reflect deal terms. Many lawyers prefer to bypass a letter of intent and proceed to the negotiation and execution of a definitive acquisition agreement.

Although the seller and the buyer will generally desire the substantive deal terms outlined in their letter of intent to be nonbinding expressions of their then current understanding of the shape of the prospective transaction, letters of intent frequently contain some provisions that the parties intend to be binding. **Appendix B** includes a form of letter of intent and a discussion of considerations relevant to the decision whether to use a letter of intent and what to include in one.

At an early stage in the negotiations, the buyer may ask for the seller to agree to negotiate exclusively with the buyer. The buyer will argue that it will have to spend considerable time and resources in investigating the target and developing a deal proposal, and it wants assurance that the target will not sell to another bidder before a proposal can be developed and negotiated. As with public companies, private companies may agree to negotiate exclusively with a suitor for a relatively short period (usually no more than a few weeks or months) to induce the prospective buyer to commence its due diligence and develop an acquisition proposal.[15] In the acquisition of a private company, the exclusivity agreement is sometimes included in a letter of intent as the seller may be reluctant to agree not to negotiate with anyone else until it has confidence the suitor is making an offer good enough to merit negotiation.[16]

III. ENTERPRISE PRODUCTS PARTNERS, L.P. V. ENERGY TRANSFER PARTNERS, L.P.

Confidentiality Agreements and Letters of Intent often contain provisions to the effect that the parties will not be bound to consummate a transaction unless and until they each negotiated and executed a Definitive Agreement. Disputes often arise over whether parties have agreed to, or by their conduct they have, committed themselves to a transaction.

Enterprise Products Partners, L.P. v. Energy Transfer Partners, L.P.[17] involved a series of preliminary agreements that were entered into between Energy Transfer Partners, L.P. (***"ETP"***), a Dallas-based Delaware master limited partnership (***"MLP"***), and Enterprise Product Partners, L.P. (***"Enterprise"***), a Houston-based Delaware MLP, in March and April 2011, with a view to forming a joint venture to build and operate a large pipeline from Cushing, Oklahoma to the Gulf Coast of Texas, which they called the "Double E Pipeline." Those preliminary agreements provided that the obligations of the parties were conditioned on the execution of a definitive joint venture agreement and approvals by the respective boards of directors. Although no definitive joint venture agreement had been signed, the parties proceeded to spend time and money on the project

[15] *See* Richard E. Climan et al., *Negotiating Acquisitions of Public Companies in Transactions Structured as Friendly Tender Offers*, 116 PENN ST. L. REV. 615, 650-656 (2012).

[16] *See* **Appendix B - Letter of Intent** at 2, 12-13.

[17] No. 05-14-01383-CV, 2017 Tex. App. LEXIS 6658, 2017 WL 3033312 (Tex. App.—Dallas July 18, 2017, no pet. h.).

and, reminiscent of *Texaco v. Pennzoil*,[18] they communicated publicly that a joint venture had been formed, and they marketed the pipeline to potential customers.

The parties' marketing efforts did not produce enough commitments to ship through the proposed new pipeline to meet their agreed minimum threshold. Enterprise terminated its participation in the project on August 15, 2011 and shortly thereafter entered into agreements with Enbridge (US) Inc. (***"Enbridge"***), another large pipeline company, for an alternative crude oil pipeline from Cushing to the Texas Gulf Coast. Enterprise and Enbridge began discussions before Enterprise announced that it had terminated the project with ETP.

ETP sued Enterprise in the 298th Judicial District Court in Dallas on September 30, 2011 alleging that Enterprise breached Enterprise's contractual obligations and fiduciary duties to ETP. Notwithstanding the express provisions in preliminary agreements that no party was bound unless and until definitive agreements were signed, ETP claimed—and the jury found—that the ensuing conduct of ETP and Enterprise had served to form a Texas law partnership and that Enterprise had breached its fiduciary duty of loyalty to ETP when it entered into agreements with Enbridge. The trial court awarded ETP judgment for $535 million on July 29, 2014.

This decision was reversed by the Court of Appeals in *Enterprise Products Partners, L.P. v. Energy Transfer Partners, L.P.*[19] on July 28, 2017. More about this saga follows.

The preliminary agreements between ETP and Enterprise provided that there would be no partnership or joint venture formed unless and until later definitive agreements were executed. The confidentiality agreement between ETP and Enterprise (the ***"Confidentiality Agreement"***) provided that they were not bound to pursue any transaction until a definitive agreement was signed as follows:

> The Parties agree that **unless and until a definitive agreement** between the Parties with respect to the Potential Transaction **has been executed and delivered**, and then only to the extent of the specific terms of such definitive agreement, **no Party hereto will be under any legal obligation of any kind whatsoever with respect to any transaction by virtue of this Agreement or any written or oral expression with respect to such a transaction by any Party or their respective Representatives, except, in the case of this Agreement, for the matters specifically agreed to herein**. A Party shall be entitled to cease disclosure of Confidential Information hereunder and **any Party may depart from negotiations at any time for any reason or no reason without liability to any Party hereto.**

The parties also signed a letter agreement and term sheet (the ***"Letter of Intent"***) that provided as follows:

> Neither this letter nor the JV Term Sheet create any binding or enforceable obligations between the Parties and, except for the [ETP] Confidentiality Agreement. . . no binding or enforceable obligations shall exist between the Parties

[18] 729 S.W.2d 768, 784 (Tex. App.—Houston [1st Dist.] 1987, writ ref'd n.r.e.).

[19] No. 05-14-01383-CV, 2017 Tex. App. LEXIS 6658 at *31, 2017 WL 3033312 at *11.

> with respect to the Transaction unless and until the Parties have received their respective board approvals and definitive agreements memorializing the terms and conditions of the Transaction have been negotiated, executed and delivered by both of the Parties.
>
> * * *
>
> **Unless and until** such definitive agreements are executed and delivered by both of the Parties, either [Enterprise] or ETP, **for any reason**, may depart from or **terminate the negotiations with respect to the Transaction at any time without any liability or obligation** to the other, whether arising in contract, tort, strict liability or otherwise.

ETP and Enterprise also signed a Letter Agreement Regarding Sharing of Engineering Costs for Proposed Cushing to Houston Pipeline (the ***"Reimbursement Agreement"***) that stated that the parties had not completed negotiations of the proposed transaction and that no party was bound until the definitive agreements were signed:

> [Enterprise and ETP] **are in the process of negotiating mutually agreeable definitive agreements** ("the Definitive Agreements") related to the construction and operation of a crude oil pipeline between Cushing, OK and Houston, TX ("The Project"). Although **the negotiation** of the Definitive Agreements **has not been completed**, the Parties desire to begin work to develop a detailed engineering design package for The Project (the "Work") prior to execution of the Definitive Agreements.
>
> * * *
>
> It is understood by each of the Parties that the execution of this Agreement is intended to create and does create legally binding obligations between Enterprise and ETP but only as set forth herein. The obligations of the Parties shall be several and not joint and no Party shall have the right, authority or power to bind the other Party to any agreement without its prior written consent (other than the authority to commit and/or expend funds under Section I of this Agreement). Each Party expressly agrees to indemnify and hold the other Party harmless from liability if it binds or attempts to bind the other Party to any other agreement without such prior written consent. **Nothing herein shall be deemed to create or constitute a joint venture, a partnership, a corporation, or any entity taxable as a corporation, partnership or otherwise.**

ETP and Enterprise communicated publicly that a joint venture had been formed and marketed the pipeline to potential customers. Marketing materials in some instances stated that the parties had already "formed a Joint Venture LLC," a "50/50 JV," which they called "Double E Crude Pipeline, LLC." These marketing efforts were conducted jointly to potential customers, who were told, along with the Federal Energy Regulatory Commission and the Texas Railroad Commission, that a joint venture – the Double E Pipeline LLC – "had been formed" by ETP and Enterprise. ETP and Enterprise also set up an "Integrated Project Team," comprised of ETP and

Enterprise engineers, to begin performing the prerequisite technical work of modeling and potentially constructing the future pipeline.

As part of their joint efforts, ETP and Enterprise announced an ***"open season,"*** a window of time during which shippers could sign a "Transportation Services Agreement" (***"TSA"***). A TSA is a long-term (sometimes decades-long) commitment to ship a certain number of barrels a day for a certain tariff rate. TSAs are vitally important to new pipeline projects because pipeline builders usually insist on having a certain level of shipper commitment prior to beginning construction in order to insure the economic viability of the prospective pipeline.

At the end of the open season, Chesapeake Energy signed a TSA with "Double E Pipeline LLC" to ship thousands of barrels a day, making it an "anchor shipper." Despite this agreement, in August 2011, Enterprise unilaterally issued a press release announcing the termination of the project due to lack of long-term commitments from potential shippers. A few weeks later, Enterprise and Enbridge Inc. announced they would jointly pursue a crude pipeline project from Cushing to the Gulf Coast.

ETP filed suit in the 298th District Court in Dallas claiming that the parties' ensuing conduct served to form a Texas partnership and that Enterprise breached its fiduciary duty of loyalty to ETP. The evidence introduced during the four-week jury trial showed that Enterprise executives had been secretly meeting with Enbridge personnel during the Double E open season. Testimonial and documentary evidence also showed that Enterprise represented to Enbridge that if the Double E project did not obtain enough shipper commitments during the open season, Enterprise would terminate Double E and announce its project with Enbridge instead.

During these meetings, Enterprise disclosed information generated by the Double E joint efforts, including technical engineering data, the pipeline route, economic modeling and Double E prospective customer information. The evidence also showed that Enterprise represented to Enbridge that the Chesapeake commitment had been made only to Enterprise, not to ETP or the joint venture. Enterprise and Enbridge ultimately did build a pipeline from Cushing, Oklahoma to the Gulf along the same route as the proposed Double E Pipeline. The biggest shipper for this new pipeline was Chesapeake Energy. The Enterprise/Enbridge pipeline also ultimately signed TSAs with other prospective customers of the proposed Double E Pipeline.

After deliberating for less than two days, the jury found for ETP, notwithstanding the express provisions in the Confidentiality Agreement, the Letter of Intent and the Reimbursement Agreement that no party was bound unless and until definitive agreements were signed. Rather, the jury concluded that ETP and Enterprise had conducted themselves as partners during the Double E joint venture and that Enterprise's conduct breached the duties it owed to ETP.

The jury's charge on whether the parties' conduct resulted in a partnership was based on the five-factor test set forth in § 152.052(a) of the Texas Business Organizations Code (the "***TBOC***") for determining whether a partnership exists: (i) the right to share profits, (ii) expression of intent to be partners, (iii) the right to participate in control of the business, (iv) sharing or agreeing to share losses or liabilities, and (v) agreeing to or contributing money or assets to the

business.[20] Under Texas law (i) a party does not have to prove all five factors to show that a partnership has been formed, (ii) whether a partnership exists turns on the totality of the circumstances, and (iii) a partnership agreement can be oral.[21] Whether or not the parties expressed an intent to form a partnership is not determinative, and the parties may still be found to have formed a partnership even if they expressly agreed otherwise if their conduct demonstrates they intended to do the things that formed a partnership.

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[20] *See Ingram v. Deere*, 288 S.W.3d 886, 895-96 (Tex. 2009), in which the Supreme Court of Texas held that while "common law required proof of all five factors to establish the existence of a partnership, . . . TRPA does not require direct proof of the parties' intent to form a partnership" and instead uses a "totality-of-the-circumstances test" in determining the existence of a partnership. The Supreme Court explained:

> Whether a partnership exists must be determined by an examination of the totality of the circumstances. Evidence of none of the factors under the Texas Revised Partnership Act will preclude the recognition of a partnership, and even conclusive evidence of only one factor will also normally be insufficient to establish the existence of a partnership under TRPA. However, conclusive evidence of all five factors establishes a partnership as a matter of law. In this case, Deere has not provided legally sufficient evidence of any of the five TRPA factors to prove the existence of a partnership. Accordingly, we reverse the court of appeals' judgment and reinstate the trial court's take-nothing judgment. *Id.* at 903-04.

