KIRKLAND & ELLIS LLP

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Letters of Intent — Ties that Bind?

Parties entering into letters of intent or term sheets (LOIs) should clearly determine which provisions of an LOI are intended to be binding and which are not, and should expect to be held to these commitments.

A recent Delaware bench decision from newly appointed VC Laster on a motion for a temporary restraining order offers a timely reminder of potential pitfalls for parties entering into letters of intent or term sheets (for ease of reference, collectively referred to as LOIs) with the expectation that they merely represent an unenforceable "agreement to agree."

In the present case, the plaintiff, Global Asset Capital, entered into a letter of intent with the defendant, Rubicon U.S. REIT, that contemplated Rubicon filing for bankruptcy in conjunction with Global signing an agreement to act as the stalking horse bidder with the benefit of a break-up fee in a court-supervised auction. While the recitation and findings of fact are extremely limited given the preliminary nature of the proceedings, the court did grant injunctive relief based on colorable claims that the exclusivity and confidentiality provisions of the LOI were breached by Rubicon and that Rubicon had failed to negotiate in good faith with Global as required by the LOI.

In reaching his decision, the judge cited a number of key factors that merit consideration by parties negotiating LOIs:

- Delaware does not recognize an inherent fiduciary out in every contract if one is not negotiated by a party. A seller that agrees to exclusivity with a potential buyer should not expect that it can later violate that agreement based on an implicit back-door exit from that commitment grounded in its fiduciary duties.
- An exclusivity or no-shop provision is a unique right, the breach of which is not "readily remedied after the fact by money damages." As such, injunctive relief is an appropriate judicial remedy to enforce the benefits bargained for by the potential buyer.
- When an LOI requires the parties to negotiate or to enter into an agreement, this creates an affirmative obligation on the parties to in fact engage and negotiate in good faith notwithstanding the fact that there are still material issues to be hashed out and other pieces to fall into place. The court stated that "radio silence is not negotiating in good faith."
- The court briefly noted that parties can protect themselves against unexpected obligations by expressly stating that the relevant terms of the LOI are non-binding.

While none of these findings are particularly novel and are consistent with prior Delaware and, to a large extent, New York and California precedent, they do highlight the importance of careful phrasing by parties of their respective obligations in an LOI, even one entered at an early stage in a sale process. "Negotiating in good faith" and "preliminary agreement" are phrases that are often casually thrown around in discussions and LOIs, but they do have legal consequences. Parties should be clear as to which provisions of an LOI are intended to be binding and which are not, and should expect that they will be held to these commitments.

Buyers and sellers are well-advised to heed VC Laster's introductory view that "… parties enter into them [LOIs] for a reason. They don't enter into them because they are gossamer and can be disregarded whenever situations change. They enter into them because they create rights."

If you have any questions about the matters addressed in this *M&A Update*, please contact the following Kirkland author or your regular Kirkland contact.

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