

# LETTERS OF INTENT

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# LETTERS OF INTENT

## INTRODUCTION

This presentation discusses how to use non-binding Letters of Intent in commercial real estate leasing transactions in order to efficiently and effectively advance the transaction to execution of legally binding documentation. This presentation only addresses clearly non-binding Letters of Intent, and specifically omits the complex legal problems in dealing with Letters of Intent which are not, by their terms, specifically intended to be non-binding. The discussion will answer the following questions:

- What** is a Letter of Intent?
- Who** drafts a Letter of Intent?
- Why** use a Letter of Intent?
- When** to use a Letter of Intent?
- How** to Draft a Letter of Intent.
- Where** will Letters of Intent Take You?

### I. **WHAT IS A LETTER OF INTENT?**

#### A. Title

A Letter of Intent may be entitled with many other terms, including:

- “Memorandum of Understanding;”
- “Gentlemen’s Agreement;”
- “Agreement in Principle;”
- “Letter of Understanding;”
- “Letter of Agreement;”
- “Term Sheet;” or
- “Transaction Outline.”

The title is not important. The term “Letter of Intent” is used to cover all non-binding preliminary agreements between parties to a transaction. The Letter of Intent is distinguished from the Request for Proposal (“RFP”) generated by the tenant’s broker to outline the tenant’s needs and expectations, and to solicit landlord offers. However, the Letter of Intent should address all issues in the RFP.

#### B. Preliminary Non-Binding Agreement

In almost every instance in a commercial real estate setting, a Letter of Intent is intended not to be a legally binding lease. Instead, it sets forth “understandings” which are written in order to expedite the negotiating and drafting process. No attorney should draft or advise their client to execute a binding Letter of Intent, except under extraordinary circumstances. Instead the attorney should advise the client to proceed directly to a full lease, perhaps using a simplified format or a commonly used printed form, such as the State Bar form or the commonly used Texas Association of Realtors (“TAR”) Improved Property Commercial Lease form (TAR-2101 last revised 5-26-06).

### C. Outline of Material Business Terms

The Letter of Intent's primary purpose is to outline the non-binding agreement of the parties to material business terms without which the parties would not proceed to spend further time, energy and money on a transaction. What terms are "material" for the purpose of proceeding with the transaction depends on the parties and the property.

### D. Outline of Material Legal Terms

Particularly with sophisticated parties, the Letter of Intent may outline material legal terms necessary to be understood and accepted by the parties as a condition to proceeding with the transaction. Sometimes this involves the "AS IS" lease of property, disclosure of unusual property conditions/defects or acceptance of certain procedures of an institutional seller.

## II. **WHO DRAFTS THE LETTER OF INTENT?**

### A. Attorney

Attorneys draft the Letter of Intent for complex transactions or those with unusual legal issues. Sometimes the parties' attorneys will review provisions of a Letter of Intent drafted by a non-lawyer. Some parties have "standard" Letter of Intent forms drafted by attorneys for use in particular transactions by a non-lawyer. Only a minority of Letters of Intent are drafted by attorneys. However, attorneys often have the opportunity to review client drafted Letters of Intent or to provide a "form" for use by a client.

### B. Principal

Where no outside broker is involved in a transaction, the principal may draft a Letter of Intent.

### C. Broker

Most Letters of Intent are drafted by a broker, generally for the buyer in a sale transaction, but either the tenant or landlord in a leasing transaction. This does not constitute the unauthorized practice of law in Texas, for the Letter of Intent is non-binding. As the Letter of Intent is a written agreement which is not legally enforceable, the broker is not acting as a lawyer or giving legal advice. However, if a Letter of Intent were binding, a broker would likely be violating the statutory prohibitions against the unauthorized practice of law as well as the prohibitions of the Texas Real Estate License Act (and its implementing rules and regulations) relating to drafting legal documents. Where there are legally binding provisions in a Letter of Intent, attorneys should remind clients to have the brokers focus on business points and let the attorney review any legal issues.

### D. Who Signs the Letter of Intent

Since the Letter of Intent is not legally binding, it is not critical who signs it. Typically, it is signed by either the principal itself or the principal's broker. Many Letters of Intent are signed by a broker. The Letter of Intent can be initialed instead of signed. The fact that a Letter of Intent is not signed by a party is not legally relevant. However, the morally binding character of a Letter of Intent is enhanced if both parties sign and if a principal of each party, rather than its broker, signs. The failure to have a Letter of Intent signed by both parties will likely ensure that the Letter of Intent is

non-binding. Where there are legally binding provisions in a Letter of Intent, all parties must sign, preferably the principals.

### **III. WHY USE LETTERS OF INTENT?**

#### **A. Efficiency**

Letters of Intent are an economical and efficient manner to move transactions forward. Letters of Intent are shorter and more informal than a formal, legally binding lease. For this reason, they can usually be drafted quickly, and because they are non-binding, tedious drafting is unnecessary. Since lawyers are routinely omitted from the drafting process, legal fees and delay are omitted.

#### **B. Establish Deal Points**

Letters of Intent will establish business agreements on material lease points such as:

1. Rent;
2. Expense issues;
3. Tenant improvements;
4. Term;
5. Timing of lease commitment;
6. Use;
7. Renewal rights;
8. Expansion/contraction rights;
9. Parking;
10. Assignment/subletting; and
11. Tenant inducements.

See Section V.B.9 of this article for detailed discussion of terms to include in a Letter of Intent.

#### **C. Provide Basis for Formal Lease**

The Letter of Intent can help the parties' attorneys move quickly to efficiently draft and negotiate formal legally binding documentation. Sometimes the Letter of Intent will dictate the specific form of lease; for example, contract forms are promulgated by the Texas Real Estate Commission, Texas Association of Realtors and State Bar of Texas ("Blue Books"). Some institutional parties dictate use of their own form. For most multi-tenant properties, the landlord's lease form will be used in almost every instance, except for certain major national tenants. The Letter of Intent can specifically provide who will prepare the first draft of the legal documentation and when it will be delivered.

Significant time and money can be saved by utilizing the Letter of Intent to provide the attorney preparing formal, legally binding documentation of a transaction with complete, accurate information at the soonest possible time.

#### **D. Binding Agreements Contained in the Non-Binding Letter of Intent**

Although the basic transaction terms contained in a Letter of Intent should not be legally binding, there are a number of agreements which may be appropriate in particular transactions to be legally binding upon the parties and may be contained in either the Letter of Intent or a separate agreement.

## 1. Confidentiality

The Letter of Intent can provide that information provided is kept confidential. Often information which is provided as a part of the due diligence period (which sometimes commences immediately upon signing the Letter of Intent), is to be returned, together with all copies.

## 2. “No Shop” Agreement

The landlord can agree not to seek other tenants (and the tenant not to negotiate for other premises) for a stated period of time, in order to allow an opportunity for the parties to negotiate and execute legally binding agreements. This can be expanded to preclude specific types of marketing activities.

## 3. Good Faith Obligation to Negotiate

The parties can contractually agree that they will execute “good faith,” “best efforts,” “all reasonable effort,” or some other standard of care in seeking to move from non-binding Letter of Intent to binding legal documentation. Without this contractual agreement, there is no obligation under Texas law to negotiate in good faith. *See English v. Fisher*, 660 S.W.2d 521, 522 (Tex. 1983); *FDIC v. Coleman*, 795 S.W.2d 706 (Tex. 1990); *Cluck v. Frost Nat'l. Bank of San Antonio*, 714 S.W.2d 408, 410 (Tex. App.--San Antonio 1986, writ ref'd n.r.e.). Apparently, this is contrary to the law in other states. The concept of good faith and fair dealing which relates to the performance of contract provisions exists in Texas and would apply to Letters of Intent. *See First Texas Sav. Ass'n of Dallas v. Dicker Ctr., Inc.*, 631 S.W.2d 179, 182 (Tex.App.--Tyler 1982, no writ). However, *John Wood Group USA, Inc. v. ICO*, 26 S.W.3d 12, 21 (Tex. App. Houston--[1<sup>st</sup> Dist.] 2000, pet. denied), held that even with a clearly worded “good faith effort” obligation to negotiate, that since the underlying Letter of Intent was non binding, then there could be no damages from breach of the good faith negotiation obligation. This makes such a provision meaningless legally, but may still be of benefit practically or morally.

## 4. Submission of Initial Legal Documentation

The Letter of Intent can designate the party whose attorney will prepare and forward the initial draft of the legal documentation to evidence the transaction, the forms used, when the documentation should be submitted and to whom it should be distributed.

## 5. Obtaining Contingent Approvals

Particularly for institutional parties, Letters of Intent will be subject to further approval. The Letter of Intent can provide that such party will promptly present the transaction for the approval of such committee and that the signatories to the Letter of Intent will recommend approval of the transaction on the terms set forth in the Letter of Intent.

## 6. Agreement to Pay Brokerage Commission

The Letter of Intent could constitute the written agreement necessary under Texas law evidencing the agreement of a party to pay a brokerage commission to specified brokers. This is relevant for properties which are not listed for sale or lease.

## E. Implied Obligation

Although the parties are not legally bound to the transaction, a Letter of Intent has the effect of binding the parties for the following reasons:

1. Psychological Commitment of the Parties to the Transaction.
2. Moral/Professional Commitment.
3. Damage to future dealings with the specific parties to the transaction.
4. Damage to the “breaching” party’s reputation in the commercial real estate community.

## IV. **WHEN TO USE LETTERS OF INTENT?**

Letters of Intent are appropriate for virtually every commercial real estate lease transaction.

Letters of Intent are not appropriate where the subject matter is complex or legalistic. Further, if the proposed Letter of Intent is overly complicated and lengthy, the parties should dispense with it and proceed directly to a legally binding lease.

## V. **HOW TO DRAFT THE LETTER OF INTENT**

### A. Forms

There are no form Letters of Intent promulgated in Texas by any real estate industry or State Bar group. Letters of Intent are typically drafted in the format of a letter from the buyer/tenant’s broker to the seller/landlord’s broker with the majority of the text being a listing, often in numerical sequence with headings, of paragraphs discussing material business terms. A Letter of Intent may be a simple “term sheet,” which is more of an outline signed or initialed by the parties. The form of a Letter of Intent is not critical so long as it is clear, concise, unambiguous and non-binding.

Several form Letters of Intent are attached as appendices:

- "A" – Lease transaction “plain English” term sheet form using the methodology of the State Bar of Texas Real Estate Forms Committee,
- "B" – Lease transaction Letter form.
- "C" – Lease Letter of Intent Checklist

A list of articles on Letters of Intent, many of which contain forms, is attached as Appendix “D.”

### B. Drafting Tips

The following are practical issues for drafting a Letter of Intent:

#### 1. Title

The Letter of Intent should be titled “Non-Binding Letter of Intent” or “Letter of Intent.” Avoid “Letter of Understanding” or “Letter of Agreement.”

## 2. Non-Binding Character

The Letter of Intent should specifically include, preferably in capitalized, underlined or bold text, a provision specifically stating that it is NOT LEGALLY BINDING. This provision should be located immediately above the signature lines (see Appendices for examples).

