



The Devil *is* the Detail: When Being More Thorough Can Get You Into Trouble

Drafting Letters of Intent

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As young lawyers, we learn the valuable lesson from colleagues and mentors that *ambiguity* in a written agreement is the enemy of a good lawyer; it has the potential to land us in court with our skills labeled inept. Ambiguity becomes our boogeyman, the stuff of our nightmares, with the power to subject us to courtrooms where laypeople determine what our writings meant. To combat ambiguity, we incorporate details to further highlight our intent; we use examples to express the meaning of the words we have chosen. We spend time crafting and re-crafting clauses to ensure every potential issue is addressed, adding detail to make certain no other meaning could possibly be ascribed to the words we have painstakingly selected. It is therefore surprising that there is one document unlike any other, a document in which the inclusion of extensive detail actually creates ambiguity about the intent of the parties to it, a document that can be the downfall of the most detail-oriented among us—that document is the letter of intent.

A letter of intent is “[a] written statement detailing the preliminary understanding of parties who plan to enter into a contract

or some other agreement; a noncommittal writing preliminary to a contract.”¹ As the definition suggests, most letters of intent are not intended to bind the parties to an agreement, but are a precursor to the real agreement between the parties, used to determine if the parties can come to a later agreement on the subject matter. However, Michigan caselaw has held that a letter of intent is “an agreement to agree at a later date and is as valid as any other contract.”² In Michigan, the parties to a letter of intent can be contractually obligated to complete the transaction contemplated by the letter of intent even if they never actually intended the letter to constitute the complete agreement.

Deal Considerations

The first course of action for any lawyer drafting a letter of intent is to understand the client’s actual objective. What is the client’s purpose in obtaining or executing the letter of intent? Does the client wish to be bound by it? Is the client trying to bind the other party? Is the client merely seeking confirmation that the

potential for a deal exists? The actual purpose of the letter of intent will dramatically impact its nature and scope.

The appropriate type of letter of intent in a given scenario also depends on which party counsel represents. Counsel to sellers of real property and assets should be wary when drafting letters of intent. In particular, the remedy of specific performance can be used to force the seller to complete the contemplated transaction. While sellers may also seek the remedy of specific performance against purchasers, if the purchaser is a shell entity or an entity without assets (as is typically the case) or the buyer's contingency allows the buyer to terminate without liability, the remedy of specific performance may be of no real value because the purchaser would not have the ability to complete the transaction.

Drafting can begin in earnest once the client's intent and role in the transaction is clearly ascertained, but careful consideration should be given to each and every clause incorporated into the letter of intent. As Michigan caselaw shows, the more inclusive the letter of intent, the more likely the court will find an obligation to complete a transaction.

How an Agreement to Agree Becomes an Obligation

To form a valid contract, there must be a meeting of the minds between the parties as to all material terms.³ When a letter of intent specifies all the "material and essential terms" of the agreement and "leaves nothing to be agreed upon as the result of a future negotiation," it becomes an enforceable contract.⁴ In particular, the court in *Heritage Broadcasting Company v Wilson Communications, Incorporated*⁵ held that a letter of intent that clearly and unambiguously identifies "the parties, the assets to be sold, the consideration, the schedule for payment, the handling of the accounts receivable, the rights and remedies of each party upon breach, and mutual termination rights if the closing did not occur within 360 days of the definitive agreement" is no longer an agreement to agree, but becomes the definitive agreement between the parties.⁶

The mere fact that the letter of intent specifically states it is the parties' goal that the identified terms and conditions "be incorporated into a definitive agreement to be *negotiated* and *entered* into" by the parties is insufficient to prevent such a detailed letter from being considered the definitive agreement.⁷ When a letter of intent includes so much detail regarding the terms that a definitive agreement would only add "the mechanics necessary to accomplish the conveyance," the definitive agreement becomes moot regardless of the stated intention.⁸ It is therefore critical that lawyers tasked with drafting letters of intent take special care not to incorporate so many details and terms

that they create a binding agreement for their client when the parties did not actually intend to be bound.

