DRAFTING LETTERS OF INTENT

Letters of intent and their benefit to structuring transactions have been debated for years. While they are commonly used, lawyers generally advise their clients to avoid them because they are usually drafted hastily by laymen and, if not properly drafted, could have significant adverse legal consequences.

A poorly drafted letter of intent, rather than being helpful, can be dangerous to those executing it. The risk that a term or clause a party intends to be non-binding will be construed by a court as binding or ambiguous is a very real possibility as illustrated by numerous Texas cases.

A letter of intent provides flexibility because parties are able to quickly initiate transactions by specifying that certain terms of the letter of intent can be binding while other terms can be non-binding. Letters of intent can be valuable tools for structuring complex transactions as they give the parties a skeletal outline from which to work as they develop their definitive contract while providing either party the ability to back out of the transaction without liability. The majority of letters of intent are intended to be merely commencement points for negotiation and not binding contracts. There is no single form letter of intent that meets every need. Therefore, this article will concentrate on the necessary provisions of a letter of intent.

Before entering into a letter of intent, the parties must understand that parties to an agreement must be in agreement regarding all of the essential terms of an agreement in order for the agreement to be enforceable. However, parties may also bind themselves regarding certain key terms while leaving less important terms for further negotiation. In the legal arena, generally, whether a term in a letter of intent is binding or non-binding is a question of fact for the fact finder (the jury). However, if the terms of the letter of intent are sufficiently precise and have a definite and certain meeting, then the question becomes one of law to be decided by the court making it possible for the court to hold that the language of the letter of intent can conclusively establish the intent of the parties. Of significant importance, is that the letter of intent be constructed using words with definite and certain meanings that clearly manifest which terms the client wants to be binding and which terms the client does not want to be binding.

When we draft letters of intent for our clients, we carefully question the client as to whether the letter of intent is intended to be an outline for the negotiation and ultimate execution of a definitive contract or are certain of the terms intended to be binding. Normally, we advise that the purchase price, confidentiality and third party negotiation provisions be binding. The purchase price is usually easy to determine. The confidentiality provisions and the third party negotiation provisions are provisions which we include that prohibit the prospective seller or buyer, as the case may be, from shopping the transaction pending the negotiation and execution of a definitive contract. Lesser details and terms too complicated or labor intensive to be realistically agreed upon at the letter of intent stage, are often omitted to be negotiated at a later date. We are always careful to make sure that certain nebulous provisions (like promises to use best efforts), are not included in letters of intent. As stated earlier, terms and conditions that are not specific can be troublesome. The law dictates that a party's own actions and conduct can be used as evidence that they intended that their letter of intent bind them. In the alternative, the

parties should also be aware that reliance on a portion of a letter of intent that they do not intend to be binding can be used to establish their intent to be bound by the entire agreement.

As such, we routinely advise our clients to remember the following rules when drafting or entering into a letter of intent. If no part of the letter of intent is meant to be binding, we either use headings at the top of the letter of intent which are in bold and all capitalized such as "**NON-BINDING LETTER OF INTENT**" or "**NON-BINDING MEMORANDUM OF ANTICIPATED TRANSACTION**" or, we include a separate paragraph, at the end of the letter of intent, delineating the non-binding nature of the letter of intent.

If certain terms and conditions of the letter of intent are intended to be binding, then we separate the terms and conditions into separate sections with headings (similar to the above) that clearly delineate which provisions are intended to be binding and which provisions are not intended to be binding. In addition, with respect to the provisions that are intended to be binding, we always provide avenues of enforcement (specific performance, damages, jurisdiction, venue, attorneys fees, etc.) for the binding provisions.

In either case, a provision as to <u>when</u> the letter of intent will expire is necessary in the event a definitive contract has not been negotiated between the parties by a certain time.

In summary, the most important provisions in a letter of intent are as follows:

1. Whether the letter of intent is intended to be binding or non-binding;
2. Which provisions of the letter of intent are intended to be binding or non-binding;
3. Enforcement provisions, as to binding provisions; and
4. Termination date of effectiveness of letter of intent.

If it is your business practice to use letters of intent on a consistent basis, it is our advice that you retain an attorney to either review the letter of intent or have your attorney draft a form letter of intent for your use in your day to day business. At a minimum, this form would provide a guide and reminder as to what terms and conditions should be included in the letter of intent to reflect and protect the interest of the parties.