See *EGAN ON ENTITIES: Corporations, Partnerships and Limited Liability Companies in Texas* (2016) 364-367.

[21] Texas does not require an express written or oral agreement to form a partnership, *see, e.g., Garcia v. Lucero*, 366 S.W.3d 275, 278 (Tex. App.—El Paso 2012, no pet.) ("The existence of a formal partnership agreement is not one of the five factors."); *Sewing v. Bowman*, 371 S.W.3d 321, 332 (Tex. App.—Houston [1st Dist.] 2012 pet. dism'd) ("Partnership formation may be implied from the facts and circumstances of a case."); *Ferch v. Baschnagel*, 03-04-00605-CV, 2009 Tex. App. LEXIS, at *28-*29, 2009 WL 349149, at *9 (Tex. App.—Austin, Feb. 13, 2009, no pet.) ("It is well established that, even if an offer and acceptance are not recorded on paper, dealings between parties may result in an implied contract where the facts show that the minds of the parties met on the terms of the contract without any legally expressed agreement."); *Shindler v. Marr & Associates*, 695 S.W.2d 699, 703 (Tex. App.—Houston [1st Dist.] 1985, writ ref'd n.r.e.) ("In order to establish a partnership de facto, neither a written nor an oral agreement is essential; a partnership relation may be implied from the facts and circumstances surrounding the transaction."). Texas, like the vast majority, if not all, jurisdictions, follows the Uniform Partnership Act and the Revised Partnership Act in this respect; partnership formation is adjudged on the factual circumstances rather than on the existence of a formal agreement.

This has always been the law in Texas. *See, e.g., Howard Gault & Son, Inc., v. First Nat'l Bank of Hereford*, 541 S.W.2d 235, 237 (Tex. Civ. App.—Amarillo 1976, no writ) ("The statement in one of the agreements that the farming operation was not a partnership is not conclusive on the question of partnership. It is the intent to do the things that constitute a partnership that determines that the relationship exists between the parties, and if they intend to do a thing which in law constitutes a partnership, they are partners whether their expressed purpose was to create or avoid the relationship."); *Fed. Sav. & Loan Ins. Corp. v. Griffin*, 935 F.2d 691, 700 (5th Cir. 1991) ("[A] statement that no partnership is formed cannot be conclusive proof that no partnership was formed."); *Shindler*, 695 S.W.2d 699, 704 (Tex. App.—Houston [1st Dist.] 1985, writ ref'd, n.r.e.) ("It is the common intention to do the things that constitute a partnership that determines the relationship existing between the parties, whether the partnership agreement is oral or written, express or implied from the conduct of the parties in proceeding with the business of the partnership. If they intend to do a thing which constitutes a partnership, they are partners whether their express purpose was to create or avoid partnership.").

Although both ETP and Enterprise were Delaware entities, the jury charge and the jury's verdict were based in Texas partnership law.

In July 2014, the district court signed a judgment for ETP awarding more than $319 million in actual damages, $150 million in disgorgement of wrongfully obtained benefits, and more than $66 million in interest. Enterprise appealed.

On July 18, 2017, the Court of Appeals reversed the judgment against Enterprise, holding that ETP had failed to prove that the conditions precedent stated in the letter agreement had been satisfied or waived. The Court rejected ETP's argument that the formation of a common law partnership between ETP and Enterprise was controlled solely by the five-factor test in TBOC § 152.052. Instead, the Court ruled that the TBOC § 152.052 five factors are non-exclusive. The conditions in the parties' Letter of Intent, which required Board approval and execution of definitive agreements, constituted conditions precedent that had to be satisfied before a partnership could be formed. The Court concluded that:

1. The unfulfilled conditions precedent in the parties' written agreements precluded forming the alleged partnership unless ETP obtained a jury finding that the parties waived those conditions precedent;

2. ETP's failure to request such a finding meant that it had to establish waiver of the conditions precedent as a matter of law; and

3. ETP did not prove as a matter of law that the parties waived the conditions precedent.

The Court therefore rendered judgment that ETP recover nothing from Enterprise. It is anticipated that ETP will petition the Texas Supreme Court to review the decision.

APPENDIX A

CONFIDENTIALITY AGREEMENT

PRELIMINARY NOTE

Confidentiality agreements are primarily a concern for the seller who is disclosing essential and very confidential information regarding its assets and business to a prospective Buyer who is currently, or if the transaction is not consummated may later become a competitor of the Seller or the ultimate purchaser of its business. Consequently, this Confidentiality Agreement has been prepared as a first draft from the Seller (the **"Discloser"**) and includes provisions favorable to the Seller. The prospective Buyer (the **"Recipient"**) may want to modify many of its provisions to be more in the Recipient's favor.

The Confidentiality Agreement is usually the first document in the acquisition process, and is signed by the Recipient before the Discloser provides any confidential information. If the parties agree to proceed with the transaction, the definitive acquisition or merger agreement between the parties (the "***Definitive Agreement***") may have its own provisions on obligations of confidentiality which would supersede the Confidentiality Agreement

This Confidentiality Agreement has no "sunset" provision and is silent on the topics of the duration of obligations of confidentiality and to what extent the obligations continue if the acquisition closes or does not close. Absent such a provision, the Discloser may take the position that they continue forever. The Recipient, on the other hand, may think that even the Discloser's proprietary know-how will become obsolete and assert that all obligations of confidentiality should come to an end at some early point. The parties may consider whether their interests would be served by "sunsetting" the Confidentiality Agreement as a whole or by providing different survival provisions for different categories of information or different obligations of confidentiality.

If a Definitive Agreement is entered into, it will have to deal with the extent to which the Confidentiality Agreement (or portions of it) will be modified or superseded by that agreement, particularly in terms of the typical "integration" provision. Article 12 of the ABA Model Asset Purchase Agreement (the "***Model Asset Purchase Agreement***") contemplates a regimen of confidentiality that will restate and supersede Recipient's and Discloser's obligations under the Confidentiality Agreement. Certain other provisions of the Confidentiality Agreement do not appear in Article 12 of the Asset Purchase Agreement because their subject matter is covered by other provisions of the Asset Purchase Agreement.

This form of Confidentiality Agreement takes the form of a "unilateral agreement" that protects the Discloser's confidential information in the hands of the Recipient. The Discloser may want details about the Recipient's capacity to finance the transaction, other transactions the Recipient has done, the identity of the Recipient's lenders and other confidential information. Moreover, where the consideration includes securities of the Buyer, the Discloser may require confidential information about the Recipient at a very early stage. Accordingly, the Recipient and the Discloser may find it appropriate to make obligations under the Confidentiality Agreement reciprocal and bilateral. An alternative, when the parties have initially signed a unilateral Confidentiality Agreement presented by the Discloser (the seller) to the Recipient (the buyer), is

for the parties to enter into a mirror agreement to protect the Recipient's information in the hands of the Discloser (of course, in that case, the prospective buyer will be the **"Discloser,"** and the prospective seller will be the **"Recipient"**).

A. Form of Confidentiality Agreement

[Date]

[Name]
[Discloser]
[Address]

PRIVATE AND CONFIDENTIAL

Dear __________:

In connection with the consideration by __________ (**"Recipient"**) of a possible transaction (the **"Transaction"**) with __________ (**"Discloser"**), Recipient has requested access to certain information, properties and personnel of Discloser.

COMMENT

In its first sentence, this Confidentiality Agreement defines that Recipient's use of Confidential Information is limited to Recipient's consideration of the proposed transaction. The Confidentiality Agreement does not characterize the transaction, does not identify the parties as "Buyer" and "Seller," and describes the transaction only as "possible" to avoid implication that any agreement about the transaction has been made between the parties or will be created by the Confidentiality Agreement.

In consideration for and as a condition to Discloser's furnishing access to such information, properties and personnel of Discloser as Discloser, in its sole discretion, agrees to deliver or otherwise make available (**"disclose"**) to Recipient, Recipient agrees to the terms and conditions set forth in this agreement:

COMMENT

Although the Confidentiality Agreement does not expressly provide that Discloser must disclose all information requested by Recipient, consideration is often given to the inclusion here of the following language: "Discloser may, in its sole discretion, withhold information where it concludes that the disclosure of such information would violate applicable law, breach a duty, subject Discloser to risk of a material penalty, or be detrimental to its interests, in which case it shall advise Recipient as to the general nature or category of information withheld." In some circumstances, the Discloser may be prohibited from disclosing certain information by restrictions under its existing contractual relationships.

1. CONFIDENTIAL AND PROPRIETARY NATURE OF THE INFORMATION

Recipient acknowledges the confidential and proprietary nature of the Confidential Information (as defined below), agrees to hold and keep the Confidential Information as provided in this agreement and otherwise agrees to each and every restriction and obligation in this agreement.

2. CONFIDENTIAL INFORMATION

As used in this agreement, the term **"Confidential Information"** means and includes any and all of the items described in paragraphs (a) and (b) below that has been or may hereafter be disclosed to Recipient by Discloser or by the directors, officers, employees, agents, consultants, advisors or other representatives, including legal counsel, accountants and financial advisors (**"Representatives"**) of Discloser:

(a) trade secrets concerning the business and affairs of Discloser (which includes the materials dated ________ ____, 20___, and disclosed to Recipient by __________), product specifications, data, know-how, formulae, compositions, processes, designs, sketches, photographs, graphs, drawings, samples, inventions and ideas, past, current, and planned research and development, current and planned manufacturing or distribution methods and processes, customer lists, current and anticipated customer requirements, price lists, supplier lists, market studies, business plans, computer software and programs (including object code and source code), computer software and database technologies, systems, structures and architectures (and related processes, formulae, composition, improvements, devices, know-how, inventions, discoveries, concepts, ideas, designs, methods and information), __________ and any other information, however documented, that is a trade secret within the meaning of __________ § ____-____-____ [applicable state trade secret law]); and

(b) information concerning the business and affairs of Discloser (which includes historical financial statements, financial projections and budgets, historical and projected sales, capital spending budgets and plans, the names and backgrounds of key personnel, personnel training techniques and materials and _____), however documented, or is otherwise obtained from review of Discloser's documents or property or discussions with Discloser's Representatives or by Recipient's Representatives (including current or prospective financing sources) or Representatives of Recipient's Representatives irrespective of the form of the communication, and also includes all notes, analyses, compilations, studies, summaries and other material prepared by Recipient or Recipient's Representatives containing or based, in whole or in part, upon any information included in the foregoing.

Any trade secrets of Discloser will also be entitled to all of the protections and benefits under _____ Section _____ [applicable state trade secret law] and any other applicable law. If any information that Discloser deems to be a trade secret is found by a court of competent jurisdiction not to be a trade secret for purposes of this agreement, such information will in any event still be considered Confidential Information for purposes of this agreement. In the case of trade secrets, Recipient hereby waives any requirement that Discloser submit proof of the economic value of any trade secret or post a bond or other security.

To the extent that any Confidential Information may include materials subject to the attorney-client privilege, the Discloser is not waiving and will not be deemed to have waived or diminished its attorney work-product protections, attorney-client privileges or similar protections and privileges as a result of disclosing any Confidential Information (including Confidential Information related to pending or threatened litigation) to Recipient, regardless of whether Discloser has asserted or is or may be entitled to assert such privileges and protections. The parties (a) share a common legal and commercial interest in all such Confidential Information that is subject to such privileges and protections; (b) are or may become joint defendants in proceedings to which such Confidential Information covered by such protections and privileges relates; and (c) intend that such privileges and protections remain intact should either party become subject to any actual or threatened proceeding to which such Confidential Information covered by such protections and privileges relates. In furtherance of the foregoing, Recipient shall not claim or contend, in proceedings involving either party, that Discloser waived its attorney work-product protections, attorney-client privileges or similar protections and privileges with respect to any information, documents or other material not disclosed to Recipient due to Discloser disclosing Confidential Information (including Confidential Information related to pending or threatened litigation) to Recipient.