Even when the parties to a letter of intent assign different meanings to a section of the letter, courts do not consider that difference in meaning as evidence of a failure of a meeting of the minds with respect to the contract. In *Heritage*, the court reasoned that the meeting of the minds can be found by looking at the "express words of the parties and their visible acts, not their subjective states of mind."⁹ The defendant argued it could not be

FAST FACTS

The most important consideration in drafting a letter of intent is to create a document that fully realizes the client's intent—either to create a nonbinding preliminary list of potential terms or enter into a binding agreement to agree.

When drafting nonbinding letters of intent, include affirmative statements that the parties' intent is not to be bound, and refrain from describing every clause required in the final agreement. Otherwise, courts may determine that the over-inclusive letter of intent is the actual agreement of the parties to complete the underlying transaction.

Courts may consider the parties' actions after execution of the letter of intent as evidence of intent at the time of execution. Counsel clients to act in accordance with the stated intent.



bound to the letter of intent because the defendant and plaintiff did not have a “meeting of the minds” regarding the legal import and operative effect of the letter after the expiration of a 45-day exclusivity period.¹⁰ The court determined that the evidence presented by the defendant showed “only that defendant may have subjectively entertained a different interpretation of the letter’s effect upon expiration of the forty-five-day period,” which, under Michigan law, is “insufficient to show that a meeting of the minds did not occur.”¹¹ In sum, the court determined the meaning of disputed portions of the letter of intent and found that the defendant meant to be bound by the letter.

Actions Can Speak Louder than Words

Not only can letters of intent be challenging to draft, but actions of clients after the execution of the letter or the execution of subsequent letters can be used to determine the clients’ intent. In *Opdyke Investment Company v Norris Grain Company*,¹² the court considered two separate letters of intent between the same parties. In a September 16, 1976 letter of intent, the court noted, the parties agreed that neither party would “be liable to the other for fees, costs or expenses incurred by reason of the good-faith pursuit of the intent of this letter.”¹³ The September letter expired by its terms in December 1976 and the parties executed a new letter of intent on March 11, 1977. The March letter did not contain the limitation of liability noted in the September letter. The Michigan Supreme Court reasoned that by failing to include the limitation of liability from the September letter, a jury could infer that the parties had intended to be bound by the March letter.

Furthermore, the Court found that the parties’ execution of letters of intent with different terms could evidence their intention “to execute a series of increasingly detailed contracts as the project progressed, with each contract legally binding and protecting each party’s interest...should the other party withdraw.”¹⁴

The Court, citing Professor Corbin, was not persuaded by the express provisions of the March letter, which contemplated the execution and negotiation of additional contracts, stating “the fact that additional contracts may have been contemplated and mentioned in the letter does not invalidate any agreement actually reached.”¹⁵ The Court was willing to allow evidence that the parties’ removal of the limitation language in the March letter created a material issue of fact for the jury to consider, even though the letter expressly stated that a final agreement was contemplated. On that theory, the Michigan Supreme Court referred the case back to the trial court, which had granted the defendant’s motion for summary judgment on the grounds that the letter of intent was not a binding agreement.

Drafting Nonbinding Letters of Intent

If a client does not wish to be bound by the terms of a letter of intent, consider using a short term sheet that is not signed by either party. At least in connection with the sale of real property or other transactions subject to the statute of frauds, an unsigned term sheet should keep clear the intent of the parties to remain unbound.

If, however, an unsigned term sheet is not acceptable to the parties and the client does not wish to be bound by the terms of the letter of intent, the letter should include a clause that clearly (a) states it is nonbinding upon the parties; (b) provides that neither party shall be bound until both parties execute a separate, definitive agreement; and (c) provides for automatic termination of the letter of intent if the separate, definitive agreement is not executed on or before a stated date. This combined approach affirmatively states the intent of the parties not to be bound, incorporates a condition precedent that must be satisfied before either party agrees to be bound (i.e., the execution of a separate definitive agreement), and contains a consequence for the failure of the condition precedent (i.e., termination of the letter of intent and any obligations).