The Letter of Intent should not rely upon language that the transaction is "subject to legal documentation" or otherwise indicate that a more formal document is anticipated, as being sufficient to indicate the non-binding character of a Letter of Intent. See *Foreca S.A. v. GRD Development Co., Inc.*, 758 S.W.2d 744, 745 (Tex. 1988); *Aegis Ins. Holding Co., L.P. v. Gaiser*, 2007 WL 906328, \*10 (Tex. App.--San Antonio 2007, unreported opinion). In *Foreca*, the Texas Supreme Court held that the statement "subject to legal documentation" in a Letter of Intent initialed by both the buyer and seller of certain equipment did not prevent the jury from determining that the document constituted an enforceable contract. *Foreca*, 758 S.W.2d at 745. Although the court indicated that the language was some evidence on the issue, it was "not conclusive on intent to contract." *Id.* at 746.

## 3. Separation of Binding and Non-Binding Provisions

If any legally binding provisions are included within an otherwise unbinding Letter of Intent, they should be separated and located in a separate section, or otherwise carefully drafted so it is obvious they are independent, legally binding obligations. Courts look to the intent of the parties in determining whether a provision is legally binding.

## 4. Good Faith Negotiations

If the parties intend, provisions can be included to mandate that they will negotiate in good faith toward a legally binding contract. This provision should have a stated term (perhaps 30 days). This provision is intended to keep the parties focused, but the decision in *John Wood Group USA, Inc. v. ICO*, 26 S.W.3d 12, 21 (Tex. App.--Houston [1<sup>st</sup> Dist.] 2000, pet. denied) may have eliminated any legal benefits by precluding damages for violation of good faith negotiation provisions.

## 5. "No Shop" Provisions

One or both parties may want an agreement that the other party will not seek other deals while the parties negotiate toward a binding contract. There should be a stated term, which should be the same stated term as the period outlined for the parties to negotiate in good faith (if applicable). Also, the property could be "removed" from the market, on specific types of marketing prohibited.

## 6. Mechanics of Drafting Legal Documentation

The Letter of Intent can state:

- a. Whose attorney will draft the legal documentation;
- b. When the first draft will be complete;
- c. To whom it will be distributed;
- d. The form of lease;
- e. The goal/deadline for completion of negotiations/signature to the binding legal documentation.

## 7. Distribution List/Cast of Characters

Accompanying the final Letter of Intent can be a complete current and accurate listing of the individuals and firms related to the transaction. Relevant information includes company names, individual contacts and their capacity; mail and street addresses, general and direct phone numbers, fax numbers and email addresses.

## 8. Signature

Have the signing party confirm their authority to do so. Be sure the principals are copied on the executed Letter of Intent, as this will reduce the opportunity for the principal to claim lack of agency.

## 9. Material Business Points

### (1) Monetary

- (a) Rent;
- (b) Expense Issues - net character base rent expense stop, CAM;
- (c) Tenant Improvement Contribution by landlord;
- (d) Parking.

### (2) Timing

- (a) Lease Term;
- (b) Lease Commencement;
- (c) Renewal Rights (term of renewal, advance notice to exercise renewal);
- (d) Expansion Rights (timing to elect right of first availability, right of first offer, right of first refusal, etc.);
- (e) Tenant Improvements (space planning, construction plans and construction).

### (3) Selections

- (a) Space planner/architect;
- (b) Contractor.

### (4) Landlord Requirements/Disclosure

- (a) Lease form;
- (b) Use limitations;
- (c) Assignment/subletting;
- (d) Other relevant matters.

### (5) Tenant Requirements

- (a) Use;
- (b) Parking;
- (c) Other relevant matters.

### (6) Tenant Inducements

- (a) Free rent;
- (b) Above building standard improvements;
- (c) Free parking/fixed rate;
- (d) Relocation costs.

## 10. Use of Attorney

Attorneys must educate their clients and brokers that when a Letter of Intent includes particularly complex or legalistic issues, the attorney should be consulted, if only to review proposed language or provide special provisions. This is also true if any significant binding provisions will be included in the Letter of Intent, particularly extensive provisions relating to the mechanics of drafting the legal documentation and good faith obligation to negotiate that documentation.

## 11. Proceed Directly to Lease

When the Letter of Intent negotiations become bogged-down in detail or “wordsmithing”, proceeding directly to a legally binding contract rather than wasting additional time on a non-binding Letter of Intent may be appropriate. The partially negotiated and unsigned Letter of Intent can still provide many benefits to the parties in proceeding to legally binding documentation.

## 12. Managing the Letter of Intent Period

As soon as a Letter of Intent is signed, it should be immediately disseminated, particularly to the attorneys for the parties. If experienced brokers are involved, the brokers can often help the attorney with information and communication between the parties. The attorney will want to manage the expectations of the parties in receiving drafts of legal documentation and timing for the negotiation process, particularly where these points have not been specified in the Letter of Intent.

## **VI. WHERE WILL LETTERS OF INTENT TAKE YOU?**

### A. The Well Drafted Letter of Intent

The well drafted Letter of Intent will help to move a transaction toward the consummation of a legally binding lease in the following ways:

1. Establishing business terms.
2. Assisting attorneys in preparation of the lease.
3. Reducing misunderstandings and saving money if the deal hasn't really been struck.
4. Addressing issues of confidentiality, providing information, not shopping the property, and the like, through binding provisions in the otherwise non-binding Letter of Intent.
5. Clearly providing that the parties are not legally bound to the transaction until the lease is executed.

### B. The Poorly Drafted Letter of Intent

A poorly drafted Letter of Intent, particularly one with ambiguous terms or a lack of clear non-binding language, will impede a transaction or cause the parties to waste time on a transaction which has no realistic chance of closing.

## C. Termination of Letters of Intent

### 1. Right to Terminate

Either party to a non-binding Letter of Intent may terminate negotiations at any time, without reason. The ramifications on the terminating party are practical, not legal, and would involve a souring of relations with other parties of the transaction, or a general diminution of reputation in the commercial real estate community.

The party that did not terminate the Letter of Intent might want to allege a cause of action against a third party for tortious interference with a contract or tortious interference with prospective business relationships, claiming they caused the termination of the Letter of Intent. Tortious interference with a contract won't prevail for non-binding Letters of Intent.

The elements for tortious interference with a contract are:

- (1) a contract subject to interference;
- (2) a willful and intentional act of interference;
- (3) such act was a proximate cause of damages; and
- (4) actual damages.

*Browning-Ferris, Inc. v. Reyna*, 865 S.W.2d 925, 926 (Tex. 1993).

In *COC Services v. CompUSA, Inc.*, 150 S.W.3d 654 (Tex. App.--Dallas 2004, pet. denied), which is discussed in greater detail in the Case Law from Recent Years section at the end of this paper, the plaintiff alleged tortious interference with a Master Franchise Agreement *form* attached as an exhibit to a non-binding Letter of Intent relating to potential CompUSA stores in Mexico. The trial court found tortious interference based on holding the exhibit was a binding agreement. On appeal, the court held that (i) as a form, essential elements of the Master Franchise Agreement were lacking, and (ii) the express language in the Letter of Intent that it was non-binding eliminated any potential fact question on the parties intent for the Master Franchise Agreement to be binding, and (iii) the merger clause in the Letter of Intent prevented admission of parole evidence to contradict the express language of the Letter of Intent.

The elements for tortious interference with prospective business relationships are:

- (1) a reasonable probability that the parties would have entered into a contractual relationship;
- (2) an *independently* tortious or unlawful act by the defendant that prevented the relationship from occurring;
- (3) the defendant did such act with a conscious desire to prevent the relationship from occurring or knew that the interference was certain or substantially certain to occur as a result of his conduct; and
- (4) the plaintiff suffered actual harm or damage as a result of the defendant's interference.

*COC Services*, 150 S.W.3d at 679.

In *COC Services*, the second element was not fulfilled. This element requires, at a minimum, that the tortious conduct constitutes a “cause in fact” that prevents the prospective business relationship from forming. *Id.* Conduct that is merely “sharp” or perceived as “unfair competition” is not actionable. *Wal-Mart Stores, Inc. v. Sturges*, 52 S.W.3d 711, 726 (Tex. 2001). Tortious interference with a business relationship was also alleged in *Electronic Bankcard Systems, Inc. v. Retriever Industries, Inc.* 2003 WL 204717 (Tex. App.--Houston [1<sup>st</sup> Dist.] 2003, unreported opinion), a Letter of Intent case discussed in detail in the Case Law from Recent Years section at the end of this paper. In *Electronic Bankcard*, the court applied the two-year statute of limitations to bar the claims.

## 2. How to Terminate

When a party desires to cease negotiations under a Letter of Intent, it should specifically notify all parties, in writing, that it is doing so. Failure to terminate in writing may result in the rejected buyer suing the new buyer and/or seller alleging interference with their contract rights or business relationship (like *Texaco v. Pennzoil*). Although litigation of this type is unusual and difficult to successfully pursue, relatively simple procedures for dealing with the termination of a Letter of Intent can help prevent potential liability.

Third parties encouraging the termination of a Letter of Intent so to transact business with a party to it, will want to insure that they simply demonstrate their desire to compete fairly, and should refrain from any activity which would be independently tortious (such as slander or libel). Such party’s focus should be on what it desires to do, rather than attacking the credibility or ability of the party under the Letter of Intent. This will reduce the likelihood of an allegation of tortious interference with a business relationship.

## 3. Good Faith Negotiation Obligation

Some Letters of Intent may contain a "good faith" or "best efforts" obligation to negotiate a legally binding contract. An inclusion of an agreement to exercise good faith efforts in the negotiation does not eliminate the general rule that an agreement to enter into negotiations in the future is unenforceable. *John Wood Group USA, Inc. v. ICO*, 26 S.W.3d 12 (Tex. App.--Houston [1<sup>st</sup> Dist.] 2000) (holding that a good-faith provision in a letter was not binding because “good faith effort” was too vague to enforce). In *Maranatha Temple, Inc. v. Enterprise Prods. Co.*, 893 S.W.2d 92, 104 (Tex. App.--Houston [1<sup>st</sup> Dist.] 1994, writ denied), the court acknowledged out of state cases hold that an agreement to use "best efforts" can be enforceable, but stated:

"the words ‘good faith effort’ or ‘best effort’ were not talismanic. Their presence in an agreement does not automatically mean that the provision which contains them is enforceable."

Clearly, a "good faith" obligation is not enforceable. It is not clear that a "best efforts" obligation will have the same result. Generally speaking, real estate lawyers consider "best efforts" a higher standard than "good faith," involving not only purity of intent, but a performance component.

## D. Multiple Letters of Intent

A party may simultaneously negotiate several Letters of Intent. However, no one should execute duplicate Letters of Intent. Instead, it should sign one and focus on negotiating the transaction

contemplated by that Letter of Intent. If other Letters of Intent are submitted, they should be accepted only as “back-up” Letters of Intent. If a party desires to proceed with parallel contract negotiations under more than one signed Letter of Intent, this fact should be disclosed in each signed Letter of Intent to prevent the potential for equitable claims such as a negligent misrepresentation as outlined below.

#### E. Course of Dealings Problems

There may be unusual instances where the existence of the Letter of Intent, together with a significant course of dealing between the parties with specific verbal representations and a significant change in position by one party in reliance upon those representations, could result in a non-contract cause of action by one party asserting that the other party is bound to the essential terms of the transaction outlined in the Letter of Intent.