COMMENT

The term **"Confidential Information"** is defined broadly to include all information concerning the business and affairs of Discloser that will be disclosed to Recipient. Exceptions are carved out—not from the definition but rather as exceptions to the obligation of nonuse and nondisclosure in Sections 6 and 7 below—in order to provide for circumstances in which the information is no longer required to be treated as Confidential Information. Such circumstances include information that becomes generally available to the public (other than by a result of unauthorized disclosure) or information that is otherwise made available to Recipient without a wrongful act on the part of the party providing the information.

In the absence of a confidentiality agreement and subject to applicable state law, trade secrets, but not confidential information, can be protected from disclosure. *See* Restatement of the Law of Unfair Competition § 41, cmt. d (1995). Many states have adopted a version of the Uniform Trade Secrets Act that defines information as a "trade secret" if it (a) derives economic value from being generally unknown to other persons who can obtain economic value from its disclosure or use and (b) is subject to efforts that are reasonable under the circumstances to maintain its secrecy or confidentiality. *See* Unif. Trade Secrets Act § 1(4), 14 U.L.A. 438 (1990) and 152 (1998 supp.); the Texas Uniform Trade Secrets Act, Tex. Civ. Prac. & Rem. Code § 134A.001, *et seq.* (2013); Alan Bush and Morgan Culbreth, *Texas Steps Into the Fray on the "Uniform" Trade Secrets Act*, 32 Corp. Couns. Rev. 83 (2013); *cf. Lamont v. Vaquillas Energy Lopeno Ltd., LLP*, 421 S.W.3d 198 (Tex. App.—San Antonio 2013) (oil and gas prospect maps were confidential information and protected trade secrets). The Restatement of the Law of Unfair Competition Section 39 defines trade secrets slightly differently, but comment b to that section states that the definition is intended to be consistent with the definition in the Uniform Trade Secrets Act. The Uniform Trade Secrets Act and the

Confidentiality Agreement complement one another because protection of information under such trade secret law provides Discloser with another enforceable way to prevent misappropriation of information. Many states have also adopted criminal statutes specifically addressed to the misappropriation of trade secrets. In other states, more general criminal statutes have been interpreted to reach such misappropriations. In some circumstances, a misappropriation of trade secrets may also violate federal wire and mail fraud statutes (18 U.S.C. §§ 1341, 1343), the National Stolen Property Act (18 U.S.C. § 2314) and the Economic Espionage Act of 1996 (18 U.S.C. §§ 1831 et seq.).

The Confidentiality Agreement serves three primary purposes: (a) it expands the state law protection of trade secrets to confidential information, (b) it clarifies and delineates the obligations of Recipient, particularly with respect to its Representatives, and (c) it helps Discloser demonstrate that it used appropriate efforts to protect the information.

The Uniform Trade Secrets Act Section 1(4) requires reasonable efforts "under the circumstances" to maintain the secrecy of information constituting trade secrets, and such efforts are at least advisable for confidential information. While executing the Confidentiality Agreement demonstrates such efforts, stamping materials to be protected "CONFIDENTIAL" further demonstrates such efforts. If the parties decide to require that all documents containing confidential information be stamped, the Discloser should include a provision that its inadvertent failure to stamp a document is not a waiver of its confidentiality. The Discloser should, at a minimum, keep a list or copies of all documents disclosed to the Recipient and all persons with whom the Recipient spoke.

Both the Discloser and the Recipient may find it advantageous to have significant oral information promptly confirmed by the Discloser in writing as being confidential and acknowledged by the Recipient. In the event of a dispute over the disclosure, the evidentiary problems of proof are lessened when oral communications are reduced to writing. Because of the difficulty in consistently adhering to such requirement, the Confidentiality Agreement excludes such a requirement. Additionally, there may be oral disclosures sufficiently sensitive that neither party wants them reduced to writing.

Special issues may arise when the Recipient is a competitor or potential competitor of the Discloser. In such cases, the Recipient may not wish to review (and the Discloser may not wish the Recipient to review) certain technical information in order to preclude any future claims of misuse of proprietary information. It may prove advantageous to list or otherwise describe all such excluded materials in, or on a schedule or supplement to, the Confidentiality Agreement.

Further, when the acquisition involves a competitor, special steps need to be taken in connection with the disclosure of pricing or other competitively sensitive information. The Recipient's possession of such information could be damaging evidence if the acquisition is not completed and an antitrust claim is subsequently

asserted. Alternatives to not disclosing such information are to (a) limit disclosure to the Recipient's personnel who are not in a position to use the information in a manner that would violate the antitrust laws or (b) defer disclosure until as late as possible in the process.

The risks that preacquisition disclosure of sensitive information will violate antitrust laws can be considerable. In the settlement of a divestiture case in which it found unlawful preacquisition transfers of competitively sensitive information, the Federal Trade Commission imposed lengthy bans upon the divesting company's obtaining or providing such information in any future acquisition of a competitor's stock or assets without specific safeguards. *In re* Insilco Corp., FTC File No. 961-0106, 5 Fed. Trade Reg. Rptr. (CCH) ¶ 24,319 (Aug. 27, 1997); *see* Blumenthal, *The Scope of Permissible Coordination between Merging Entities prior to Consummation*, 63 Antitrust L.J. 1 (1994).

The final paragraph of Section 2 addresses how to disclose sufficient information to the Recipient to facilitate a meaningful evaluation of litigation-related confidential information without waiving the attorney-client and other privileges that protect the information. See the Comment to Section 12.6 of the Model Asset Purchase Agreement and the authorities discussed therein.

Furthermore, if the acquisition is not consummated, the Recipient should be required to return the competitively sensitive information (together with copies and derivative materials) or to certify to the Discloser that all copies of such information have been destroyed. Section 9 of the Confidentiality Agreement imposes such a requirement.

3. RESTRICTED USE OF CONFIDENTIAL INFORMATION

Recipient agrees that the Confidential Information (a) will be kept confidential by Recipient and Recipient's Representatives and (b) without limiting the foregoing, will not be disclosed by Recipient or Recipient's Representatives to any person (including current or prospective financing sources) except with the specific prior written consent of _____ (the **"Discloser Contact"**) [a designated individual or a designated position, such as chief financial officer] or except as expressly otherwise permitted by this agreement. It is understood that Recipient may disclose Confidential Information to only those of Recipient's Representatives who (a) require such material for the purpose of evaluating the Transaction and (b) are informed by Recipient of the confidential nature of the Confidential Material and the obligations of this agreement. Recipient further agrees that Recipient and Recipient's Representatives will not use any of the Confidential Information either for any reason or purpose other than to evaluate and to negotiate the Transaction. Recipient also agrees to be responsible for enforcing this agreement as to Recipient's Representatives and to take such action, legal or otherwise, to the extent necessary to cause them to comply with this agreement and thereby prevent any disclosure of the Confidential Information by any of Recipient's Representatives (including all actions that Recipient would take to protect its own trade secrets and confidential information) except as permitted by this agreement.

COMMENT

The Confidentiality Agreement defines who will be allowed to use the Confidential Information and the scope and extent of such use.

The foregoing provisions require only that Recipient inform the persons to whom the Confidential Information is disclosed of the confidential nature and the obligations under this Agreement. A Discloser may want to add clauses providing that the Confidential Information may not be disclosed except to persons approved in writing by the Discloser contact prior to any disclosure and requiring such persons to acknowledge, in writing, the obligations of the Confidentiality Agreement. Such written acknowledgment could be accomplished by having a one-sentence cover letter signed by each Representative ("I hereby agree to be bound by the attached agreement from X to Y dated Z") or (as a less burdensome alternative) by having the Recipient's Representatives sign a statement acknowledging that they are familiar with the confidentiality obligations in the Confidentiality Agreement and agree to be bound by its provisions. Another alternative is to merely provide in the Confidentiality Agreement that the Recipient retains responsibility for any unauthorized disclosures or use of the confidential information and for ensuring compliance with the Confidentiality Agreement. This approach may be more acceptable to the Discloser if the Recipient's employees have signed secrecy agreements as a condition of employment with the Recipient.

4. NONDISCLOSURE OF TRANSACTION

Except as expressly permitted by Section 3 and except as expressly permitted by a definitive agreement with respect to the Transaction, if any, entered into between the parties, neither Recipient, Discloser nor their Representatives will disclose to any person the fact that the Confidential Information has been disclosed to Recipient or Recipient's Representatives or that Recipient or Recipient's Representatives have inspected any portion of the Confidential Information or that any discussions or negotiations are taking place concerning the Transaction, provided, however, Recipient and its Representatives may make such a disclosure if, and solely to the extent that, Discloser has already done so or Recipient has received the written opinion of its outside counsel that such a disclosure must be made by Recipient in order that it not commit a violation of law, and further provided, Recipient and its Representatives shall consult with Discloser, to the extent reasonably practicable, before making any such disclosure, and any such permitted disclosure shall not affect or impair Recipient's obligations of confidentiality with respect to the Confidential Information. Without limiting the generality of the foregoing, Recipient further agrees that, without the prior written consent of Discloser, Recipient will not, directly or indirectly, enter into any agreement, arrangement or understanding, or any discussions that might lead to such an agreement, arrangement or understanding, with any person regarding a possible transaction involving Discloser[, provided, however, nothing contained herein shall be deemed to inhibit, impair or restrict the ability of Recipient or its Representatives to have discussions or negotiations with other persons relating to potential financing and/or partnering in connection with and/or investment in the Transaction so long as each of such persons agrees in writing to be bound by the terms of this agreement].

COMMENT

As the parties often want to keep secret the very fact of any negotiation discussions, the Confidentiality Agreement prevents the disclosure of such information or the fact that negotiations are taking place.

Because Recipient may need to disclose the pendency of the discussions under certain circumstances (e.g., under federal securities laws), Recipient is permitted to disclose information without violating Section 4 based upon the written opinion of its counsel that the disclosure is required by applicable law. Recipient is obligated to consult with Discloser, to the extent reasonably practicable, before making any such disclosure.

5. DISCLOSER CONTACT

All requests by Recipient or Recipient's Representatives for Confidential Information, meetings with Discloser's personnel or Representatives or inspection of Discloser's properties must be made to the Discloser Contact.

COMMENT

The Confidentiality Agreement imposes a procedural "bottleneck" whereby all communications with employees of Discloser must be approved by a designated Representative of Discloser—the Discloser Contact—in advance. This procedure provides an opportunity for any employees to be interviewed to be briefed beforehand by Discloser and its counsel so that no unauthorized disclosures of information will be made.

The Discloser and the Recipient may want to implement mechanisms to catalog, control and monitor the delivery of, and access to, Confidential Information and also to coordinate their efforts to some degree.

6. EXCEPTIONS

All of the foregoing obligations and restrictions do not apply to that part of the Confidential Information that Recipient demonstrates (a) was or becomes generally available to the public prior to, and other than as a result of, a disclosure by Recipient or Recipient's Representatives or (b) was available, or becomes available, to Recipient on a nonconfidential basis prior to its disclosure to Recipient by Discloser or a Discloser's Representative, but only if (i) the source of such information is not bound by a confidentiality agreement with Discloser or is not otherwise prohibited from transmitting the information to Recipient or Recipient's Representatives by a contractual, legal, fiduciary or other obligation and (ii) Recipient provides Discloser with written notice of such prior possession either (A) prior to the execution and delivery of this agreement or (B) if Recipient later becomes aware of (through disclosure to Recipient or otherwise through Recipient's work on the Transaction) any aspect of the Confidential Information of which Recipient had prior possession, promptly upon Recipient becoming aware of such aspect.