To further support your client’s desire not to be bound by the letter of intent, be sure to keep the letter simple. Make sure that terms necessary for the completion of the transaction remain to be negotiated. The court will find a binding agreement when the letter of intent is so detailed that it leaves nothing to negotiate but the mechanics of the transfer. If the letter does not include all the material terms of a deal, it cannot be the manifested intent of the parties to complete the underlying transaction and, therefore, cannot be binding upon the parties.

In addition, always discuss with your client the pitfalls of acting contrary to the letter of intent. The *Opdyke* Court created the potential for the parties to use the actions and future writings of the parties as evidence of the objective of the parties when they executed the letters of intent. If the client does not wish to be bound by the letter of intent, the client should take care not to act as if it is bound by the agreement. For example, if the letter of intent contemplates that a definitive agreement will be negotiated and due diligence investigations will be performed within a



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stated number of days after the definitive agreement is executed, it would be best practice to advise the client to wait to start performing the due diligence until after the definitive agreement is executed. Otherwise, the court may look at the actions of the purchaser in performing due diligence as contrary to the requirement that a definitive agreement be negotiated and executed.

Finally, remember that letters of intent usually do not contain a waiver of a trial by jury. This is not surprising because, most often, the parties to the letter do not consider it to be a binding agreement. If a dispute arises involving a letter of intent, it will most likely be resolved by a jury trial, which means a jury will be tasked with determining the plain language of the letter that was executed by the parties.

Drafting Binding Letters of Intent

If the client's aim is creating a binding letter of intent, best practice for counsel is to include each and every term and clause counsel will typically include in a formal agreement memorializing the contemplated transaction. For example, in addition to provisions identifying the parties, purchase price, title company, and closing date in connection with the sale of real property, counsel should also include provisions governing events of default and remedies, the proration of taxes, operating income, representations and warranties, casualty, condemnation, assignment documentation, and the type of deed, and every other provision typically included in a purchase and sale agreement for real property, including a provision waiving the right to a trial by jury. In the case of a binding letter of intent, the letter is the definitive agreement between the parties and should be drafted with all the restrictions, limitations, and protections typically included by counsel to the parties of that sort of transaction.

Conclusion

In Michigan, courts have transformed the letter of intent from a statement of the preliminary understanding of the parties to an agreement into an enforceable agreement to agree. Determining

and expressing the true intention of the client is the most important task when drafting a letter of intent. Counsel tasked with drafting nonbinding letters of intent must use extreme caution not to create a binding agreement for their clients by incorporating so much detail that a court could determine that the parties' objective was to create a binding agreement. Affirmative statements that the letter is nonbinding, along with the requirement that a definitive agreement be executed and a deadline for the execution of the definitive agreement, are all important in confirming the nonbinding nature of a letter of intent.

If a binding letter of intent is contemplated by the parties, wholesale inclusion of the terms and conditions usually appearing in the formal agreement is appropriate. Regardless of whether the letter is binding or nonbinding, counseling clients not to act contrary to the stated intent in the letter is crucial to prevent disputes over its meaning. ■



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ENDNOTES

1. Black's Law Dictionary (9th ed).
2. *Zander v Ogihara Corp*, 213 Mich App 438, 442; 540 NW2d 702 (1995).
3. *Heritage Broadcasting Co v Wilson Communications, Inc*, 170 Mich App 812, 818; 428 NW2d 784 (1988).
4. *Id.*
5. *Id.*
6. *Id.* at 819.
7. *Id.* at 815-819 (emphasis added).
8. *Id.* at 819.
9. *Id.* at 818-819.
10. *Id.* at 817.
11. *Id.* at 819.
12. *Opdyke Investment Co v Norris Grain Co*, 413 Mich 354; 320 NW2d 836 (1982).
13. *Id.*
14. *Id.* at 360.
15. *Id.*