##### 1. Partial Performance

A party may argue that each party to the transaction should be bound to an otherwise unenforceable Letter of Intent through their partial performance. Where there is partial performance, courts will apply a five-factor test to determine whether the parties intended to be bound by a preliminary agreement.

The five factors are as follows:

- (1) the language of the agreement;
- (2) the context of the negotiations;
- (3) the existence of open terms;
- (4) nature of the partial performance; and
- (5) the necessity of putting the agreement in final form, as indicated by the customary form of such transactions.

*John Wood Group USA, Inc. v. ICO, Inc.*, 26 S.W.3d 12, 18 (Tex. App.--Houston [1<sup>st</sup> Dist.] 2000, pet. denied) (citing *Arcadian Phosphates, Inc. v. Arcadian Corp.* 884 F.2d 69, 70 (2<sup>nd</sup> Cir. 1989) (applying New York law)); *COC Services v. CompUSA, Inc.*, 150 S.W.3d 654, 668 (Tex. App.--Dallas 2004, pet. denied).

In *COC Services*, the parties attached a detailed legal agreement form as an exhibit to a Letter of Intent that contained non-binding language. After the proposed transaction failed to materialize, COC Services argued that through partial performance of the exhibit, the parties expressed their intent to be bound to it. The partial performance element may not be supported by actions consistent with the Letter of Intent (which is non-binding), but must relate to the alleged contract (i.e., the exhibit, which in this case was a Master Franchise Agreement). Due diligence efforts relating to the underlying business transaction was held to be related to the Letter of Intent, not the Master Franchise Agreement. Further, inconsistent positions taken by CompUSA in some documentation was not sufficient to outweigh the preponderance of the evidence to the contrary. The court held that there was not partial performance of the primary obligation under the Master Franchise Agreement (e.g., no payment of fees or opening of stores). *Id.* at 669. Without performance of critical components of the alleged legally binding agreement, the partial performance claim fails.

## 2. Promissory Estoppel

The legal concept of “promissory estoppel” can be invoked to preclude a party from relying upon the non-binding character of what is otherwise a legally unenforceable writing.

The elements for promissory estoppel are as follows:

- (1) a promise;
- (2) the foreseeability of the promisee’s reliance;
- (3) actual, reasonable substantial reliance by the promisee on the promise; and
- (4) damages.

*Henderson v. Texas Commerce Bank-Midland, N.A.*, 837 S.W.2d 778, 782 (Tex. App.--El Paso 1992, writ denied); and *FDIC v. Perry Bros., Inc.*, 854 F. Supp. 1248, 1267 (N.D. Tex. 1994), *aff’d in part, rev’d in part*, No. 94-40630, *unreported per curiam opinion* (5<sup>th</sup> Cir. 1995) (citing *English v. Fischer*, 660 S.W.2d 521 (Tex. 1983)).

Promissory estoppel may be asserted when one party makes a promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee, which does induce such action or forbearance and when an injustice can be avoided only by the enforcement of the promise. *Id.*

Although normally a defensive theory, promissory estoppel has increasingly been pled as an affirmative cause of action. *Farah v. Mafrige & Kormanik, P.C.*, 927 S.W.2d 663, 672 (Tex. App.--Houston [1<sup>st</sup> Dist.] 1996, writ denied). The Texas Supreme Court stated that promissory estoppel is defensive in nature in that it does not create a contract where none existed before, but only prevents a party from insisting upon strict legal rights when to do so would be unjust. *Wheeler v. White*, 398 S.W.2d 93, 96 (Tex. 1965). In *Wheeler*, the Texas Supreme Court applied promissory estoppel to allow enforcement of an oral agreement to lend money which the Court of Appeals found unenforceable due to vagueness.

The function of waiver or estoppel is to preserve rights, not to create independent causes of action. . . . Waiver and estoppel are defensive in nature and operate to prevent the loss of existing rights. They do not operate to create liability where it does not otherwise exist.

*Hruska, et ux. v. First State Bank of Deanville, et al.*, 747 S.W.2d 783, 785 (Tex. 1988).

In *State Nat’l. Bank v. Academia, Inc.*, 802 S.W.2d 282 (Tex. App.--Corpus Christi 1990, writ denied), the court held that a contract otherwise unenforceable due to the parol evidence rule could not be enforced under a promissory estoppel cause of action. *Academia* supports a defense that no justifiable reliance is possible on a contract otherwise unenforceable under section 26.01 of the Texas Business and Commerce Code (Texas Statute of Frauds). *See also Farah v. Mafrige & Kormanik, P.C.*, 927 S.W.2d 663, 672 (Tex. App.--Houston [1<sup>st</sup> Dist.] 1996, writ denied). Further, the affirmative defense of limitations applies to promissory estoppel. *Id.*

Promissory estoppel requires extraordinary circumstances such as those outlined in the *Texaco, Inc. v. Pennzoil Co.*, 729 S.W.2d 768 (Tex. App.-Houston [1<sup>st</sup> Dist] 1987 writ ref’d, n.r.e.), *cert. dismiss’d* 108 S. Ct. 1305 (1988). In *Texaco v. Pennzoil*, Pennzoil reached an agreement in principal to acquire

Getty Oil but no formal documentation was executed. Texaco stepped in and negotiated a binding agreement to acquire Getty Oil, thereby cutting off Pennzoil. Pennzoil and Getty previously signed a Letter of Intent, produced a press release that they had reached a “deal,” and then took other actions consistent with a completed agreement. Under the complex circumstances involved, which related to a corporate acquisition under New York law, the court held that the parties intended that the Letter of Intent be binding based on a review of the following factors:

- Whether a party expressly reserved the right to be bound only when a written agreement was signed;
- Whether there was partial performance by one of the parties that the party disclaiming the contract accepted;
- Whether all essential terms of the alleged contract were agreed upon; and
- Whether the complexity or magnitude of the transaction was such that a formal executed writing would normally be expected.

As a result of the holding that the Getty/Pennzoil Letter of Intent was drafted to be binding, the court held that Texaco had tortiously interfered with Pennzoil’s rights, thus resulting in a significant verdict.

The parties to a transaction should be careful that their actions are consistent with the non-binding character of the Letter of Intent. If one party can assert that the course of conduct of the other party led to a substantial change in position by a party acting in reasonable reliance on those actions, then the normally non-binding Letter of Intent may be held to become binding based upon the equitable legal principle of estoppel.

### 3. Fraudulent/Negligent Misrepresentation

Another cause of concern regarding Letters of Intent is fraudulent/negligent misrepresentation. The elements are as follows:

- A business relationship;
- Representation made by one party intended to be relied upon by the other party;
- Reasonable reliance;
- Representation either falsely made (and the party making the representation knew it)[fraudulent misrepresentation] or recklessly made (with the party failing to check out its validity)[negligent misrepresentation]; and
- Damage to the party.

See *Federal Land Bank Ass’n v. Sloan*, 825 S.W.2d 439, (Tex. 1991) and *McCamish, Martin, Brown & Loeffler v. Appling*, 991 S.W.2d 787 (Tex. 1999) discussing negligent misrepresentation and *State Nat’l. Bank of El Paso v. Farah Mfg. Co.*, 678 S.W.2d 661, 682 (Tex. App.--El Paso 1984, writ dism’d by agr.) and *T.O. Stanley Boot Co. v. Bank of El Paso*, 847 S.W.2d 218, 222 (Tex. 1990) discussing fraudulent misrepresentation.

Plaintiffs asserting fraudulent/negligent misrepresentation have three major proof obstacles:

- *reasonable* reliance,
- misrepresentation of an *existing fact*, and
- *intent* [for fraudulent misrepresentation].

Proving reasonable reliance in the context of a well-drafted Letter of Intent, particularly if the defendant has been careful in documenting its course of dealings with the plaintiff, is difficult.

In a commercial real estate setting, this cause of action could arise when a landlord signs a Letter of Intent, makes verbal representations to the potential tenant that the transaction will be consummated, and the tenant then materially changes its position by terminating its current lease, or, perhaps, by taking possession of the leased premises. If the landlord then tries to change the deal, based on the non-binding nature of the Letter of Intent, the doctrine of fraudulent/negligent misrepresentation will operate to bind the landlord to the transaction.

For discussion of fraudulent misrepresentation in the context of a real estate Letter of Intent, see *HK Partners, Inc. v. Power Computing Corporation*, 1999 WL 332573 (Tex. App.--Austin 1999, unpublished opinion), where the court held not only that fraudulent misrepresentation was not a proper claim, but even if it was, there was a lack of evidence to overturn a motion for summary judgment denying the fraudulent misrepresentation of claim in the context of a pre-development agreement with contingent language.

#### 4. Deceptive Trade Practices Act

A consumer may maintain an action under the Texas Deceptive Trade Practices-Consumer Protection Act (“DTPA”) for a commercial real estate transaction of \$500,000 or less. TEX. BUS. & COM. CODE § 17.41 et. seq. A cause of action can be based on an otherwise non-binding Letter of Intent. See *Investors, Inc. v. Hadley*, 738 S.W.2d 737 (Tex. App.--Austin 1987, writ denied); *Security Bank v. Dalton*, 803 S.W.2d 443, 452 (Tex. App.--Fort Worth 1991, writ denied). The lower proof requirements and statutory penalties of the DTPA can be problematic if an otherwise non binding Letter of Intent is coupled with a course of dealing indicating a binding agreement.

#### 5. Real Estate Fraud Act

The Texas Real Estate Fraud Act, section 27.01 of the Texas Business and Commerce Code, might be alleged to apply to a Letter of Intent. The act requires an allegation that misrepresentations were made to induce a party to enter a “contract”. Where a Letter of Intent has binding provisions, it clearly is a contract within contemplation of the act, but where it is clearly stated to be non-binding, an argument can be made that it is not a contract. In most instances where negligent/fraudulent misrepresentation is alleged, this act can also be alleged.

### F. Defenses to Alleged Binding Letter of Intent

#### 1. Clear Non-Binding Language

Many clients are unsure if a statement that a Letter of Intent is non-binding is, itself, binding. The issue addressed by such a statement is the requirement that there be intent to enter into a contract. This intent requirement is eliminated by a clear statement the Letter of Intent is non-binding. See *John Wood Group USA, Inc. v. ICO, Inc.*, 26 S.W.3d 12 (Tex. App.--Houston [1<sup>st</sup> Dist.] 2000, pet. denied); *Wiley v. Bertelsen*, 770 S.W.2d 878 (Tex. App.--Texarkana 1989, no writ); *Scott v. Ingle Bros.*, 489 S.W.2d 554 (Tex. 1972). However, merely referencing a more definitive agreement to be executed later is not sufficient for an otherwise complete Letter of Intent to be considered a binding contract. *Garner v. Boyd*, 330 F. Supp. 22 (N.D. Tex. 1970); *Foreca, S.A. v. GRD Dev. Co.*, 758

S.W.2d 744 (Tex. 1988). Performance of the transaction referenced in the Letter of Intent without a formal contract indicates an intent for it to be a binding contract. *Houston Chronicle v. McNair Truck Lease*, 519 S.W.2d 924 (Tex. App.--Houston [1<sup>st</sup> Dist] 1975, writ ref'd n.r.e.).