COMMENT

There is often an exception for materials independently developed by a Recipient, but it is not included in this Confidentiality Agreement because of the potential for disputes over what was "independently developed."

The requirement that the Recipient demonstrate prior possession shifts the burden of proof to the person claiming to be exempt from the obligations of confidentiality.

In certain instances, the Discloser will include a provision prohibiting the Recipient from competing with the Discloser for a specified period of time because of the difficulty the Discloser might otherwise have in proving that the Recipient did, in fact, use the confidential information in its business. Such a noncompetition provision is generally strongly resisted by prospective buyers who are engaged, or have an interest in engaging, in the same business as the Discloser. Moreover, there may be antitrust risks in such a restriction on competition.

7. LEGAL PROCEEDINGS

If Recipient or any of Recipient's Representatives becomes legally compelled (by oral questions, interrogatories, requests for information or documents, subpoena, civil or criminal investigative demand or similar process) to make any disclosure that is prohibited or otherwise constrained by this agreement, Recipient or such Representative, as the case may be, will provide Discloser with prompt notice of such legal proceedings so that it may seek an appropriate protective order or other appropriate relief or waive compliance with the provisions of this agreement. In the absence of a protective order or Recipient's receiving such a waiver from Discloser, Recipient or its Representative is permitted (with Discloser's cooperation but at Recipient's expense) to disclose that portion (and only that portion) of the Confidential Information that Recipient or the Representative is legally compelled to disclose; provided, however, that Recipient and Recipient's Representatives must use reasonable efforts to obtain reliable assurance that confidential treatment will be accorded by any person to whom any Confidential Information is so disclosed.

COMMENT

A Confidentiality Agreement will not protect Discloser against disclosures of information required by legal proceedings. The Discloser, however, wants to be in a position to object to the disclosure of any information or, at a minimum, that it is able to limit or control the scope of any court-ordered disclosure. The Confidentiality Agreement addresses this concern by requiring Recipient and its Representatives to notify Discloser upon their receipt of any such request for information, which enables Discloser to seek a protective order or other relief.

8. CONTACT WITH EMPLOYEES

Without the prior written consent of the Discloser Contact, neither Recipient nor any of Recipient's Representatives will (a) initiate or cause to be initiated (other than through the Discloser Contact) any communication with any employee of Discloser concerning the

Confidential Information or the Transaction or (b) for a period of two years after the date of this agreement, solicit or cause to be solicited the employment of any person who is now employed by Discloser.

COMMENT

The Recipient typically wants to interview employees of the Discloser while in the process of evaluating the acquisition. The Discloser, however, may object because (1) it may prematurely communicate to the Discloser's employees the possibility of a sale of the business and (2) it raises the concern that the Recipient may solicit these employees for employment if the acquisition is not consummated.

Thus, the Confidentiality Agreement requires that Recipient not to solicit any employees of Discloser for a period after the date of the Confidentiality Agreement. The Recipient may argue that this provision should be limited to "key" employees, excluding those not encountered in connection with (or more broadly, not involved with) the proposed acquisition. The Recipient may also insist on being permitted to continue ordinary-course-of-business hiring practices, e.g., help-wanted ads in newspapers and trade publications. A possible solution is to list the "protected" employees or define them to include those persons involved in negotiating the acquisition.

9. RETURN OR DESTRUCTION OF CONFIDENTIAL INFORMATION

If Recipient determines that it does not wish to proceed with the Transaction or if Discloser notifies Recipient that it does not wish Recipient to consider the Transaction any further, then (a) Recipient (i) shall promptly deliver to Discloser Contact all documents or other materials disclosed by Discloser or any Discloser's Representative to Recipient or Recipient's Representatives constituting Confidential Information, together with all copies and summaries thereof in the possession or under the control of Recipient or Recipient's Representatives, and (ii) shall destroy materials generated by Recipient or Recipient's Representatives that include or refer to any part of the Confidential Information, without retaining a copy of any such material or (b) alternatively, if the Discloser Contact requests or gives his prior written consent to Recipient's request, Recipient will destroy all documents or other matters constituting Confidential Information in the possession or under the control of Recipient or Recipient's Representatives. Any such destruction pursuant to the foregoing must be certified by an authorized officer of Recipient in writing to Discloser (and such certification shall include a list of the destroyed materials).

COMMENT

The Recipient will often prefer to destroy materials rather than return them. This is particularly the case because the distinction between Confidential Information disclosed by Discloser and Confidential Information generated by Recipient is often hard to apply in practice. The Recipient's Representatives may well have made notes on the documents they received from the Discloser or incorporated the content of those documents into memoranda and analyses, which are not readily redactable. Accordingly, the Recipient may be unwilling to accept a provision that

permits the Discloser to withhold consent to the Recipient's blanket destruction as an alternative to return. The Discloser may be willing to permit blanket destruction but only when the documents disclosed by it that are to be destroyed, rather than returned, are listed. The Recipient may find this unduly burdensome. In addition, the Recipient may want to couple the destruction alternative with a right to retain an archival set of all confidential information with its in-house or outside lawyers.

10. NO OBLIGATION TO NEGOTIATE OR ENTER A TRANSACTION

Discloser reserves the right, in its sole discretion, to reject any and all proposals made by Recipient or Recipient's Representatives with regard to a Transaction and to terminate discussions and negotiations with Recipient and Recipient's Representatives at any time. Neither Recipient nor Discloser shall have rights or obligations of any kind whatsoever with respect to the Transaction by virtue of this agreement other than for the matters specifically agreed to herein. Without limiting the preceding sentences, nothing in this agreement requires either Recipient or Discloser to enter into a Transaction or to negotiate such transaction for any specified period of time.

COMMENT

See *Crane Co. v. Coltec Industries, Inc.*, 171 F.3d 733 (2d Cir. 1999), in which two public companies entered into a confidentiality agreement that contained a provision similar to the second sentence of Section 10 above which was applied as part of the justification for holding that the plaintiff had no contractual right that was violated when the other party entered into a merger agreement with another suitor.

The parties may want to consider provisions that the confidentiality obligations terminate upon the completion of the acquisition and add a separate section to the Confidentiality Agreement stating the survival period of the confidentiality obligations if the acquisition closes or fails to close.

11. NO REPRESENTATIONS OR WARRANTIES

Discloser retains the right to determine, in its sole discretion, what information, properties and personnel it wishes to make available to Recipient, and neither Discloser nor its Representatives make any representation or warranty (express or implied) concerning the completeness or accuracy of the Confidential Information, except pursuant to representations and warranties that may be made in a definitive agreement for the Transaction, if any, between the parties.

COMMENT

Because at the time the parties enter into the Confidentiality Agreement neither the Discloser nor the Recipient knows what information might be of particular interest to the Recipient or whether the discussions will lead to a definitive agreement, the Discloser may seek a disclaimer of any representations or warranties concerning

the accuracy or completeness of the Confidential Information. This provision is common.

In *RAA Management, LLC v. Savage Sports Holdings, Inc.*,[22] the Delaware Supreme Court held that non-reliance disclaimer language in a confidentiality agreement was effective to bar fraud claims by a prospective buyer. The prospective buyer had been told by seller during early discussions that seller had no significant unrecorded liabilities, but due diligence showed otherwise. The confidentiality agreement provided that seller made no representations regarding any information provided and that buyer could only rely on express representations in a definitive acquisition agreement, which was never signed. After deciding not to pursue a transaction, the buyer sued seller to recover its due diligence and other deal costs. In affirming the Superior Court's dismissal of the buyer's complaint, the Delaware Supreme Court wrote:

> Before parties execute an agreement of sale or merger, the potential acquirer engages in due diligence and there are usually extensive precontractual negotiations between the parties. The purpose of a confidentiality agreement is to promote and to facilitate such precontractual negotiations. Non-reliance clauses in a confidentiality agreement are intended to limit or eliminate liability for misrepresentations during the due diligence process. The breadth and scope of the non-reliance clauses in a confidentiality agreement are defined by the parties to such preliminary contracts themselves. In this case, RAA and Savage did that, clearly and unambiguously, in the NDA.
>
> * * *
>
> The efficient operation of capital markets is dependent upon the uniform interpretation and application of the same language in contracts or other documents. The non-reliance and waiver clauses in the NDA preclude the fraud claims asserted by RAA against Savage. Under New York and Delaware law, the reasonable commercial expectations of the parties, as set forth in the non-reliance disclaimer clauses in Paragraph 7 and the waiver provisions in Paragraph 8 of the NDA, must be enforced. Accordingly, the Superior Court properly granted Savage's motion to dismiss RAA's Complaint.

12. REMEDIES

Recipient agrees to indemnify and hold Discloser and its Shareholders[, and Discloser's Representatives,] harmless from any damages, loss, cost or liability (including legal fees and the cost of enforcing this indemnity) arising out of or resulting from any disclosure by Recipient or

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[22] 45 A3d 107 (Del. 2012).

Recipient's Representatives of the Confidential Information other than as expressly permitted by this agreement. In addition, because an award of money damages (whether pursuant to the foregoing sentence or otherwise) would be inadequate for any breach of this agreement by Recipient or Recipient's Representatives, and any such breach would cause Discloser irreparable harm, Recipient also agrees that, in the event of any breach or threatened breach of this agreement, Discloser will also be entitled, without the requirement of posting a bond or other security, to equitable relief, including injunctive relief and specific performance. Such remedies will not be the exclusive remedies for any breach of this agreement but will be in addition to all other remedies available at law or equity to Discloser.

COMMENT

The Discloser wants the Recipient to acknowledge its right to injunctive relief in order to facilitate the Discloser's obtaining an injunction if it is the Discloser's best remedy. The Recipient may object to the legal fees provision, and perhaps an intermediate position is to provide that the prevailing party receives its legal fees reimbursed. The Discloser may also want to add the bracketed phrase to include its Representatives among the indemnitees if they are at risk for any of the kinds of matters covered by this section.

13. ATTORNEY-CLIENT PRIVILEGE

Discloser is not waiving, and will not be deemed to have waived or diminished, any of its attorney work product protections, attorney client privileges, or similar protections and privileges as a result of disclosing its Confidential Information (including Confidential Information related to pending or threatened litigation) to the Recipient, regardless of whether the Discloser has asserted, or is or may be entitled to assert, such privileges and protections. The parties (a) share a common legal and commercial interest in all of the Discloser's Confidential Information that is subject to such privileges and protections, (b) are or may become joint defendants in Proceedings to which the Discloser's Confidential Information covered by such protections and privileges relates, (c) intend that such privileges and protections remain intact should either party become subject to any actual or threatened Proceeding to which the Discloser's Confidential Information covered by such protections and privileges relates, and (d) intend that after the Closing the Recipient shall have the right to assert such protections and privileges. No Recipient shall admit, claim or contend, in Proceedings involving either party or otherwise, that any Discloser waived any of its attorney work product protections, attorney client privileges, or similar protections and privileges with respect to any information, documents or other material not disclosed to a Recipient due to the Discloser disclosing its Confidential Information (including Confidential Information related to pending or threatened litigation) to the Recipient.

COMMENT

One of the more troublesome problems related to the disclosure of Confidential Information during the due diligence process is how to disclose certain information to the Recipient to facilitate a meaningful evaluation of litigation related Confidential Information without waiving any work product protections, attorney client privileges, and similar protections and privileges. The language of Section

13 above mirrors Section 12.6 of the Model Asset Purchase Agreement and constitutes an attempt to allow the seller to furnish to the buyer Confidential Information without waiving the seller's work product, attorney client privilege and similar protections by demonstrating that the buyer and seller have or should be presumed to have common legal and commercial interests, or are or may become joint defendants in litigation. *See* the Comment to Section 12.6 of the Model Asset Purchase Agreement for the basis and effect of Section 13.

