

Your “Non-Binding”
Letter of Intent Is Legally
Binding – and It Just Cost
Your Client \$113 Million

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Case Law Uses Different Terms for Preliminary Agreements

- Case law typically uses these terms interchangeably:
 - Letter of intent.
 - Memorandum of understanding.
 - Commitment letter.
 - Term sheet.
 - Preliminary agreement.

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Case Law Governing LOIs Is Incoherent

- Replete with “incoherent guidance.”
- Precedents are in “hopeless conflict.”
- “Confusing.”
- “Inconsistent.”
- “All over the board.”

Source: Omri Ben-Shahar, *Pre-Closing Liability*.

Seminal Delaware Case: Siga Technologies

- Binding?
- Bad Faith?
- Damages?

Source: *Siga Techs., Inc. v. PharmAthene, Inc.*, 132 A.3d 1108 (Del. 2015), *as corrected* (Dec. 28, 2015)

Evolution and Trends

- Previous cases: “either/or”
- Modern trend
 - LOIs presumed non-binding BUT
 - If LOI says “***parties shall negotiate in good faith***”
 - Then parties must negotiate “in good faith in an effort to reach a final agreement.”

What Is Binding?

- Look for declaration statements
- “Shall, Will, Must.”

What Does Bad Faith Include?

1. Renouncing the deal.
2. Abandoning the negotiations
3. Insisting on conditions that do not conform to the LOI.
4. Proposing terms inconsistent with LOI.

Sources: *Teachers Ins. & Annuity Ass'n of Am. v. Tribune Co.* (S.D.N.Y. 1987); *Siga Technologies, Inc. v. PharmAthene, Inc.* (Del. 2013).

Remedies for Failure to Negotiate in Good Faith

- a. Specific performance.
- b. Reliance damages (i.e., recovery of fees and expenses), and
- c. Expectation damages (i.e., recovery of lost profits) (allowed in Delaware) (*may* be recovered in Missouri and Kansas in limited circumstances).

What's the Difference Between **Reliance Damages** and **Expectation Damages**? Potentially a lot!

- Assume Buyer spends \$500k to buy Target that is worth \$100MM, but Target backs out of the LOI in bad faith.
- If Buyer gets **reliance damages** only, it gets \$500k.
- If Buyer gets **expectation damages**, it gets (potentially) **\$100MM!**

Missouri Case Law (Mostly Ancient)

- LOIs must contemplate a formal written agreement.
- If the parties do not intend to be bound until the formal written agreement, it must be specifically set out in the LOI.
- Expectation damages *may* be recovered.

Kansas Case Law (Mostly Ancient)

- Courts will utilize Delaware law for guidance.
- LOIs must indicate that the parties intend to continue negotiating and contemplate a formal written agreement.
- Parties' actions consistent with a preliminary agreement may evidence an intent to be bound (contemplating a subsequent formal agreement is not dispositive).
- Lost profits *may* be recovered.

LOI Structure

- Non-binding business terms
- Parties often expressly provide these terms are binding in the LOI:
 - Exclusive negotiation
 - Termination fee (if applicable)
 - Governing law
 - Fees and expenses

Recap

- Seminal case (*Siga Technologies*).
- Evolution of the LOI law.
- Potential damages.
- Missouri/Kansas applicability

What are the takeaways?

Takeaway No. 1

Revise your standard LOI.

Takeaway No. 2

Eliminate the phrase “*the parties shall negotiate in good faith,*” unless the parties really intend to be legally bound by such language.

Takeaway No. 3

Eliminate other declarative statements: “the parties *shall,*” “the parties *must,*” etc.; again, unless the parties intend to be legally bound.

Conclusion

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