## 2. Lack of Description

A real estate contract requires a legally sufficient description, which may not rely on extrinsic evidence except to reasonably identify the property based on information contained in the contract. See *Wilson v. Fisher*, 188 S.W.2d 150 (Tex. 1945); *Morrow v. Shotwell*, 477 S.W.2d 538 (Tex. 1972); *Estate of Eberling v. Fair*, 546 S.W.2d 329 (Tex. App.--Dallas 1976, writ ref'd n.r.e.). Many Letters of Intent fail to have legally sufficient legal descriptions.

## 3. Lack of Consideration

There must be the exchange of something of value ("consideration") for agreements to be binding. Where a Letter of Intent contains a reference to a feasibility review period, with a clearly stated right for the buyer to terminate during that review period without forfeiting any earnest money, even if the Letter of Intent (or portions thereof) is intended to be binding, it is not likely to be enforced due to the lack of consideration for the agreement. A contract that lacks consideration lacks mutuality of obligation and is therefore unenforceable. *Federal Sign v. Texas S. Univ.*, 951 S.W.2d 401 (Tex. 1997), *superseded by statute on other grounds*.

However, even without monetary payment, a court may find consideration for an enforceable contract. *Copeland v. Alsobrook*, 3 S.W.3d 598 (Tex. App.--San Antonio 1999, writ denied). In *Copeland*, the Court held:

"Consideration is a present exchange bargained for in return for a promise. . . . It can be either a benefit to the promisor or a detriment to the promisee. . . . A promise for a promise is sufficient consideration."

*Id.* at 606 (citing *Crest Constr., Inc. v. Murray*, 888 S.W.2d 931 (Tex. App.--Beaumont, 1994, *rev'd on other grounds*, 900 S.W.2d 342, Tex. 1995)).

## 4. Unsigned Letter of Intent

Sometimes the parties may have exchanged drafts of a Letter of Intent but never signed them. This lack of signature can be asserted as reflecting the lack of intent which is critical to the making of an enforceable contract. Further, where there has simply been an exchange of Letters of Intent but no single Letter of Intent has been signed by both parties, the same argument can be made. In *RHS Interests, Inc. v. 2727 Kirby, Ltd.*, 994 S.W.2d 895 (Tex. App.--Houston [1<sup>st</sup> Dist.] 1999, no pet.), the court held that a unilateral Letter of Intent sent after a telephone call between the buyer and seller's broker was not sufficient to establish a binding contract where the language in the Letter of Intent clearly reflected that there were further negotiations contemplated. However, in *Hardin Constr. Group, Inc. v. Strictly Painting*, 945 S.W.2d 308, 313 (Tex. App.--San Antonio 1997, orig. proceeding), the court held that an unsigned contract (in this case a construction contract) together with indications that the parties had agreed to all but one provision (which the court held was not an "essential term" of the contract), and substantial performance by one party, constituted an enforceable contract.

## 5. Lack of Essential Terms

To be an enforceable contract, a court must be able to find that the document is sufficiently definitive to set forth the essential terms such that it can be inferred that the parties meant to be bound. The court in *Texas Oil Company v. Tenneco, Inc.*, 917 S.W.2d 826, 830-31 (Tex. App.--Houston [14<sup>th</sup> Dist.] 1994), *judgment reversed in part on other grounds by* 958 S.W.2d 178 (Tex. 1997), set forth a helpful list of issues in determining whether a Letter of Intent for sale of a company was sufficient definitive to be enforceable. Those guidelines are as follows:

- The rules regarding indefiniteness of material terms of a contract are based on the concept that a party cannot accept an offer so as to form a contract unless the terms of that contract are reasonably certain. (Citing Restatement [Second] of Contracts §33(1) (1991)).
- The actions of the parties may conclusively establish their intent to enter a binding agreement, even if some terms are left for a future agreement.
- Texas courts prefer to validate transactions rather than void them.
- A court may not create a contract where none exists and generally may not interpolate or eliminate material terms, however, parties may agree on some terms sufficiently to create a contract, leaving other terms for later negotiation. Further, a court may uphold an agreement by supplying missing terms, such as implying a reasonable price.
- Contract terms are reasonably certain "if they provide a basis for determining the existence of a breach and for giving an appropriate remedy". This is in line with the policy that parties, and not the courts, should make contracts.
- Where the parties intended to make an agreement and there is a certain basis for granting a remedy, courts should find the contract terms definitive enough to provide a remedy. Uncertainty of terms, however, can preclude one remedy without affecting others. For example, less certainty is necessary in a suit for damages than one for specific performance.
- Where the parties are agreeing to make a future contract and the agreement leaves material terms to be agreed upon later, that agreement is not definitive and specific as to material and central terms and, is therefore, unenforceable.

## 6. Disguised Contract Claims

Courts are increasingly realizing that many allegedly tort causes of action are simply repackaged contract claims. If the basis for the alleged tortious action is the breach of an alleged agreement between the parties, the claim sounds only in contract, not in tort. *Southwestern Bell Tel. Co. v. DeLanney*, 809 S.W.2d 493 (Tex. 1991).

## G. Supreme Court Case Law

The Texas Supreme Court has addressed Letters of Intent in two significant opinions which are frequently cited.

1. *Scott v. Ingle Bros. Pacific, Inc.*, 489 S.W.2d 554 (Tex. 1972).

The Court provided a helpful overview on the issue of when a written document constitutes a legally binding agreement. In *Scott*, a separate employment agreement was referenced in the purchase agreement for a business, but a separate employment agreement was never prepared or executed. The employee who would benefit from the employment agreement worked with the company for a period of time and was terminated. The employee sought to establish that the language in the purchase agreement was sufficient as a binding employment agreement. The Court reviewed the legal difficulties in resolving a dispute of this type.

“In this troublesome area, Corbin on Contracts is helpful. In Section 29, Partial Agreements – ‘Contracts to Make a Contract’, it is stated that:

‘People do business in a very informal fashion . . . A transaction is complete when the parties meant it to be complete. It is a mere matter of interpretation of their expressions to each other, a question of fact. \*\*\*

‘Even though certain matters are expressly left to be agreed upon in the future, they may not be regarded by the parties as essential to their present agreement. Furthermore, the terms left for future settlement may be within definite and prescribed limits.’ § 1 Corbin on Contracts (1963) 87-91.

The text continues, as relevant here:

‘The court will be more ready to find that the apparently incomplete agreement was in fact complete and required the payment and acceptance of a ‘reasonable’ price or a performance on ‘reasonable’ terms, in case the parties have already rendered some substantial performance or have taken other material action in reliance upon their existing expressions of agreement. The fact that they have so acted is itself a circumstance bearing upon the question of completeness of their agreement. \*\*\*

‘Two persons may fully agree upon the terms of a contract, knowing that there are other matters on which they have not agreed and on which they expect further negotiation. Such an expectation does not prevent the agreement already made from being an enforceable contract. This may be true even though they expressly provide in their agreement that the new matters, when agreed upon, shall be incorporated into a written lease or other formal document along with the contract already made.’ *Id.* at 93-95.

Corbin concludes that:

‘Often it is a difficult question of fact whether the parties have this understanding; and there are very many decisions holding both ways. . . . It is a question of fact that the courts are deciding, not a question of law. . . . In very many cases the question may properly be left to a jury.’ *Id.* at 87.

Further in this area, it is stated in 17 Am. Jur.2d., Contracts §28,

‘Many cases support the general rule that the fact, in and of itself, that parties to an . . . informal agreement intend that it shall be reduced to a . . . more formal contract will not necessarily prevent present, binding obligations from arising, notwithstanding the contemplated . . . formal contract is never drawn up and executed . . . .’ [at page 365]

‘However, the fact that parties to negotiations contemplated the drawing and execution of a formal written contract is regarded in numerous cases as evidence that they intended the prior . . . informal agreement . . . to be merely tentative and not final. It is not, of course, conclusive evidence of such an intention . . . .’ [at page 366]

The problem is discussed in §26 of the Restatement of Contracts. The Tentative Draft of §26 for the Restatement, Second, states the rule,

‘Manifestations of assent that are in themselves sufficient to conclude a contract will not be prevented from so operating by the fact that the parties also manifest an intention to prepare and adopt a written memorial thereof; but the circumstances may show that the agreements are preliminary negotiations.’

The comments thereunder suggest circumstances which may be helpful in determining whether a contract has been concluded. *See also Mississippi & Dominion S.S. Co. v. Swift*, 86 Me. 248, 29 A. 1063, 1066-1067 (1894), which is cited in the above tentative draft. This court said in *Simmons & Simmons Construction Co. v. Rea*, 155 Tex. 353, 286 S.W.2d 415, (1955), that ‘intention is usually an inference to be drawn by the fact finder from other facts and circumstances.’”

The court summarized the uncertainty in the area as follows: “an agreement simply to enter into negotiations for a contract later does not create an enforceable contract. But parties may agree upon some of the terms of the contract, and understand them to be an agreement, and yet leave other portions of an agreement to be made later.” 489 S.W.2d at 555.

This case demonstrates the importance of course of dealings in a contract dispute.

2. *Foreca S.A. v. GRD Development Company, Inc.*, 758 S.W.2d 744 (Tex. 1988).

In *Foreca*, the Court considered whether a handwritten term sheet initialed by the buyer and seller of certain equipment was an enforceable contract. The buyer notified the seller approximately four weeks after initialing the term sheet that the buyer was no longer interested in acquiring the equipment. The seller brought suit alleging breach of contract while the buyer asserted that the term sheet was only a non-binding Letter of Intent since one of its terms stated it was “subject to legal documentation.”

The Court held that the jury's determination that the term sheet was an enforceable contract was supported by evidence and that the “subject to legal documentation” language was not conclusive on the issue of intent to contract. The Supreme Court's discussion was quite instructive and is reproduced below.

“This case involves a situation increasingly common in business negotiations. GRD and Foreca negotiated over the sale of amusement park rides. Agreement was reached as to certain material terms, yet another formal document was contemplated by the parties. Was the contemplated formal document a condition precedent to the formation of a contract or merely a memorial of an already enforceable contract?”

Professor Corbin's writing is instructive on this question:

One of the most common illustrations of preliminary negotiation that is totally inoperative is one where the parties consider the details of a proposed agreement, perhaps settling them one by one, with the understanding during this process that the agreement is to be embodied in a formal written document and that neither party is to be bound until he executes this document. *Often it is a difficult question of fact whether the parties have this understanding; and there are very many decisions holding both ways. These decisions should not be regarded as conflicting, even though it may be hard to reconcile some of them on the facts that are reported to us in the appellate reports. It is a question of fact that the courts are deciding, not a question of law; and the facts of each case are numerous and not identical with those of any other case. In very many cases the question may properly be left to a jury.*

A. Corbin, *Corbin on Contracts* §30 at 97 (1963) (emphasis added). Professor Corbin is not alone among commentators in espousing this view. *See, e.g.*, J. Calamari & J. Perillo, *Contracts* § 2-7 (3d ed. 1987). Restatement (Second) of Contracts §27 (1979); Note, *Contemplated Written Agreements - Contract or Memorial*, 26 *Balor L.Rev.* 132 (1974); 17 *Am.Jur.2d Contracts* § 28 (1964).