14. MISCELLANEOUS

COMMENT

The following miscellaneous provisions are similar to those under Article 13 of the Model Asset Purchase Agreement and are subject to the comments under that Article for discussion of issues and considerations in using these provisions.

(a) *Modification*. This agreement and the agreements set forth in this agreement may be modified or waived only by a separate writing signed by Discloser and Recipient expressly modifying or waiving this agreement orsuch agreements.

(b) *Waiver*. Neither the failure nor any delay by any party in exercising any right, power or privilege under this agreement will operate as a waiver of such right, power or privilege, and no single or partial exercise of any such right, power or privilege will preclude any other or further exercise of such right, power or privilege or the exercise of any other right, power or privilege.

(c) *Person*. The term **"person"** means any individual, corporation (including any nonprofit corporation), general or limited partnership, limited liability company, joint venture, estate, trust, association, organization, labor union or other entity or governmental body.

(d) *Severability*. The invalidity or unenforceability of any provision of this agreement shall not affect the validity or enforceability of any other provisions of this agreement, which shall remain in full force and effect. If any of the covenants or provisions of this agreement are determined to be unenforceable by reason of its extent, duration, scope or otherwise, then the parties contemplate that the court making such determination shall reduce such extent, duration, scope or other provision and enforce them in their reduced form for all purposes contemplated by this agreement.

(e) *Costs*. Recipient agrees that if it is held by any court of competent jurisdiction to be in violation, breach or nonperformance of any of the terms of this agreement, then it will promptly pay to Discloser all costs of such action or suit, including reasonable attorneys' fees.

(f) *Section Headings, Construction*. The headings of Sections in this agreement are provided for convenience only and will not affect its construction or interpretation. All references to **"Section"** or **"Sections"** refer to the corresponding Section or Sections of this agreement unless otherwise specified. All words used in this agreement will be construed to be of such gender or number as the circumstances require. Unless otherwise expressly provided, the word **"including"** does not limit the preceding words or terms.

(g) *Jurisdiction; Service of Process*. Any action or proceeding seeking to enforce any provision of, or based upon any right arising out of, this agreement may be brought against either of the parties in the courts of the State of ______ County of ______, or, if it has or can acquire jurisdiction, in the United States District Court for the ______, District of ______, and each of the parties consents to the jurisdiction of such courts (and of the appropriate appellate courts) in any such action or proceeding and waives any objection to venue laid therein. Process in any action or proceeding referred to in the preceding sentence may be served on any party anywhere in the world.

(h) *Governing Law*. This agreement will be governed by the laws of the State of ______ without regard to conflicts-of-laws principles.

(i) *Execution of Agreement*. This agreement may be executed in one or more counterparts, each of which will be deemed to be an original copy of this agreement, and all of which, when taken together, shall be deemed to constitute one and the same agreement. The exchange of copies of this agreement and of signature pages by facsimile transmission shall constitute effective execution and delivery of this agreement as to the parties and may be used in lieu of the original agreement for all purposes. Signatures of the parties transmitted by facsimile shall be deemed to be their original signatures for any purpose whatsoever.

[consider adding the following, if appropriate]

(j) *Construction*. The parties have participated jointly in the negotiation and drafting of this agreement. If an ambiguity or question of intent or interpretation arises, this agreement shall be construed as if drafted jointly by the parties and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any of the provisions of this agreement.

If you are in agreement with the foregoing, please sign and return one copy of this agreement, which thereupon will constitute our agreement with respect to its subject matter.

Very truly yours,

[Discloser's Name]

By:_______________
Name:
Its:

DULY EXECUTED and agreed to on _____ _____, 20_____.

[Recipient's Name]

By:_______________
Name:
Its:

APPENDIX B

LETTER OF INTENT

PRELIMINARY NOTE

A letter of intent is often entered into between a buyer and a seller as a result of the successful completion of the first phase of negotiations of an acquisition transaction. The letter generally, but not always, describes the purchase price or a formula to be used to determine the purchase price and certain other key economic and procedural terms that form the basis for further negotiations. A buyer and seller fully expect that the letter of intent will be superseded by a definitive written acquisition agreement.

There are several reasons why letters of intent are used. Both a buyer and seller frequently prefer a letter of intent to test the waters for the prospects of a definitive agreement before incurring the costs of negotiating a definitive agreement and performing, or permitting to be performed, an acquisition review of the target company. The parties may also feel morally, if not legally, obligated to key terms if those terms are set down in writing. Sometimes the purchase price is sufficiently complicated that it is helpful to describe it in writing to ensure that the buyer and the seller have consistent expectations.

Signing a letter of intent early on, rather than waiting for the definitive agreement, often facilitates compliance with regulatory requirements. For example, a premerger notification report can be filed under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 upon entering into a letter of intent, thereby starting the clock on the applicable waiting period. A signed letter of intent may also assist the buyer in convincing some lenders to evaluate the transaction for the purpose of providing financing. The letter of intent often provides a format for the transaction, which can be used as the basis for drafting the definitive agreement. Announcements to customers, suppliers and employees about the potential transaction are frequently triggered by the signing of a letter of intent.

Letters of intent are also used to regulate the rights and obligations of the parties while a definitive agreement is being negotiated. For example, a “no-shop” provision is often included preventing a seller from negotiating with another party while negotiations with a buyer are ongoing. A letter of intent generally permits a buyer to inspect the target company’s assets and to review its operations and books and records while simultaneously prohibiting a buyer from disclosing or using in competition with the target company trade secrets and other proprietary information disclosed by the target company to a buyer during the negotiations. A letter of intent often covers how expenses of the acquisition and negotiations, such as brokers’ fees and fees and expenses of attorneys and other advisors, will be paid and limits the rights of each party to publicize the acquisition or negotiations without the consent of the other party. Frequently, a letter of intent will establish the time frame for closing the acquisition and, sometimes, certain other milestones prior to the closing.

Many commentators and business lawyers believe that letters of intent generally are more favorable to a buyer than to a seller. A signed letter of intent, even if not binding, together with a

buyer's inspection of the target company's assets and review of its operations and books and records, often will place a seller at a negotiating disadvantage in that there may be an expectation on the part of the target company's employees, vendors, customers, lenders and investors of a sale to a buyer. A buyer's investigation of the target company may also uncover information that can be used by a buyer to compete with the target company if the sale is not consummated, even if the target company receives protection against the disclosure or use by a buyer of the target company's trade secrets and other proprietary information. A no-shop provision in the letter of intent may prevent a seller from introducing other interested parties to the acquisition to enhance its negotiating position with a buyer. In those cases where a letter of intent is not to be used, the buyer should consider entering into a stand-alone no-shop agreement with the seller.

Notwithstanding these considerations, sellers are often as insistent as buyers that a letter of intent be executed before work on a definitive agreement is begun. One reason for a seller's insistence on a letter of intent may be that the negotiation of a letter of intent provides a seller with an excellent opportunity to negotiate certain key acquisition issues at a time when a seller possesses maximum leverage.

Although letters of intent are common, no consensus exists among business lawyers regarding their desirability. Many lawyers advise their clients that the great disadvantage of a letter of intent is that provisions intended by the parties to be nonbinding may be later found by a court to be binding. Also, there is often an inherent conflict between the goals of the parties in negotiating a letter of intent. A buyer generally is most interested in securing a no-shop commitment and other standstill or exclusive negotiating types of provisions (often called ***"exclusivity provisions"***) from the seller, and seeks to maintain great flexibility regarding the purchase price and other key provisions that may be impacted by the results of a buyer's acquisition review of the target company. A buyer often seeks to have the exclusivity provisions incorporated in the letter of intent or in a separate agreement entered into early in the discussions. A seller, on the other hand, generally will attempt to define more clearly the purchase price, limitations on its exposure with respect to the representations and warranties that will be part of the definitive agreement, and key terms of employment agreements, noncompete covenants and other ancillary arrangements. If possible, a seller will prefer to avoid altogether or to limit the scope of any exclusivity commitment. The negotiation of a letter of intent sometimes becomes bogged down in detailed discussions that are generally reserved to the negotiation of the definitive agreement. Because of these twin concerns of the possible, but unintended, binding nature of the letter of intent and the risk that the negotiation of the letter of intent will become bogged down in endless detail, lawyers often advise their clients to forgo a letter of intent and commence negotiations with respect to a definitive acquisition agreement.

Whether or not a letter of intent should be binding can be a matter of great importance, and it is important that the lawyer understand the client's desires in this regard. For example, the acquisition may be so economically or strategically attractive that the client is willing, as a business decision, to be bound at this initial stage. The parties might also intend to be bound if the acquisition review has been completed and all economic issues have been settled. Clients must be made aware, however, that a fully binding letter of intent can lead to problems and unexpected results if the parties later are unable to agree to the terms of a definitive agreement. In that event, a court may impose upon the parties its interpretation of commercially reasonable terms for any unresolved issues.

The legal principles for when a letter of intent is binding are fairly easy to state:

(a) If the parties intend *not to be bound* to each other prior to the execution of a definitive agreement, the courts will give effect to that intent and the parties will not be bound until the agreement has been executed. This is true even if all issues in the negotiations have been resolved.[23]

(b) On the other hand, if the parties intend to be bound prior to the execution of a definitive agreement, the courts will also give effect to that intent and the parties will be bound even though they contemplate replacing their earlier understanding with the definitive agreement at a later date.[24] Whether the parties intended to be and are bound by an oral agreement is a question of fact.[25]

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23 *See R. G. Group, Inc. v. Horn & Hardart Co.*, 751 F.2d 69 (2d Cir. 1984); *V'Soske v. Barwick*, 404 F.2d 495 (2d Cir. 1968); *but see Patriot Rail Corp. v. Sierra Railroad Company*, 2011 WL 318400 (E.D. Cal. Feb. 1, 2011) (under California law although the letter of intent contained language providing that it was non-binding, the Court held that the letter of intent included an implied covenant that buyer have the intent to purchase the target; the implied covenant of good faith and fair dealing could be violated by the buyer entering into the letter of intent and receiving confidential information if it did not have a good faith intent to acquire the target). *EQT Infrastructure Limited v. Smith*, 861 F. Supp. 2d 220 (S.D.N.Y. 2012) (under duty of good faith and fair dealing implied in New York contracts, seller liable to buyer for adding condition that was not in letter of intent that seller succeed in selling unrelated business); *see* RESTATEMENT (SECOND) OF CONTRACTS § 205. Duty of Good Faith and Fair Dealing (every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement); *but cf Cole v. Hall*, 864 S.W.2d 563 (Tx. Ct. App Dallas 1993 (Texas does not recognize implied duty of good faith and fair dealing except for certain special relationships, such as those between insurer and insured, principal and agent, joint ventures and partnerships).

24 *See Texaco, Inc. v. Pennzoil Co.*, 729 S.W.2d 768 (Tex. Ct. App. 1987), *cert. denied*, 485 U.S. 994 (1988), *but see Durbin v. Dal-Briar Corp.*, 871 S.W.2d 263 (Tex. App. 1991); *cf. Isern v. Ninth Court of Appeals*, 925 S.W.2d 604 (Tex. 1996) (superseded by statute), *cert. denied*, *Watson v. Isern*, 117 S. Ct. 612 (1996); *R. G. Group*, 751 F.2d at 74; *V'Soske*, 404 F.2d at 500.

