KIRKLAND & ELLIS LLP

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Letters of Intent — Say What You Mean and Mean What You Say

A recent decision by the Georgia Court of Appeals upholding a jury verdict awarding millions to a spurned suitor highlights the potential pitfalls for parties using letters of intent or term sheets as stepping stones to a definitive deal.

In a recent *Kirkland M&A Update*, we reviewed a Delaware decision that highlights the risk that letters of intent can create unexpected legal obligations and may not merely represent an unenforceable "agreement to agree." We noted the court's admonition that parties can protect themselves against these unexpected outcomes by clearly limiting which obligations are intended to be legally binding. A recent decision by the Georgia Court of Appeals upholding a jury verdict awarding $281 million to a spurned suitor shows that even careful drafting of "non-binding" language in a letter of intent may not be effective in avoiding unanticipated binding obligations if the parties' conduct, including in respect of the letter of intent itself, is inconsistent with those provisions.

In the Georgia case, David McDavid entered into a letter of intent that provided him with a 45-day exclusivity period to negotiate the acquisition of the Atlanta Hawks and Atlanta Thrashers professional sports franchises from Turner Broadcasting. The letter of intent expressly provided that "neither party ... [would] be bound ... unless and until such party ... has executed the Definitive Agreements" and that "[n]o such binding agreement shall exist ... unless and until the parties have negotiated, executed and delivered ... Definitive Agreements." The letter of intent expired under its terms at the end of the 45-day period. While McDavid sought an extension of the letter of intent (and exclusivity period), Turner demurred noting that the parties were "very, very close to a deal." Negotiations on final terms and documents continued for several months with multiple indications from Turner that the parties "have a deal" and the "deal is done." At the very end of the process, a second suitor appeared and Turner engineered a quick sale of the teams to this suitor (signing the agreements as McDavid was preparing to fly to Atlanta for a press conference announcing his deal). McDavid sued Turner for breach of oral contract.

The appellate court, applying Georgia law, upheld the jury verdict finding such an oral contract and awarding McDavid substantial damages. While Turner argued that the letter of intent clearly excluded the possibility that the parties would be bound to a sale unless written definitive agreements were signed, the court noted that Turner had elected to allow the letter of intent to expire at the end of the initial exclusivity period. The letter of intent provided that only the confidentiality terms survived a termination of the letter, and the court held that thereafter Turner no longer benefitted from the protection of the "non-binding" provisions. As such, Turner's conduct for the ensuing months would be judged by its expressions and conduct (which in addition to the assurances to McDavid noted above included internal preparations for a sale announcement), all of which the court found evinced an intent to be bound to a deal.

This decision offers a few practice tips for dealmakers pursuing a deal involving a letter of intent or term sheet:

- In addition to focusing on clearly evidencing which provisions are intended to be legally binding, parties to a letter of intent should ensure that the section of the letter of intent outlining such intentions survives a termination of the letter of intent. Moreover, it is not uncommon for a letter of intent to expire at the end of an exclusivity or negotiation period, even as parties continue to work out the final details of a transaction. Such an expiration without survival of these key terms may mean the parties will no longer benefit from the protective "non-binding" provisions of the letter of intent, and may be judged based on their statements and conduct (that at late stages more often than not are at risk of being interpreted as giving rise to a binding agreement based on all material terms being agreed).
- A party should be judicious in the use and phrasing of assurances it offers to the other side as negotiations drag on, especially when there are multiple bidders. Even while significant issues remain open, parties are

often tempted to offer a strong affirmation of desire and intent to reach a signing in order to calm jittery nerves. As was alleged here, those strong statements (e.g., "close to a deal," "have a deal," etc.), especially when combined with normal preparations for a potential signing, may be susceptible in hindsight to misinterpretation as evidence of the existence of agreement on all material terms and, therefore, of an intention to be bound to an oral contract.

- Somewhat surprisingly (given that a written agreement was never signed with McDavid), the court took note of the fact that the draft agreements exchanged by the parties contained a standard "merger clause" providing that the written definitive agreement would "supersede all prior agreements, understandings and negotiations, both written and oral." The court held this language to acknowledge the possibility of a pre-signing oral agreement, especially since the "merger clause" never became effective. Parties may wish to protect themselves against such an interpretation by expressly stating in drafts of the "merger clause" that no concession is made that such pre-signing agreements (oral or otherwise) exist.

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It is likely that the jury in this case was swayed by the extreme facts and it bears noting that the court's review was limited by virtue of being a review of the jury verdict (its sole question was whether there is "some evidence to support the verdict"). However, the case, like the earlier Delaware decision, highlights the potential pitfalls for parties using letters of intent or term sheets as stepping stones to a definitive deal. Traps for the unwary reside both in words carelessly omitted and in words included without sufficient attention to their survival or impact.

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

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