This court quoted with approval, more than a decade ago, this excerpt from Professor Corbin's treatise. In *Scott v. Ingle Bros. Pacific, Inc.*, 489 S.W.2d 554 (Tex. 1972), we encountered a similar contract formation dispute. Scott sold a mop manufacturing plant to Ingle. The purchase agreement provided that an employment agreement ‘[had] been prepared’ whereby Scott would manage the business for five years at a stated salary. No such employment agreement had actually been reduced to writing. A dispute arose, and Ingle discharged Scott. Scott brought suit for breach of an employment contract. In a unanimous opinion, Chief Justice Greenhill posed the question before the court:

[W]as that portion of the ‘purchase agreement’ dealing with the employment of the seller, Scott, an enforceable contract? This depends upon the intention of the parties. An agreement simply to enter into negotiations for a contract later does not create an enforceable contract. But parties may agree upon some of the terms of a contract, and understand them to be an agreement, and yet leave other portions of an agreement to be made later.

*Scott*, 489 S.W.2d at 555. Thus, the intention of the parties would be determinative: ‘Whether the execution of a separate employment agreement was, and is, essential to a mutuality of assent is a question of the intention of the parties.’ *Id.* Upon restating the principle that intention is usually an inference to be drawn by the fact finder, the court held that whether the clause in the purchase agreement was meant to be a contract was for the

trier of fact to determine. *Id.* at 557. See Note, *Contemplated Written Agreements - Contract of Memorial*, 26 Baylor L.Rev. 132 (1974). See also *Preload Tech., Inc. v. A.B.&J. Constr. Co., Inc.*, 696 F.2d 1080, 1090 (5<sup>th</sup> Cir. 1982); *Kanow v. Brownshadel*, 691 S.W.2d 804, 806 (Tex. App.--Houston [1<sup>st</sup> Dist.] 1985, no writ); *Frank B. Hall & Co., Inc. v. Buck*, 678 S.W.2d 612, 629 (Tex. App. --Houston [14<sup>th</sup> Dist.] 1984, writ ref'd n.r.e.), *cert. denied*, 472 U.S. 1009, 105 S.Ct. 2704, 86 L.Ed.2d 720 (1985); *John E. Mitchell Co. v. Anderson*, 520 S.W.2d 927, 934 (Tex. Civ. App.--Waco 1975, writ ref'd n.r.e.); *Houston Chronicle Publ'g Co. v. McNair Trucklease, Inc.*, 519 S.W.2d 924, 928 (Tex. Civ. App.--Houston [1<sup>st</sup> Dist.] 1975, writ ref'd n.r.e.).

*Scott* guides our analysis today. Accordingly, we hold that it is a question of fact in this case whether the terms agreed to and embodied in the September 2 and October 19, 1983 writings were intended to be the final expressions of the contract or were only preliminary negotiations which the parties did not intend to have legal significance until execution of the contemplated legal documentation. This question was properly submitted to and answered by the jury in fulfillment of its fact finding responsibilities. In some cases, of course, the court may decide, as a matter of law, that there existed no immediate intent to be bound. This case, however, is not such a case. The evidence as to the intent of the parties is disputed. More important, the 'subject to legal documentation' language is not conclusive on intent to contract. See *Scott*, 489 S.W.2d at 556. The jury's resolution of this issue should be allowed to stand.”

This case demonstrates the importance of clear drafting in Letters of Intent.

#### H. Case Law from Recent Years

1. *RHS Interest, Inc. v. 2727 Kirby, Ltd.*, 994 S.W.2d 895 (Tex. App. -- Houston [1<sup>st</sup> Dist.] 1999, no pet.).

In *RHS Interest, Inc.*, a buyer submitted two successive Letters of Intent to the owner of an office building. The listing broker responded after receiving the second Letter of intent and gave verbal approval to the deal, with certain modifications. The broker followed up with a written letter confirming the terms of the transaction. The buyer's Letter of Intent form contained the following provisions:

“This offer is a summary of a transaction to be more fully described in an earnest money contract, the specifics of which will be negotiated in good faith. This letter serves only as an offer . . . and is not binding as an agreement unless and until a fully executed earnest money contract is signed.”

The listing broker's letter repeatedly mentioned “a binding purchase and sale agreement” and a “formal purchase and sale agreement”. A number of terms in the second of the buyer's Letter of Intent, such as time periods, earnest money and commissions were changed. Additionally, the broker's letter agreed to cease marketing efforts to allow the buyer to begin inspections. Buyer commenced inspections, but never signed a contract nor deposited any earnest money. Subsequently, the seller discontinued negotiations toward a contract.

Buyer sued for specific performance of the Letter of Intent as a binding contract. Seller asserted the following defenses:

- (1) no binding contract;
- (2) statute of frauds;
- (3) insufficient legal description;
- (4) lack of material terms; and
- (5) lack of consideration.

The trial court granted the seller's motion for summary judgment and the buyer appealed. On appeal, the court upheld the summary judgment on the basis of a lack of consideration. However, the court also held that there was no binding contract due to the language quoted above in the buyer's Letter of Intent and the seller's agent's acceptance letter. The court held there were clearly significant negotiations ahead and the parties did not contemplate to be bound by the exchange of Letters of Intent. In addressing the lack of consideration point, the court followed *Antwine v. Reed*, 199 S.W.2d 482 (Tex. 1947), where the Texas Supreme Court refused specific performance under a fully executed real estate contract since the buyer never tendered any earnest money. The court also noted that any money spent on inspections by the buyer was not substantial performance or other material action which would substitute for cash consideration because of the "preliminary" context of the exchanged Letters of Intent. The court did acknowledge that under different circumstances, where there had been substantial performance or other material action in reliance upon the transaction, that such actions would be a consideration substitute, citing *Scott v. Ingle Bros. Pacific, Inc.*, 489 S.W.2d 554 (Tex. 1972).

This case demonstrates a significant hurdle for a party seeking to enforce a Letter of Intent as a binding contract, even if clear non-binding language is not included.

2. *HK Partners, Inc. v. Power Computing Corporation*, 1999 WL 332573 (Tex. App.--Austin 1999, unpublished opinion).

In the *HK Partners* case, HK Partners formed a development team to respond to a request for proposal from Power Computing for construction of a manufacturing facility in Georgetown, Texas.

HK Partners' submission was accepted, but no formal contract was signed. Several drafts of a proposed pre-development agreement were exchanged over a three week period, but none were signed. Power Computing then changed its entire approach to the project, instructed HK Partners to discontinue its work, submit an invoice for work completed to date, and submit a new proposal conforming to Power Computing's new approach (wherein HK Partners would have a more limited role). HK Partners declined to submit a new proposal and submitted an invoice for \$250,000.00, which Power Computing refused to pay, claiming it was excessive.

HK Partners asserted that the pre-development agreement memorialized a "broader agreement" between the parties that HK Partners had been selected as the owner/developer/landlord of the entire project. Power Computing asserted that its sole purpose was to confirm that HK Partners was to proceed immediately with pre-development work and that Power Computing would compensate HK Partners on a "pay-as-you-go" basis. Power Computing filed a declaratory judgment action seeking to confirm that there was no contract for development of the entire project and that it was obligated only to pay the fair value of the pre-development work actually performed. HK Partners counterclaimed for breach of contract, fraud and negligent misrepresentation.

The appellate court upheld summary judgment granted in favor of Power Computing on the contract and fraud claims. Power Computing's promises to sign a pre-development agreement were

insufficient to create a binding contract. Further, the pre-development agreement itself was too indefinite to be enforced as a “broader agreement” relating to the entire project because it did not specify any of the material terms inherent in contracts to develop commercial real estate. Power Computing’s only promise was to sign a pre-development agreement either (i) affirmatively stating HK Partners would be the owner/developer/landlord or (ii) referencing a “continuing relationship” between the parties on the project. That promise did not provide the terms necessary to create a contract for the development of an entire manufacturing plant, since it failed to address issues such as scope of the project, budget, design, duration or lease terms.

The court also considered HK Partners' allegation of an “implied-in-fact” contract based on the course of dealings between the parties. An implied-in-fact contract requires a meeting of the minds of the parties as evidenced by their course of dealings. *See Haws & Garrett Gen. Contractors, Inc. v. Gorbett Bros. Welding Co.*, 480 S.W.2d 607, 609 (Tex. 1972). The conduct must evidence an objective assent to the terms of an agreement. The parties' conduct and course of dealings were insufficient to evidence the “broader agreement” for a binding contract to develop the entire project. The court also dispensed with the argument that the doctrine of promissory estoppel precluded Power Computing from denying an agreement existed, holding that promissory estoppel does not create a contract where none existed under contract law principles.

On the issue of fraud, the Court held that HK Partners alleged fraud and breach of contract based on essentially the same facts; that being Power Computing’s failure to allow HK Partners to be the owner/developer/landlord of the project. Therefore, although HK Partners couched a cause of action as common law fraud, it is really seeking to recover the benefit of the alleged contract. Since the real objective is to enforce the contract, it cannot use a fraud allegation to circumvent the unenforceability of the contract. In the related issue of fraudulent misrepresentation, HK Partners asserts that Power Computing fraudulently agreed to sign the pre-development agreement and later refused to do so. The court held that a promise of future performance constitutes actionable fraud only if the promise was made with no intention of performing it at the time it was made. Power Computing never denied that it promised to sign a pre-development agreement, only that it changed its mind regarding the direction of the project (presumably with a legitimate basis). Although the court indicated that failure to perform as promised is one factor that may be considered to establish deceitful intent of a party at the time the promise was made, standing alone, failure to perform is not evidence of fraud. Since that was the sole evidence produced by HK Partners, the fraudulent misrepresentation failed.

This case demonstrates that parties move forward in reliance on Letters of Intent at their own risk.

3. *John Wood Group USA, Inc. v. ICO, Inc.*, 26 S.W.3d 12 (Tex. App.--Houston [1<sup>st</sup> Dist.] 2000, pet. denied).

In *John Wood*, the appeal was argued by some of the best appellate lawyers in Texas and the opinion is well drafted and supported. A Letter of Intent was signed by a buyer and seller of a corporate division in a multi-million dollar transaction. The Letter of Intent stated it was “not binding”, but that the parties agreed to exercise “good faith efforts” to negotiated legally binding documents.

The critical provision reads as follows:

“15. *Binding Effect.* This Letter Agreement constitutes a summary of the principal terms and conditions of the understanding which has been reached regarding the sale

of certain assets to Purchaser [ICO]. *It does not address all of the terms and conditions which the parties must agree upon to become binding and consummated.* The Purchaser, however, does intend to move forward with its due diligence and expects to expend considerable sums to review the sellers' Business. In consideration therefor, the parties have agreed to make certain covenants of this Letter binding upon the parties notwithstanding the fact that not all details of the transactions have been agreed upon. *Accordingly, it is understood and agreed that this letter is an expression of the parties' mutual intent and is not binding upon them except for the provisions of paragraphs (4), (7), (9), (10), (11), (12), (13), and (14) hereof.* (Emphasis added)."

The parties could not agree on the actual book value of the division (the basis for the purchase price) and after the "no shop" period expired, the seller sold the division to another buyer. The jilted buyer sued for breach of the contract set forth in the Letter of Intent and fraud.

The buyer won on both claims, but elected to recover on the breach on contract claim, receiving an award of \$8,500,000 actual damages, \$2,700,000 punitive damages and \$4,500,000 contingent attorney's fees (40%) for a total recovery of \$15,700,000.