25 In *Turner Broadcasting System, Inc. v. McDavid*, 2010 WL 1136274 (Ga. Ct. App. Mar. 26, 2010), a $281 million verdict for breach by Turner Broadcasting System, Inc. ("Turner") of an oral agreement to sell certain assets to David McDavid ("McDavid") was upheld. In November 2002, Turner and McDavid began negotiating the sale of two sports teams, and on April 30, 2003, the parties signed a letter of intent, which outlined the proposed terms and provided for a 45-day exclusive negotiating period. The letter of intent stated, among other things, that "neither party ... [would] be bound ... unless and until such party . . . has executed the Definitive Agreements." The letter of intent expired at the end of the exclusivity period, with only the confidentiality provisions stated to survive. The parties continued to negotiate. McDavid asked Turner about extending the letter of intent, but was told there was no need because they were "very, very close to a deal." Throughout the summer, the parties engaged in negotiations to address remaining outstanding issues.

In August, the parties worked to draft the purchase agreement and exhibits and identified "open issues," Turner drafted a memo to its employees, prepared for a press conference to announce the deal, and consulted with McDavid on management decisions for the business to be acquired. In mid-August, Turner proposed a simplified structure for the transaction, to which McDavid agreed, based on assurances that it would not change the deal and that Turner was "ready to close on the deal . . . made on July 30th." On August 19, the board of directors of Turner's parent company approved the McDavid deal.

On August 20, another bidder expressed an interest in purchasing the assets from Turner, and negotiations with the second bidder commenced.

On September 12, Turner and McDavid "verbally reached a final agreement" on the remaining open items and Turner's principal negotiator announced that "[t]he deal is done. Let's get documents we can sign...."

(c) Parties intending to be bound prior to the execution of a definitive agreement will be bound even if there are certain issues that have not been resolved. Depending upon the importance of the open items, the courts will either supply commercially reasonable terms for those unresolved issues or impose a contractual duty on the parties to negotiate the resolution of those issues in good faith.[26]

That same day, however, Turner signed an agreement with the second bidder. Three days later, Turner informed McDavid that Turner had sold the assets to another buyer. McDavid subsequently filed suit for breach of an oral contract and promissory estoppel.

After an 8-week trial, the jury found for McDavid on the breach of oral contract claim, rejecting Turner's argument that the parties had not executed a final purchase agreement or agreed to all essential terms. On appeal, the Court noted that the determination as to whether an oral contract existed presented issues of fact for the jury, and held that there was sufficient evidence to support the verdict.

The Court noted that whether there was mutual assent to a contract was determined pursuant to an "objective theory," with a party's intent deemed to be "that meaning a reasonable man in the position of the other contracting party would ascribe to the first party's manifestation of assent, or that meaning which the other contracting party knew the first party ascribed to his manifestations of assent."

The Court held that evidence of the parties' expressions and conduct supported a conclusion that each intended to be bound to the deal, including statements made by Turner representatives that "we have a deal" and "the deal is done" and Turner's internal memo to employees, preparations for a press conference to announce the deal, and consultation with McDavid on management decisions.

The Court acknowledged the letter of intent's express disclaimer to the effect that the parties would not be bound absent a written, signed definitive agreement, but found that the letter of intent also provided for expiration on June 14 of all terms other than the confidentiality terms, including the provision that the parties would be bound only by a definitive written agreement," which request suggested that an oral agreement was "not precluded."

Although it was clear that the parties intended to sign written agreements documenting the terms of their oral agreement, the Court held that the failure to sign such written agreements did not affect the validity of the oral agreement itself. While the contemplation of a subsequent written contract served as "strong evidence that [the parties] did not intend to be bound by a preliminary agreement," the jury was authorized to find the existence of a binding oral contract based on conflicting evidence of the parties' intent. The Court focused on the merger clause contained in the draft agreements circulated among the parties and their legal counsel, which provided that the written agreement would "supersede all prior agreements, understandings and negotiations, both written and oral," and stated that such language could be viewed as an acknowledgment of the possibility of a previous oral agreement.

In rejecting Turner's argument that contracts pertaining to "complex, expensive business matters" should be enforceable only if in writing, the Court commented that the statute of frauds explicitly sets forth which contracts fall within its purview and that the contract at issue is not included therein.

It is significant that Turner was held to be bound by an oral agreement with McDavid, despite the language in the earlier letter of intent and Turner's assertion of its continued intent not to be bound except by written agreement. The question of whether the parties have mutually assented to an oral agreement is a question of fact, which emphasizes the importance of properly memorializing or expressing the intent to be bound only by written agreement. The fact that the letter of intent explicitly provided for survival of its confidentiality provisions, but not the writing requirement, following its expiration undermined Turner's position that the written agreement requirement was meant to continue in effect throughout negotiations.

The Court's statement that the merger clause in the draft agreements could be construed as recognition that an oral contract may exist prior to the execution of a definitive agreement is troubling, as was the Court's imposition of a "best efforts" obligation to fulfill the conditions to closing.

[26] *See Itek Corp. v. Chicago Aerial Indus.*, 248 A.2d 625 (Del. 1968).

(d) Documents disseminated by an investment banker as part of an auction process can affect the contractual rights of the parties even though none of the parties signed them.[27]

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[27] *See WTG Gas Processing, L.P. v. ConocoPhillips Co.*, 309 S.W.3d 635 (Tex. App.—Houston [14th Dist.] March 2, 2010), which arose from ConocoPhillips sale of a natural-gas processing facility to Targa Resources instead of WTG Gas Processing, L.P. WTG sued ConocoPhillips for breach of contract, fraud and negligent misrepresentation and Targa for tortious interference with contract or prospective business relationship. The trial court granted separate motions for summary judgment filed by ConocoPhillips and Targa and signed a final judgment that WTG take nothing on all its claims.

ConocoPhillips decided to sell several of its natural gas processing plants and pipelines and engaged Morgan Stanley to conduct the sale. Morgan Stanley issued a "teaser," inviting interested parties to potentially bid on individual assets or certain assets combined. After WTG signed a confidentiality agreement, Morgan Stanley gave WTG a confidential information memorandum, which described the assets in more detail and outlined the progressive steps of the transaction process: interested parties submit a non-binding indication of interest ("IOI") containing requisite items; Morgan Stanley and ConocoPhillips would evaluate the IOIs and invite a limited number of bidders to attend a management presentation, participate in due diligence, receive further information, including a draft purchase and sale agreement ("PSA"), and attend a site visit from which to submit bids; and upon evaluation of the final bids, Morgan Stanley would narrow the number of bidders and enter into final PSA negotiations. The confidential information memorandum also provided in pertinent part:

> Morgan Stanley and ConocoPhillips reserve the right to . . . negotiate with one or more parties at any time and . . . enter into preliminary or definitive agreements at anytime and without notice or consultation with any other parties. Morgan Stanley and ConocoPhillips also reserve the right, in their sole discretion, to reject any and all final bids without assigning reasons and to terminate discussions and/or negotiations at any time for any reason or for no reason at all.

After submitting an IOI for one of the pipelines, WTG was invited to, and did, participate in the next stage of the process. Then Morgan Stanley invited WTG to submit a binding proposal and outlined the requirements for such a bid ("the bid procedures"). The proposal was required to include ConocoPhillips's draft PSA marked by WTG to show its proposed changes. Among other provisions, the bid procedures contained the following language:

- A Proposal will only be deemed to be accepted upon the execution and delivery by ConocoPhillips of a [PSA].
- [ConocoPhillips] expressly reserves the right, in its sole discretion and at any time and for any reason, to exclude any party from the process or to enter into negotiations or a [PSA] with any prospective purchaser or any other party . . . and to reject any and all Proposals for any reason whatsoever . . . . [ConocoPhillips] also expressly reserves the right to negotiate at any time with any prospective purchaser individually or simultaneously with other prospective purchasers . . . . None of ConocoPhillips, its affiliates, representatives, related parties or Morgan Stanley will have any liability to any prospective purchaser as a result of the rejection of any Proposal or the acceptance of another Proposal at any time.
- Until the [PSA] for this transaction is executed by ConocoPhillips and a purchaser, [ConocoPhillips], its affiliates and related parties shall not have any obligations to any party with respect to the contemplated transaction, and following such execution and delivery, the only obligations of ConocoPhillips, its affiliates and related parties will be to the other party to the [PSA], and only as set forth therein.

WTG submitted a "final binding bid." Subsequently WTG increased its bid after being informed that its offer was lower than others under consideration, but that ConocoPhillips was more comfortable with WTG because of fewer changes needed to its PSA and the parties' past relationship. WTG was then informed by Morgan Stanley that it likely would be the winning bidder if it increased its bid to a specified amount to make it comparable to another offer ConocoPhillips was considering, and WTG increased its bid accordingly.

Morgan Stanley thereafter telephoned WTG stating that ConocoPhillips had decided to "go forward with" WTG; ConocoPhillips and WTG had a "deal"; ConocoPhillips had some "immaterial" changes—"wording" issues—to WTG's draft PSA; the parties would "proceed to get it signed"; and ConocoPhillips would forward a revised version of the PSA. At that point, WTG's draft PSA was not in executable form as it did not fully describe the assets to be purchased or include all exhibits. WTG and ConocoPhillips did not thereafter engage in any negotiations relative to a PSA, ConocoPhillips made no counter proposal, and the parties never executed a PSA.

Meanwhile, Targa had submitted bids for multiple assets and expressed a strong preference to make a group purchase. At that point, although Targa's single bid was higher than the total separate offers, ConocoPhillips viewed the separate sales as more optimal than a package sale to Targa. Thereafter, Targa submitted another bid and made some concessions on terms in light of ongoing discussions with Morgan Stanley. Morgan Stanley forwarded this proposal to ConocoPhillips, noting it was a total premium of $22 million over the existing offers. ConocoPhillips indicated to Morgan Stanley that this offer had potential if the parties could negotiate other details.

Morgan Stanley informed WTG that ConocoPhillips was considering another offer. In response to e-mail from WTG regarding its plans to conduct the due diligence, ConocoPhillips confirmed to WTG that ConocoPhillips was considering another offer and a decision about the new bid would not likely be made for perhaps another month.

For the ensuing two months, ConocoPhillips negotiated with Targa. During this period, WTG, ConocoPhillips and Morgan Stanley continued to communicate regarding the status of the sale, and WTG periodically apprised them regarding the status of WTG's due diligence efforts, while they kept WTG informed that ConocoPhillips was still evaluating the other offer.

Morgan Stanley then notified WTG that due diligence should be conducted at WTG's own risk and reminded WTG the bid materials advised that ConocoPhillips could negotiate with any party until a PSA was signed. After WTG informed ConocoPhillips and Morgan Stanley that once certain aspects of due diligence were complete, WTG would be prepared to "finalize and sign" a PSA, Morgan Stanley advised WTG that negotiations with the other party were down to the "critical stage," but ConocoPhillips wanted to keep communications open with WTG as a "good alternative."

After ConocoPhillips and Targa executed a PSA, WTG sued ConocoPhillips for breach of contract, fraud and negligent misrepresentation and Targa for tortious interference with contract or prospective business relationship. ConocoPhillips and Targa each filed a traditional motion for summary judgment, which the trial court granted.

Although a PSA was never executed, WTG contended ConocoPhillips accepted WTG's offer during the phone conversation by saying that ConocoPhillips had decided to "go forward with" WTG, they had a "deal," ConocoPhillips had "immaterial" changes to WTG's PSA, and "the parties would "proceed to get it signed."

Based on the following provisions in the bid procedures, ConocoPhillips argued that these oral representations, if any, did not constitute acceptance of WTG's offer:

> A Proposal will only be deemed to be accepted upon the execution and delivery by ConocoPhillips of a [PSA].
>
> Until the [PSA(s)] for this transaction is executed by ConocoPhillips and a purchaser, [ConocoPhillips] . . . shall not have any obligations to any party with respect to the contemplated transaction, and following such execution and delivery, the only obligations of ConocoPhillips . . . will be to the other party to the [PSA(s)], and only as set forth therein.