The appellate court reversed and rendered judgment for the seller on most issues, holding:

- a. If the Letter of Intent is unambiguous, the interpretation of it is a matter of law for the court, not a jury to determine. Generally, the intent to be bound is to be determined by the court.
- b. This Letter of Intent was nonbinding as a matter of law due to the use of the words "not binding," citing the *RHS Interests* case discussed earlier in this paper as well as a host of out of state cases.
- c. The court discussed policy considerations in interpreting Letters of Intent and stated the following:

"[T]he basic concept of a letter of intent is to provide the parties with a way to structure their agreement without entering a binding contract. However, the use of a letter of intent is not without risk. Absent careful drafting, the parties may find themselves bound by a letter agreement that does not contain all of the protections for which they would normally negotiate or for which due diligence is incomplete. Under some circumstances, a binding contract may be formed if the parties agree on the material terms, even through they leave open other provisions for later negotiation. . . . Similarly, a letter of intent may be binding even though it refers to the drafting of a future, more formal agreement. . . .

Therefore, a party who does not wish to be prematurely bound by a letter agreement should include a provision clearly stating that the letter is nonbinding, as such negotiations of liability have been held to be effective."

- d. Reaffirmed that an informal agreement may be binding without extensive legal documentation and listing the critical basic deal terms as (i) identification of the item to be sold, (ii) consideration and (iii) mutual consent (which was missing here).

e. Breach of a binding agreement to “cooperate and work in good faith and do all acts and things...reasonably required to effectively carry out or better evidence or perfect the full intent and meaning of this Letter Agreement”, will not support damages where the Letter of Intent was nonbinding, because (i) under Texas law an agreement to negotiate in the future is unenforceable, even if the agreement calls for a “good faith effort” in negotiation, citing *Maranatha Temple, Inc. v. Enterprise Prods. Co.*, 893 S.W.2d 92, 104 (Tex.App.--Houston [1<sup>st</sup> Dist.] 1994, writ denied) and (ii) the terms are too vague to be enforceable as a contractual obligation, citing *Richter v. Bank of America National Trust and Savings Association*, 939 F.2d 1176 (5<sup>th</sup> Cir. 1991)(applying Texas law in holding that an alleged oral agreement by a bank to negotiate a reasonable loan restructure was not enforceable because it was too indefinite).

f. The “good faith” obligation was superfluous, as good faith is inputted in all contracts through the Uniform Commercial Code. Tex. Bus. & Com. Code Section 1.203 states “...[e]very contract or duty within this title imposes an obligation of good faith in its performance or enforcement.”

g. Benefit of the bargain damages are not recoverable in the event of the breach of a “no shop” prohibition in a Letter of Intent which is nonbinding, although liquidated damages set forth in a properly drafted provision will be enforceable.

h. Fraud will not substitute for the contract cause of action for a clearly nonbinding Letter of Intent as there can be no false promise that the Letter of Intent was binding if it clearly states it is nonbinding. Thus, the buyer could not have relied on the alleged fraud in entering into the Letter of Intent thinking it was binding.

4. *COC Services v. CompUSA, Inc.*, 150 S.W.3d 654 (Tex. App.—Dallas 2004, pet. denied).

Like *John Wood*, *COC Services* involved very knowledgeable attorneys and a substantial amount of money. *COC Services* followed *John Wood* and discussed additional issues that were unique to this case. This case involved a franchise deal to establish CompUSA stores in Mexico; however, the deal never materialized. CompUSA and COC Services (COC) entered into negotiations for a Master Franchise Agreement (MFA) in which COC would be master franchisee. Another group of parties (Carso) was contemplated to be the subfranchisee. However, Carso never became the subfranchisee and bought CompUSA instead. As a result, COC brought actions for breach of contract and tortious interference with contract against CompUSA and Carso.

CompUSA and COC initially signed a Letter of Intent, which stated the parties would not enter into any agreement with any other party with respect to the establishment of any similar business in Mexico, until the expiration of the Letter of Intent. The Letter of Intent also stated that the parties intended to execute an MFA, among other agreements. The Letter of Intent stated the following, in pertinent part:

“However, in the event that the MFA [and] License Agreement for the initial Licensed Business to be executed by Initial Licensee Entity ... are not executed ... on or before [the Expiration Date] ... this Letter of Intent will expire, *and neither of the undersigned shall have any further obligation or liability hereunder with respect to a potential master franchise or license for the development and operation of the Stores....* (Emphasis added).”

After CompUSA failed to execute the MFA, COC filed suit. This case differed from *John Wood* because it involved the issue of partial performance. This issue was raised by COC, which argued that, despite the terms of the Letter of Intent, through partial performance of the MFA, the parties' expressed mutual consent to be bound to the MFA. Thus, COC argued that post-Letter of Intent conduct raised a fact issue on intent. The court noted that *John Wood* acknowledged partial performance as one factor to consider in determining whether the parties to a preliminary agreement intended to be bound. In dicta, *John Wood* cited a five-factor test that looks to (1) the language of the agreement, (2) the context of the negotiations, (3) the existence of open terms, (4) partial performance, and (5) the necessity of putting the agreement in final form, as indicated by the customary form of such transactions (citing *Arcadian Phosphates, Inc. v. Arcadian Corp.*, 884 F.2d 69 (2d Cir.1989)).

In applying this test to the facts surrounding the Letter of Intent, the court concluded that the first factor, the language of the Letter of Intent, is most important. The Letter of Intent expressly stated that neither party would be bound to the detailed MFA, unless it was executed. Also, there was no probative evidence to raise a fact question whether the parties intended to abrogate the "no-further obligation" provision of the Letter of Intent and to be bound to the incomplete and unexecuted MFA. The court also addressed the other factors and noted, among other things, that the context of the negotiations always included a trilateral arrangement with a third party, there were open price terms that were essential to the economic structure of the agreement and that COC never partially performed its primary obligations under the MFA. Thus, the court held that the parties did not agree to be bound to the MFA and COC's cause of action for breach failed. The terms of the Letter of Intent prevailed.

This case demonstrates the potential difficulties in overcoming the explicit language contained in Letters of Intent.

5. *Electronic Bankcard Systems, Inc. v. Retriever Industries, Inc.* 2003 WL 204717 (Tex. App.-Houston [1<sup>st</sup> Dist.] 2003, unreported opinion).

In *Electronic Bankcard*, Retriever Industries, Inc. (RII) drafted a letter entitled "Letter of Intent" which was signed by it and Electronic Bankcard Systems (EBS) regarding RII acquiring assets from EBS. This letter followed contentious disputes between the parties regarding prior business relationships. EDS later declined to sell the assets and RII sued to enforce the letter as a binding contract. The letter did not have affirmative non-binding language and indicated a more detailed agreement would be forthcoming. When disagreements surrounding the letter arose, EBS asserted it was merely agreeing to cooperate in future negotiations for the assets listed in the Letter of Intent. To the contrary, RII argued that the Letter of Intent was binding. The trial court held the letter to be a binding agreement.

The appeals court provided the following pertinent information regarding the Letter of Intent:

"The letter began with the following statement: 'In accordance with our letters dated February 23, 1995 to you and your attorney, Joseph E. Mudd, our agreement with you and EBS has been terminated.' The letter went on to inform Francis that, although he was not entitled to compensation following his termination, appellees were 'willing to proceed with an offer' to purchase various assets held by Francis and EBS. The letter requested that Francis and EBS have their attorney 'draft an agreement covering these points,' and to then fax the agreement to appellees. The letter ended with the following statement:

‘My signatures below indicate my unconditional acceptance and agreement with the terms and conditions outlined above (of this ‘Letter of Intent’) for EBS and myself. I also agree to sign a more detailed ‘Agreement’ for myself and EBS that stipulates the above terms and conditions.’”

The court cited *Foreca, S.A. v. GRD Dev. Co., Inc.*, 758 S.W.2d 744, 745 (Tex. 1988) and *Scott v. Ingle Bros. Pacific, Inc.*, 489 S.W. 2d 554, 555 (Tex. 1972) for the proposition that when parties engage in negotiations contemplating future agreements and the party’s intent is ambiguous, then the intent of the parties to be bound should be determined by the trier of fact.

The appeals court held the letter contained statements that, taken together, created an issue of fact as to whether the parties intended to be bound. First, the title “Letter of Intent” could raise an inference that the purpose of the letter was to outline what the parties intended to do in the future. Second, the statement that the parties were “willing to proceed with an offer” could mean that the letter itself was not an offer, but that the parties’ contemplated a future offer for the assets listed in the letter. Finally, the language “I also agree to sign a more detailed Agreement” could mean that the letter was only an outline for future negotiations and agreements. Consequently, the court concluded that a fact question existed and that the letter was not, as a matter of law, a binding contract.

Like *Foreca*, this case reiterates the need for clear drafting and the need to include non-binding language, or a letter may become a binding contract.

## **VII. CONCLUSION**

Understanding the purpose of Letters of Intent and minding simple rules in drafting Letters of Intent will help move the lease transaction forward quickly and efficiently to formal lease execution.

**APPENDIX "A"**  
**"Term Sheet" Letter of Intent Form**  
**(Using State Bar Format)**

**Letter of Intent (Office Lease)**

This Letter of Intent to lease real property is between Landlord and Tenant as identified below and is effective on the date of the last of the signatures by Landlord and Tenant.

**Non-Binding Terms of Proposed Transaction**

**Date:**

**Landlord:**

**Landlord's Address:**

**Tenant:**

**Tenant's Address:**

**Premises**

Approximate Square Feet: \_\_\_\_\_ net rentable, \_\_\_\_\_ usable (\_\_\_\_% add on factor)

Name of Building:

Street Address/Suite:

City, State, Zip:

**Base Rent (monthly): \$**

**Adjustments to Base Rent:**

**Term (months):**

**Commencement Date:**

**Termination Date:**

**Renewals:**

**Expansions:**

**Right of First Refusal:**

**Security Deposit: \$**

**Holdover Rent: % of Base Rent**

**Permitted Use:**

**Signage:**

**Liability Insurance:** Death/Bodily Injury: \$ \_\_\_\_\_ Property: \$ \_\_\_\_\_

**Guarantors:**

**Tenant's Pro Rata Share: %**

**Parking: \_\_\_\_\_ reserved at \$ \_\_\_\_\_ monthly, \_\_\_\_\_ unreserved at \$ \_\_\_\_\_ monthly**

**Essential Services-**heating, ventilating, air conditioning, water, and utility connections reasonably necessary for occupancy of the premises for the permitted use in building standard levels and quantities.