In support of its contention that the above-cited bid procedures negated any purported acceptance of WTG's offer, ConocoPhillips cited several cases to the effect that words in a letter of intent to the effect that "does not address all of the terms and conditions which the parties must agree upon to become binding and consummated . . . that this letter is an expression of the parties' mutual intent and is not binding upon them except for the provisions of [several numbered paragraphs]" are sufficient to defeat a suitors' breach of contract claim. WTG in turn cited several cases to support its position that the fact the parties contemplated later execution of a written agreement did not necessarily preclude their informal agreement from constituting a binding contract.

When the courts impose a duty to negotiate open terms in good faith, the courts will impose liability if one party acts in bad faith.[28] On the other hand, if the parties do negotiate in good faith, the fact that a final agreement is not reached will not result in liability.[29]

In determining whether the parties intend to be bound, the courts generally examine the following factors:

(a) the actual words of the document;

In granting defendants' motion for summary judgment, the court found that the ConocoPhillips bid procedures were much more definitive than the "subject to legal documentation" language in cases cited by WTG and that the bid procedures unequivocally provided that ConocoPhillips did not intend to accept an offer, or bear any contractual obligations to another party, absent execution of a PSA. Thus, execution of a PSA was clearly a condition precedent to contract formation and not merely a memorialization of an existing contract. The court acknowledged that the provisions reflecting intent not to be bound in the letter of intent cases cited by defendants were contained in a written agreement signed by both parties, and concluded that WTG accepted them by making its bid "[i]n accordance with the [CIM] . . . and the [bid procedures]."

Additionally, WTG argued "Texas jurisprudence allows parties to orally modify a contract even if the contract itself contains language prohibiting oral modification, if parties agree to disregard this language," and that a party may waive a condition it originally imposed as prerequisite to contract formation. The court concluded the oral representations were insufficient as a matter of law to constitute waiver of the bid procedures at issue because allowing a jury to decide the oral representations alone constituted waiver would vitiate the purpose of the overall bid process and the procedures, which provided that one of ConocoPhillips's "key objectives" was "to obtain the highest possible value" and it would evaluate proposals "with the goal of negotiating and executing a [PSA(s)] with the party that submits the Proposal which best meets [ConocoPhillips's] objectives."

Both the offering memorandum and the bid procedures demonstrated they were intended to ensure that ConocoPhillips achieved its objectives by prescribing an aggressive, competitive bidding process. ConocoPhillips reserved the right to pursue the most favorable bid until execution of a PSA by specifying it could entertain a bid at any time, negotiate with any prospective purchaser at any time, and negotiate with multiple parties at the same time.

The court noted that arriving at the final terms of a complex, commercial transaction involves extensive time, effort, research, and finances, and that parties to a complex transaction may need to reach a preliminary agreement in order to proceed toward execution of a final agreement. Consequently, parties may structure their negotiations so that they preliminarily agree on certain terms, yet protect themselves from being prematurely bound in the event they disagree on other terms.

Accordingly, the court found that the bid procedures at issue were intended in part to prevent an informal, preliminary agreement with a prospective purchaser from forming a binding contract before execution of the formal writing and held that representations during a phone conversation cannot alone constitute waiver of the bid procedures and acceptance of WTG's offer when the bid procedures were implemented partly to prevent such representations from constituting acceptance of an offer.

Targa's claims for tortious interference with contract likewise failed. The court noted: "The elements of tortious interference with contract are (1) existence of a contract subject to interference, (2) willful and intentional interference, (3) interference that proximately caused damage, and (4) actual damage or loss." Because it had concluded there was no contract between WTG and ConocoPhillips, the court held that, as a matter of law, Targa is not liable for tortious interference.

[28] *See Bruce V. Marcheson Implementos E. Maquinos Agriculas Tatu, S.A.* (Civil No. 87-774-A S.D. Iowa 1990), *modified*, *Bruce v. Marcheson Implementos E. Maquinos Agriculas Tatu, S.A.* (Civil No. 87-774-S S.D. Iowa 1991); *Fickes v. Sun Expert, Inc.*, 762 F. Supp. 998 (D. Mass. 1991).

[29] *See Feldman v. Allegheny Int'l, Inc.*, 850 F.2d 1217 (7th Cir. 1988); *Copeland v. Baskin Robbins U.S.A.*, 117 Cal. Rptr. 2d 875 (Cal. App. 2002).

(b) the context of the negotiations;

(c) whether either or both parties have partially performed their obligations;

(d) whether there are any issues left to negotiate; and

(e) whether the subject matter of the discussions concerns complex business matters that customarily involve definitive written agreements.[30]

Courts have consistently stated that the most important factor in determining whether or which provisions in a letter of intent are binding is the language used by the parties in the document. The language of the letter of intent should, therefore, be definite and precise. The lawyer should advise the client, however, to avoid factual situations that have led some courts to find provisions of a letter of intent to be binding despite language seemingly to the contrary in the document. There are many things that can overcome the words in a letter of intent purporting to make a document or certain provisions in a document nonbinding. Oral communications and other actions are often given great weight by courts in interpreting the intent of the parties. Oral statements such as "Looks like we have a deal!" or handshakes can indicate an intent to be bound.[31]

Most letters of intent are intended to be at least partially binding. A buyer may be reluctant to enter into a letter of intent unless it secures a binding promise from a seller that restricts a seller's ability to "shop" the target company for some period of time.[32] Unless a confidentiality agreement is already in place, a seller will want a buyer to be bound to a nondisclosure obligation.

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30 *See Teachers Ins. and Annuity Ass'n v. Tribune Co.*, 670 F. Supp. 491 (S.D.N.Y. 1987); *Arcadian Phosphates, Inc. v. Arcadian Corp.*, 884 F.2d 69 (2d Cir. 1989); *Texaco*, 729 S.W.2d at 768; *R. G. Group*, 751 F.2d at 75.

31 *See American Cyanamid Co. v. Elizabeth Arden Sales Corp.*, 331 F. Supp. 597 (S.D.N.Y. 1971); *Computer Sys. of Am., Inc. v. IBM Corp.*, 795 F.2d 1086 (1st Cir. 1986). *But see Reprosystem, B. V. v. SCM Corp.*, 727 F.2d 257 (2d Cir. 1984), *cert. denied*, 469 U.S. 828 (1984); *R. G. Group*, 751 F.2d at 75-76.

32 *See Global Asset Capital, LLC vs. Rubicon US REIT, Inc.*, C.A. No. 5071-VCL (Del. Ch. Nov. 16, 2009), in which in the context of explaining why he granted a temporary restraining order enjoining the target and its affiliates from disclosing any of the contents of a letter of intent or soliciting or entertaining any third-party offers for the duration of the letter of intent, Delaware Vice Chancellor Laster wrote:

> [I]f parties want to enter into nonbinding letters of intent, that's fine. They can readily do that by expressly saying that the letter of intent is nonbinding, that by providing that, it will be subject in all respects to future documentation, issues that, at least at this stage, I don't believe are here. I think this letter of intent is binding . . . [A] no-shop provision, exclusivity provision, in a letter of intent is something that is important. . . . [A]n exclusivity provision or a no-shop provision is a unique right that needs to be protected and is not something that is readily remedied after the fact by money damages. . . . [C]ontracts, in my view, do not have inherent fiduciary outs. People bargain for fiduciary outs because, as our Supreme Court taught in Van Gorkom, if you do not get a fiduciary out, you put yourself in a position where you are potentially exposed to contract damages and contract remedies at the same time you may potentially be exposed to other claims. Therefore, it is prudent to put in a fiduciary out, because otherwise, you put yourself in an untenable position. That doesn't mean that contracts are options where boards are concerned. Quite the contrary. And the fact that equity will enjoin certain contractual provisions that have been entered into in breach of fiduciary duty does not give someone carte blanche to walk as a fiduciary. . . . I don't regard fiduciary outs as inherent in every agreement.").

It is important for a client to have its lawyer's advice at the outset if the client contemplates entering into a letter of intent. The issue of whether and what parts of the letter of intent should be binding or nonbinding and the risks of entering into a letter of intent at all are important aspects for a client to understand. The level of detail in the letter of intent and which issues should be confronted or deferred are key strategic questions that should be discussed with the client, and their likely impact on the negotiation of the acquisition should be fully explored. In addition, public companies may have disclosure requirements under the federal securities laws that are triggered at some point in the negotiations, perhaps even before a letter of intent is concluded.

The sample Letter of Intent contemplates the proposed acquisition by a single corporate buyer of substantially all of the assets of a privately held company, which is an S corporation with eight individual stockholders, two of whom own ninety percent of its outstanding capital stock. The purchase price would be payable with a combination of cash, notes and the assumption of certain liabilities and obligations. This Fact Pattern is consistent with the Fact Pattern that serves as the basis for the Model Asset Purchase Agreement.

The Letter of Intent has been prepared as Buyer's reasonable first draft, recognizing the custom that a buyer or its counsel will generally prepare the first draft of a letter of intent. There is a broad range of what may be considered reasonable; the Letter of Intent tends toward the buyer-favorable end of that range.

The Letter of Intent is divided into two parts: provisions intended not to be binding and provisions intended to be binding. The nonbinding provisions consist primarily of the "deal points," such as a description of the proposed transaction, the purchase price, key ancillary agreements and important conditions. The binding provisions focus on the regulation of the negotiation process, including access for the Buyer to conduct its acquisition review, no-shop restrictions and break-up fees, nondisclosure obligations, procedures for making public announcements, payment of the parties' expenses and termination provisions. The non-binding and binding portions of the Letter of Intent are clearly delineated to assist a court in determining the intent of the parties, if that becomes necessary. Another, more common practice that also works well is to set out binding and nonbinding provisions without grouping them in separate parts and to include a general statement that the entire letter of intent is nonbinding, except for certain provisions which are then specifically itemized.

Letters of intent that are shorter and more informal than the sample Letter of Intent can also be effective, and many clients prefer a less-comprehensive approach. The primary advantages of a comprehensive letter of intent, like the sample Letter of Intent, are (a) issues that are "deal-breakers" can be identified early in the negotiation process before substantial expenses are incurred in acquisition review and the drafting of a definitive agreement with accompanying disclosure letter or schedules, and (b) resolution of difficult issues at the letter of intent stage can make the negotiation of a definitive agreement considerably easier, permitting the buyer more time and energy to prepare for the transition to its ownership of the company. The primary disadvantage of a comprehensive letter of intent is that it may burden the negotiations with too many difficult issues

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But see Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 51 (Del. 1994) (noting that a board cannot "contract away" its fiduciary duties); *ACE Ltd. v. Capital Re Corp.*, 747 A. 2d 95, 107-08 (Del. Ch. 1999).

too early in the process and may damage the deal's momentum or even cause a breakdown in the negotiations that may have been avoided if more issues had been deferred until a later time. The lawyer and the client should discuss the strategic impact of a comprehensive letter of intent on the negotiating dynamics of a deal before a letter of intent based upon the sample Letter of Intent is prepared.

The confidentiality provision set forth in paragraph 9 of the Letter of Intent has been presented in the alternative in order that Buyer might either preserve an acceptable confidentiality agreement previously entered into by the parties (such as, for example, the Model Confidentiality Agreement set forth elsewhere herein) or, in the event that no such agreement has been entered into or that any such existing agreement is deemed unacceptable by Buyer's counsel, set forth a substantive "short-form" confidentiality provision. The substantive confidentiality provision might be useful to a buyer under circumstances where a prior confidentiality agreement was entered into by the buyer without the knowledge and/or review of the buyer's counsel. On the other hand, the seller may be unwilling to relinquish the protections of a "full-blown" confidentiality agreement, especially after one has already been signed. Therefore, although it is unusual for confidentiality provisions to be heavily negotiated as part of a Letter of Intent, it would not be irrational for provisions similar to those contained in either the Confidentiality Agreement (see Appendix A) or Article XII of the Model Asset Purchase Agreement to find their way into the Letter of Intent.

In light of the multitude of considerations that are part of negotiating a letter of intent, it cannot be overemphasized that virtually everything in a letter of intent is subject to variation based upon the particular context of the proposed acquisition. There is no such thing as a standard letter of intent applicable to all proposed acquisitions.

A. Form of Letter of Intent

______________, 20___

Company
[Address]

Re: Proposal to Purchase Assets of the Company

Dear [Chairman/President]:

This letter will confirm that Buyer is interested in acquiring substantially all of the assets of the Company, and assuming certain of its liabilities and obligations, on terms that would be mutually agreeable. In this letter, (a) Buyer and the Company are sometimes called singularly a "Party" and collectively the "Parties;" (b) the shareholders of the Company are sometimes called

the “Shareholders;” and (c) Buyer’s possible acquisition of the assets of the Company is sometimes called the “Possible Acquisition.”

[PART ONE]

The Parties wish to commence negotiating a definitive written acquisition agreement providing for the Possible Acquisition (a ***“Definitive Agreement”***). To facilitate the negotiation of a Definitive Agreement, the Parties request that Buyer’s counsel prepare an initial draft. The execution of any such Definitive Agreement would be subject to the satisfactory completion of Buyer’s ongoing investigation of the Company’s business and would also be subject to approval by Buyer’s board of directors.

Based upon the information currently known to Buyer, it is proposed that the Definitive Agreement include the following terms:

[BASIC TRANSACTION]

1. The Company would sell all of its operating assets, property, rights, good-will and business to Buyer at the price (the ***“Purchase Price”***) set forth in Paragraph 2 below. The closing of this transaction (the “Closing”) would occur as soon as possible after the termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the ***“HSR Act”***).

[PURCHASE PRICE]

2. The Purchase Price would be ______ dollars ($______) (subject to adjustment as described below) and would be paid in the following manner:

   (a) at the Closing, Buyer would pay the Company the sum of $______ in cash;

   (b) at the Closing, Buyer would deposit with a mutually acceptable escrow agent the sum of ______ dollars ($______), which would be held in escrow for a period of at least ______ (______) years in order to secure the performance of the Company’s obligations under the Definitive Agreement and related documents; and

   (c) at the Closing, Buyer would execute and deliver to the Company an unsecured, nonnegotiable, subordinated promissory note. The promissory note to be delivered to the Company by Buyer would have a principal amount of ______ dollars ($______), would bear interest at the rate of ______ percent (______%) per annum, would mature on the ______ (______) anniversary of the Closing, and would provide for ______ (______) equal [annual] [quarterly] payments of principal along with [annual] [quarterly] payments of accrued interest.

The Purchase Price assumes that the Company will transfer working capital at the Closing at least equal to ______ dollars ($______), its working capital as of its most recent balance sheet prior to execution of this letter. For this purpose, working capital shall be determined by subtracting current liabilities to be assumed (consisting of accounts and notes payable, accrued expenses, provisions for taxes and current maturity on long-term debt) from current assets to be

acquired (consisting of cash and cash equivalents, accounts receivable, inventory and pre-paid expenses). The Purchase Price would be increased or decreased based upon the amount by which the working capital transferred at the Closing exceeds or falls short of the initial working capital as reflected on the Company's most recent balance sheet on a dollar-for-dollar basis.

[EMPLOYMENT AND NONCOMPETITION AGREEMENTS]

3. At the Closing:

   (a) Buyer and A would enter into a ______-year (______-year) employment agreement under which A would agree to serve as Buyer's [Vice President and Chief Operating Officer] and would be entitled to receive a salary of ______ dollars ($______) per year; and(b) each Shareholder would execute a ______-year (______-year) noncompetition agreement in favor of Buyer.

[OTHER TERMS]

4. The Company and the Shareholders would make comprehensive representations and warranties to Buyer and would provide comprehensive covenants, indemnities and other protections for the benefit of Buyer. The consummation of the contemplated transactions by Buyer would be subject to the satisfaction of various conditions, including:

   (a) ____

   (b) ____

[PART TWO]

The following paragraphs of this letter (the "Binding Provisions") are the legally binding and enforceable agreements of Buyer, the Company and the Shareholders.

[ACCESS]

5. During the period from the date this letter is signed on behalf of the Company and the Shareholders (the "Signing Date") until the date on which either Party provides the other Party with written notice that negotiations toward a Definitive Agreement are terminated (the "Termination Date"), the Company will afford Buyer full and free access to the Company, its personnel, properties, contracts, books and records and all other documents and data, subject to the confidentiality provisions referred to or described in paragraph 9 of this letter.

[EXCLUSIVE DEALING]

6. Until the later of (a) [90] days after the Signing Date or (b) the Termination Date:

   (a) Neither the Company nor the Shareholders will, directly or indirectly, through any representative or otherwise, solicit or entertain offers from, negotiate with or in any manner encourage, discuss, accept or consider any proposal of any other person

relating to the acquisition of the Company, its assets or business, in whole or in part, whether directly or indirectly, through purchase, merger, consolidation or otherwise (other than sales of inventory in the ordinary course); and

(b) Either the Company or any Shareholder will, as the case may be, immediately notify Buyer regarding any contact between the Company, such Shareholder or their respective representatives and any other person regarding any such offer or proposal or any related inquiry.

[BREAK-UP FEE]

7. If (a) either the Company or any Shareholder breaches Paragraph 6 of this letter or the Company provides to Buyer written notice that negotiations toward a Definitive Agreement are terminated, and (b) within [six] months after the date of such breach or the Termination Date, as the case may be, either the Company or any Shareholder signs a letter of intent or other agreement relating to the acquisition of a material portion of the Company or its capital stock, assets or business, in whole or in part, whether directly or indirectly, through purchase, merger, consolidation or otherwise (other than sales of inventory or immaterial portions of the Company's assets in the ordinary course) and such transaction is ultimately consummated, then, immediately upon the closing of such transaction, the Company will pay to Buyer the sum ______ dollars ($______). This fee will not serve as the exclusive remedy to Buyer under this letter in the event of a breach by the Company or any Shareholder of Paragraph 6 of this letter or any other of the Binding Provisions, and Buyer will be entitled to all other rights and remedies provided by law or in equity.

[CONDUCT OF BUSINESS]

8. During the period from the Signing Date until the Termination Date, the Company shall operate its business in the ordinary course and refrain from any extraordinary transactions.

[CONFIDENTIALITY]

9. Except as expressly modified by the Binding Provisions, the Confidentiality Agreement entered into between the Company and Buyer on ______, 20______, shall remain in full force and effect.

or

9. Except as and to the extent required by law, Buyer will not disclose or use, and will direct its representatives not to disclose or use to the detriment of the Company, any Confidential Information (as defined below) with respect to the Company furnished, or to be furnished, by either the Company or the Shareholders or their respective representatives to Buyer or its representatives at any time or in any manner other than in connection with its evaluation of the transaction proposed in this letter. For purposes of this Paragraph, "Confidential Information" means any information about the Company stamped "confidential" or identified in writing as such to Buyer by the Company promptly following its disclosure, unless (a) such information is already known to Buyer or its representatives or to others not bound by a duty of confidentiality at the time of its disclosure or such information

becomes publicly available through no fault of Buyer or its representatives; (b) the use of such information is necessary or appropriate in making any filing or obtaining any consent or approval required for the consummation of the Possible Acquisition; or (c) the furnishing or use of such information is required by or necessary or appropriate in connection with legal proceedings. Upon the written request of the Company, Buyer will promptly return to the Company or destroy any Confidential Information in its possession and certify in writing to the Company that it has done so.

[DISCLOSURE]

10. Except as and to the extent required by law, without the prior written consent of the other Party, none of Buyer, the Company or its Shareholders will, and each will direct its representatives not to make, directly or indirectly, any public comment, statement or communication with respect to, or otherwise to disclose or to permit the disclosure of the existence of discussions regarding, a possible transaction between the Parties or any of the terms, conditions or other aspects of the transaction proposed in this letter. If a Party is required by law to make any such disclosure, it must first provide to the other Party the content of the proposed disclosure, the reasons that such disclosure is required by law, and the time and place that the disclosure will be made.

[COSTS]

11. Buyer and the Company will be responsible for and bear all of their respective costs and expenses (including any broker's or finder's fees and the expenses of its representatives) incurred at any time in connection with pursuing or consummating the Possible Acquisition. Notwithstanding the preceding sentence, Buyer will pay one-half and the Company will pay one-half of the HSR Act filing fee.

[CONSENTS]

12. During the period from the Signing Date until the Termination Date, Buyer and the Company will cooperate with each other and proceed, as promptly as is reasonably practical, to prepare and to file the notifications required by the HSR Act.

[ENTIRE AGREEMENT]

13. The Binding Provisions constitute the entire agreement between the Parties and supersede all prior oral or written agreements, understandings, representations and warranties and courses of conduct and dealing between the Parties on the subject matter thereof. Except as otherwise provided herein, the Binding Provisions may be amended or modified only by a writing executed by all of the Parties.

[GOVERNING LAW]

14. The Binding Provisions will be governed by and construed under the laws of the State of ______ without regard to conflicts-of-laws principles.

[JURISDICTION; SERVICE OF PROCESS]

15. Any action or proceeding seeking to enforce any provision of, or based on any right arising out of, the Binding Provisions may be brought against any of the Parties in the courts of the State of ______, County of ______, or, if it has or can acquire jurisdiction, in the United States District Court for the______ District of ______, and each of the Parties consents to the jurisdiction of such courts (and of the appropriate appellate courts) in any such action or proceeding and waives any objection to venue laid therein. Process in any action or proceeding referred to in the preceding sentence may be served on any Party anywhere in the world.

[TERMINATION]

16. The Binding Provisions will automatically terminate on ______, 20______, and may be terminated earlier upon written notice by either Party to the other Party unilaterally, for any reason or no reason, with or without cause, at any time, provided, however, that the termination of the Binding Provisions will not affect the liability of a Party for breach of any of the Binding Provisions prior to the termination. Upon termination of the Binding Provisions, the parties will have no further obligations hereunder, except as stated in Paragraphs 6, 7, 9, 10, 11, 13, 14, 15, 16 and 18, which will survive any such termination.

[COUNTERPARTS]

17. This letter may be executed in one or more counterparts, each of which will be deemed to be an original of this letter and all of which, when taken together, will be deemed to constitute one and the same letter.

[NO LIABILITY]

18. The provisions of paragraphs 1 through 4 of this letter are intended only as an expression of intent on behalf of Buyer, are not intended to be legally binding on Buyer, the Company or the Shareholders and are expressly subject to the execution of an appropriate Definitive Agreement. Moreover, except as expressly provided in paragraphs 5 through 18 (or as expressly provided in any binding written agreement that the Parties may enter into in the future), no past or future action, course of conduct or failure to act relating to the Possible Acquisition, or relating to the negotiation of the terms of the Possible Acquisition or any Definitive Agreement, will give rise to or serve as a basis for any obligation or other liability on the part of Buyer, the Company or the Shareholders.

If you are in agreement with the foregoing, please sign and return one copy of this letter, which thereupon will constitute our understanding with respect to its subject matter.

Very truly yours,

BUYER:

By: ____________________________________
Name: __________________________________
Title: __________________________________

Agreed to as to the Binding Provisions on ______________, 20___.

COMPANY:

By: _________________________________
Name: _______________________________
Title: ________________________________

____
Shareholder
[address]

____
Shareholder
[address]