**Operating Expenses-** Includes \_\_\_\_\_

Excludes \_\_\_\_\_

**Building Operating Hours:** \_\_\_\_\_

**Common Areas:** \_\_\_\_\_

**Tenant Allowance: \$**

**Floor plan of Premise: Exhibit A**

**Approved Tenant Space Plan: Exhibit B**

**Work letter: Exhibit C**

[INSERT OTHER APPLICABLE PROVISIONS]

**Tenant Obligations:**

1. Lease the premises from the commencement date to the termination date.
2. Accept the premises in their present condition "as is," the premises being currently suitable for Tenant's intended use, except of alterations made pursuant to the Work letter.
3. Obey all laws, ordinances, orders, and rules and regulations applicable to the use, condition, and occupancy of the premises, including the rules and regulations of the building adopted by Landlord.
4. Pay monthly, in advance, on the first day of the month, the base rent to Landlord at Landlord's address.
5. Pay, as additional rent, \_\_\_\_\_.
6. Pay a late charge of \_\_\_% of any rent not received by Landlord by the \_\_\_\_\_ day of the month in which the rent is due.
7. Pay for all utility services used by Tenant and not provided by Landlord and Tenant's pro rata share of any utility services provided by Landlord.
8. Pay monthly Tenant's pro rata share of estimated monthly operating expenses, and annually, the actual operating expenses, within \_\_\_ days of notice of the amount due.
9. Allow Landlord to enter the premises to perform Landlord's obligations, inspect the premises, and show the premises to prospective purchasers or tenants.
10. Repair, replace, and maintain any part of the premises that Landlord is not obligated to repair, replace, or maintain, normal wear excepted.
11. Repair any damage to the premises caused by Tenant.
12. Submit in writing to Landlord any request for repairs, replacement, and maintenance that are the obligations of Landlord.
13. Maintain public liability insurance for the premises and the conduct of Tenant's business, naming Landlord as an additional insured, in the amounts stated in the basic lease terms and definitions.
14. Maintain insurance on Tenant's personal property.
15. Deliver certificates of insurance to Landlord before the commencement date and thereafter when requested.
16. Indemnify, defend, and hold Landlord harmless from any loss, attorney's fees, expenses, or claims arising out of use of the premises.
17. Deliver to Landlord a financing statement perfecting the security interest.
18. Vacate the premises on termination of this lease.

**Tenant Limitations:**

1. Use the premises for other than the permitted purpose.
2. (a) Create a nuisance, (b) interfere with any other tenant's normal business operations or Landlord's management of the building, (c) permit any waste, or (d) use the premises in any way that is extra hazardous, would increase insurance premiums, or would void insurance on the building.
3. Change locks or alter the premises, except as provided in the Work letter or \_\_\_\_\_.
4. Assign this lease or sublease any portion of the premises without Landlord's written consent, except \_\_\_\_\_.

**Landlord Obligations:**

1. Lease to Tenant the premises from the commencement date to the termination date.
2. Obey all laws, ordinances, orders, and rules and regulations applicable to the use, condition, and occupancy of the building.
3. Provide normal utility service connections to the building.
4. Repair, replace, and maintain the (a) roof, (b) foundation, (c) parking and common areas, (d) structural soundness of the exterior walls, doors, corridors, windows, and (e) other structures or equipment serving the premises.
5. Insure the building against all risks of direct physical loss in an amount equal to at least 90 percent of the full replacement cost of the building as of the date of the loss and liability; Tenant will have no claim to any proceeds of Landlord's insurance policy.
6. Return the security deposit to Tenant, less itemized deductions, if any, within thirty days after the termination of the lease.

7. Advance the Tenant Allowance per the Work letter.
8. Provide the essential services.
9. Provide an annual accounting of operating expenses passed through to Tenant.

**Landlord Limitations:**

1. Interfere with Tenant's possession of the premises as long as Tenant is not in default.
2. Unreasonably withhold consent to a proposed assignment or sublease.

**Specific Matters:**

1. **Alterations-** \_\_\_\_\_.
2. **Rent Abatement-** \_\_\_\_\_.
3. **Landlord's Lien-** \_\_\_\_\_.
4. **Alternative Dispute Resolution-** Landlord and Tenant shall submit in good faith to mediation before filing a suit for damages.
5. **Limitation of Warranties.** There are no implied warranties of merchantability, of fitness for a particular purpose, or of any other kind.

**Representations and Warranties of the Parties**

[INSERT RELEVANT REPRESENTATIONS AND WARRANTIES]

**Disclosures**

[INSERT RELEVANT DISCLOSURES]

**Contingencies**

[INSERT RELEVANT CONTINGENCIES]

Each party agrees to exercise good faith efforts to satisfy any contingency within its reasonable control.

**Binding Agreements Relating to Proposed Transaction**

1. The Lease shall be prepared on the [ALTERNATIVES-most current form of lease promulgated by the State Bar of Texas in its Real Estate Forms Manual/ Texas Association of Realtors Commercial lease form/ Landlord's standard lease form]. The Lease shall be prepared by Landlord's Attorney within \_\_\_ days of the effective date of this letter and distributed contemporaneously to all parties by [messenger/fax/over night delivery/email].
2. If the Lease is not finally negotiated, signed and tendered to Landlord with the security deposit and first month's rent within \_\_\_ days of the effective date of this letter, this letter shall terminate.
3. Landlord agrees to abate all marketing efforts for the Premise during the term hereof. Any existing signs may remain. Any ordered advertising shall be canceled, if cancelable without penalty, otherwise ordered advertising may proceed, but no additional advertising may occur. Brokers and prospective buyers will not be shown the Premises and may be given only currently available printed information about the Premises prepared by Landlord's Broker.

INSERT OTHER APPLICABLE ITEMS]

**Binding/Non-Binding Nature**

LANDLORD IS NOT LEGALLY BOUND TO ENTER INTO THE TRANSACTION DESCRIBED HEREIN UNLESS AND UNTIL A COMPLETE LEASE IS EXECUTED BY LANDLORD AND TENANT AND TENDERED TO LANDLORD TOGETHER WITH THE SECURITY DEPOSIT AND THE FIRST MONTH'S RENT. LANDLORD IS BOUND TO COMPLY WITH THE PROVISIONS SPECIFICALLY LISTED AS BINDING AGREEMENTS. [LANDLORD ACKNOWLEDGES RECEIPT OF \$10.00 AND OTHER VALUABLE CONSIDERATION, WHICH LANDLORD ACCEPTS AS LEGALLY SUFFICIENT TO BIND LANDLORD TO PERFORM THE BINDING AGREEMENTS].

THIS LETTER OF INTENT SUPERSEDES ALL PRIOR RELATED DISCUSSIONS AND AGREEMENTS BETWEEN THE PARTIES REGARDING THE PREMISES.

**Exhibits:**

- “A”- Floor plan of Premises [Not Attached]**
- “B”- Tenant Site Plan [Not Attached]**
- “C”- Work letter [Not Attached]**

\_\_\_\_\_  
[Name and title of landlord]

Date signed:

\_\_\_\_\_  
[Name and title of tenant]

Date signed:

**APPENDIX "B"**  
**Letter of Intent Letter Form**

[Letterhead of Broker]

Address of Prospective Tenant or their Broker

RE: Letter of Intent to Lease [Description of leased premises] ("Premises")

Dear Sir:

On behalf of Landlord, I am authorized to offer to lease the Premises to Tenant on the following terms.

This letter of intent contains both non-binding provisions relating to the real estate transaction itself, and binding provisions relating to the actions of the parties with respect to certain procedures relating to inspection of the Premises and the process toward negotiation and documentation of a legally binding agreement.

This letter of intent supersedes all prior related discussions and agreements between the parties regarding the Premises.

**Non-Binding Understandings Regarding the Real Estate Transaction:**

1. Premises. The Premises shall consist of approximately \_\_\_\_\_ rentable square feet (\_\_\_\_\_ usable square feet) on the \_\_\_\_\_ floor, Suite \_\_\_\_\_. The common area factor for the Premises is \_\_\_\_\_.
2. Building. The Premises is located in \_\_\_\_\_.
3. Use. The Premises shall be used for general office purposes.
4. Commencement Date. Approximately \_\_\_\_\_.
5. Term. \_\_\_\_\_ years.
6. Base Rent.            Years                    Rental Rate Per Rentable Sq. Ft.
  
7. Operating Expenses. Tenant will be responsible for its pro rata share of operating expenses and real estate taxes in excess of [ALTERNATIVES- actual <insert base year. amounts/\$\_\_\_\_ per sq. ft] ("Expense Stop") grossed up to \_\_\_\_\_% occupancy.

Increases in controllable operating expenses will be capped at \_\_\_\_\_% on a cumulative and compounding basis. Controllable operating expenses will be defined as those expenses within the reasonable control of Landlord, thus, excluding taxes, insurance, utilities, etc.

The net Base Rent (Base Rent less the Expense Stop) will be adjusted annually [ALTERNATIVES-in accordance with the Consumer Price Index <DEFINE WHICH CPI>/\_\_\_\_%]

8. Electricity. Tenant shall pay a pro rata share of the Building's electric utility expenses incurred in the operation of the Building (estimated to be \$\_\_\_\_\_ per rentable sq. ft. in \_\_\_\_\_). Above-standard electrical usage is metered and billed to tenants on an "as used" basis.
9. Security Deposit. A Security Deposit equal to one (1) month of Base Rent is required to be submitted when the Lease is signed.
10. Parking. \_\_\_\_\_
11. Lease Assumption. Landlord will reimburse Tenant for its current lease rent obligation for a period of up to \_\_\_\_ months in an amount not to exceed \$\_\_\_\_\_ per month. Any proceeds from subleasing Tenant's existing office shall be distributed to Landlord.
12. Space Planning. Landlord's architect will provide initial space planning and interior design services at no charge to Tenant. Landlord will provide an allowance for space planning, construction drawings and mechanical, electrical and plumbing documentation equal to the lesser of \$\_\_\_\_\_ per rentable square foot or the actual cost of drawings.
13. Base Building Conditions. Landlord will provide the Premises in its current shell condition with: (I) ceiling grid installed, (ii) HVAC distribution equipment installed, (iii) fire sprinklers in place, (iv) ceiling tiles and lights stacked on floor, (v) building standard window covering installed, (vi) building columns drywalled taped and bedded, (vii) surfaces beneath or above exterior windows furred, drywalled, taped and bedded and (viii) finished concrete floors.
14. Tenant Improvements. The space will be provided in its "as-is" condition. In addition, Landlord will provide an allowance of \$\_\_\_\_\_ per net rentable square foot for the design and construction of standard and above-standard improvements. All improvements to the Premises will be paid for with this allowance including any required demolition and finished ceiling (and above ceiling) improvements.

Landlord will contract with the construction contractor, manage the construction, act as liaison between Tenant, the contractor and the designer and coordinate the relationship between the construction, the building and the building's systems. In consideration for its construction supervision services, Landlord will earn a construction management fee equal to \_\_\_\_\_percent (\_\_\_%) of the total construction costs.

[ALTERNATIVES- The tenant improvements will be competitively bid to at least \_\_\_\_\_ (\_\_\_) general contractors that have been approved by Landlord and Tenant. All construction information will be made available to Tenant. Landlord does not require the use of any specific contractors or subcontractors.]

15. Funding of Additional Improvements. Should the cost of construction for Tenant's offices exceed the Tenant Allowance, Landlord agrees to amortize the additional build-out costs up to an amount equal to \$\_\_\_\_\_ per rentable square foot over the term of the lease at the annual interest rate of \_\_\_\_\_% compounded and payable monthly.
16. Moving Allowance. Landlord will reimburse Tenant for actual third party costs directly associated with (I) relocating Tenant's furniture, fixtures and equipment, (ii) telephone installation and (iii) stationery replacement in an amount equal to the lesser of \$\_\_\_\_\_ per rentable square foot or the actual costs incurred.

17. Refurbishment. At the end of the \_\_\_\_ year of the Lease, Landlord will provide a refurbishment allowance of \$\_\_\_\_ per rentable square foot for space initially occupied. The refurbishment allowance must be utilized to remodel or improve Tenant's Premises within \_\_\_\_ (\_\_) months of its availability.
18. Cancellation Option. Tenant will be provided with a Cancellation Option at the end of the \_\_\_\_ year of the Lease subject to the following provisions:
- 1) Tenant shall repay the unamortized portion of all costs (at an interest rate of \_\_\_\_% per year) incurred by Landlord in connection with the Lease.
  - 2) Tenant will pay a cancellation fee equal to \_\_\_\_ months rent.
  - 3) Tenant will provide Landlord with \_\_\_\_ months prior written notice of its intention to cancel.
  - 4) Tenant shall not cancel for the purpose of moving to another office building within \_\_\_\_\_ counties.
19. Renewal Option. Tenant shall have \_\_\_\_ option(s) to renew this lease for a period of \_\_\_\_ years at the then prevailing market rate. If Tenant elects to exercise its option to renew, it must do so in writing \_\_\_\_\_ (\_\_\_\_) months prior to Lease expiration. Market rate shall be determined as follows: \_\_\_\_\_
20. Right of First Refusal. Tenant shall have the Right of First Refusal to lease \_\_\_\_ rentable square feet of space located \_\_\_\_\_.
21. Expansion Option. Upon the \_\_\_\_ anniversary date of the Lease, Landlord will grant Tenant the right to expand into \_\_\_\_\_ rentable square feet. In order to exercise this expansion option, Tenant must provide Landlord with at least \_\_\_\_\_ (\_\_) months prior written notice. The expansion space will be offered at the then prevailing market rate for the Building. All other terms and conditions of the Lease shall remain the same.
22. Hours of Operation. The Building hours of operation are 7:00 AM to 6:00 PM Monday through Friday and 9:00 AM to 1:00 PM Saturdays, except holidays. After hours HVAC may be obtained with 24 hour notice at a charge of \$\_\_\_\_ per hour.
23. Assignment and Subletting. Tenant will have the right to assign the lease or sublease all or a portion of the Premises with Landlord's consent which shall not be unreasonably withheld or delayed (subject to certain restrictions).
24. Hazardous Material. To Landlord's knowledge, the Building does not contain asbestos or other hazardous materials.
25. Americans with Disabilities Act. Landlord has a plan to bring the Building's common areas into compliance with the Americans With Disabilities Act of 1990 (the "ADA"). A copy of this plan is available for Tenant's review in the Building's management office. From and after the Commencement Date, Landlord will be responsible for the ADA in the Building's common areas and Tenant will be responsible for the ADA in the Premises.
26. Subordination, Non-disturbance. Landlord will exercise good faith efforts to obtain a Subordination, Non-disturbance and Attornment agreement from Landlord's lender (on its standard form) with the goal of such discussions being to deliver it with the Lease, or if not then available, prior to the Commencement Date.

27. Amenities. \_\_\_\_\_
28. Signage. \_\_\_\_\_
29. Communications Antenna. Tenant will have the right to install a satellite dish or other communications equipment on a balcony of the Building provided the installation thereof is harmonious with the appearance of the Building and does not interfere with other tenants or then existing equipment. The cost of installation, maintenance and insurance for such equipment will be borne by Tenant and Landlord will have the right to approve all aspects of this equipment installation and operation.
30. Review. This proposal is subject to (i) a financial review of Tenant by the Landlord and (ii) review and approval by Landlord's lender.

EXCEPT AS PROVIDED BELOW, THIS IS A NON-BINDING LETTER OF INTENT SUBMITTED TO OUTLINE THE MATERIAL BUSINESS TERMS FOR PROPOSED LEASE BY TENANT. NEITHER PARTY SHALL BE BOUND TO THE TRANSACTION UNTIL A FINAL LEASE, ACCEPTABLE TO ALL PARTIES HAS BEEN EXECUTED TOGETHER WITH THE SECURITY DEPOSIT AND FIRST MONTH'S RENT. SUBJECT TO THE BINDING AGREEMENTS BELOW, EITHER PARTY MAY TERMINATE NEGOTIATIONS AT ANY TIME.

**Binding Agreements of the Parties:**

The following agreements of Landlord and Tenant are legally binding with regard to the specified matters:

1. Exclusive Dealings. During the \_\_\_\_\_ day period following the execution of this Letter of Intent, Landlord will not enter into any negotiations with other parties regarding the lease of the Premises.
2. Good Faith Negotiations. The parties agree to exercise good faith in negotiating toward a legally binding Lease. The parties agree that the Lease shall contain the material provisions set forth in this Letter of Intent. If despite good faith negotiations, the parties have not executed a legally binding Lease within \_\_\_\_\_ days following the execution of this Letter of Intent, either party may terminate negotiations.
3. Confidentiality. The parties shall keep this Letter of Intent, their negotiations and any information regarding the Premises confidential, except as necessary to comply with applicable laws and regulations and for consultation with professionals retained by the parties relating to the real estate transaction. In the event a legally binding Lease is not executed, Tenant agrees to return all copies of information regarding the Premises to Landlord together with copies of all third party reports obtained by Tenant. Tenant agrees that any third party reports obtained by Tenant shall be addressed to both Tenant and Landlord.
4. Inspection of Premises. Landlord grants to Tenant the right to conduct inspections of the Premises including structural and environmental studies. Tenant shall not unreasonably interfere with the operations of the Premises and shall obtain advance approval from Landlord to any inspections, which approval shall not unreasonably withheld or delayed. Tenant indemnifies and holds Landlord harmless from all liability relating to Tenant's inspections and studies.
5. Preparation of Documentation. Landlord agrees to cause its legal counsel to prepare a draft Lease for delivery to Tenant and its legal counsel within \_\_\_\_\_ days from the date this Letter of Intent is executed. The form of Lease shall be [ALTERNATIVES: the most current form promulgated by the Texas Association of Realtors for Commercial Property/ State Bar of Texas form/ Landlord's standard form/ revised for this transaction].

BY YOUR SIGNATURE, YOU REPRESENT THAT YOU ARE AUTHORIZED TO SIGN ON BEHALF OF LANDLORD. LANDLORD ACKNOWLEDGES TENANT IS RELYING UPON THE ENFORCEABILITY OF THE FOREGOING AGREEMENTS IN PROCEEDING WITH THIS TRANSACTION. LANDLORD ACKNOWLEDGES RECEIPT OF \$10.00 AND OTHER VALUABLE CONSIDERATION FROM TENANT.

If the foregoing terms are acceptable to you, please so indicate by your signature below and the return of the executed Letter of Intent to my attention.

Very truly yours,

[Landlord's Representative]

AGREED THIS \_\_\_\_\_ DAY OF \_\_\_\_\_, 20\_\_.

\_\_\_\_\_  
[Tenant's Representative]

cc: [Tenant]

[Landlord]

**APPENDIX “C”**  
**Lease Letter of Intent Checklist**

**I. THE PARTIES & LEASE**

1. Tenant’s information
  - a. Name
  - b. Address
  - c. Type of entity and place of formation
  - d. Tax identification number
  - f. Contact person
2. Owner’s Information
  - a. Name
  - b. Address
  - c. Building/Center ownership information
  - d. Contact person
  - e. Building management information (e.g., name, address)
  - f. Lease form to be used (e.g., owner’s/tenant’s standard form)

**II. THE SPACE**

1. Description of space (e.g., location, size, suite #, floor)
2. Space planning information (e.g., floor loads, floor duct locations)
3. Base building plans
4. Owner’s construction obligations for space/common area
5. Tenant improvements
  - a. Owner’s/Tenant’s obligation
  - b. Tenant improvement allowance (e.g., amount, when paid, conditions for payment [e.g., no default, assignment])
6. Electricity requirements (e.g., wattage per square foot)
7. Casualty damages: owner/tenant rights and responsibilities regarding partial/total destruction of space
8. Condemnation
9. Restoration of space at lease end (e.g., removal of alterations)

**III. LEASE TERM**

1. Term of lease (number of years)
2. Lease commencement
  - a. Date
  - b. Conditions to commencement (e.g., co-tenancy, owner’s buildout, tenant’s buildout)
  - c. Ramifications of delay (e.g., penalties, termination, self-help)
3. Early occupancy
4. Delayed possession

**IV. RENT & EXPENSES**

1. Rent commencement
2. Date
3. Conditions triggering commencement (e.g., delivery of space, co-tenancy)
4. Base rent and escalation method (e.g., CPI or rent bumps)
5. Percentage rent
6. Definition of gross sales/receipts (inclusions/exclusions)
7. Breakpoint (natural or artificial)
8. Operating expenses/CAM costs
9. Inclusions/Exclusions

10. Base year
  11. Pro rata share
  12. Cap
  13. Gross up
  14. Adjustments
  15. Merchants association/promotional fund (e.g., contribution amount, withdrawal right)
  16. Electricity charge
  17. Real estate tax
  18. Base year or base amount
  19. Pro rata share
  20. Right to contest
  21. Security deposit (e.g., amount, treatment of interest, application form [such as letter of credit], reductions)
  22. Rent abatement (e.g., conditions, duration, amount)
  23. Rent acceleration right
  24. Rent concessions
  25. Guaranty (e.g., limits, "good guy")
- V. USE & OPERATION**
1. Tenant's use of space
  2. Operating restrictions/requirements
  3. Duration/Hours of operation
  4. Continuous operations
  5. Trade name requirements
  6. Radius restriction
  7. Restrictions on owner
  8. Exclusive
  9. Cotenancy
  10. Covenant to open
  11. Conduct of business
  12. Tenant's right to finance equipment/improvements
- VI. BUILDING & SERVICES**
1. Parking (e.g., assigned spaces, charge, restrictions on owner, parking ratio)
  2. Building amenities (e.g., garage, cafeteria, newsstand, day care, high-tech communications capabilities)
  3. Signage (e.g., location, restrictions)
  4. Building directory
  5. Roof antenna rights (and riser availability)
  6. Building access (e.g., 24 hrs, 7 days)
  7. Size, design, and layout of building/center (e.g., plot plan, floor plan, gross leasable area, signage and location)
  8. Building services furnished by owner (e.g., HVAC, plumbing, electricity, passenger elevators, freight elevators)
  9. Business hours of building/center
  10. Hours of basic service (e.g., HVAC, elevator)
  11. After-hours service costs
  12. Supplemental A/C and other services (e.g., availability, cost)
  13. Temperature range for HVAC
  14. Quality of building/center and services (e.g., 1st class)
  15. Interruption of services (who bears responsibility)
  16. Legal documentation needed regarding leasing or ownership of property (e.g., ground lease, REA)
- VII. ASSIGNMENT & SUBLETTING**
1. Consent conditions
  2. Exceptions

3. Stock transfer or similar transfer
  4. Recapture rights
  5. Profit sharing
  6. Change of use restrictions
  7. Assignee's/Subtenant's loss of rent concessions
- VIII. OPTIONS & RIGHTS**
1. Expansion
  2. Renewal/Extension
  3. Purchase
  4. Termination (owner and/or tenant)
  5. Conditions (e.g., gross sales, co-tenancy)
  6. Right of first refusal/offer)
  7. Right to go dark (e.g., owner's recapture right)
  8. Relocation right
  9. Self-help right (tenant and/or owner)
- IX. REPRESENTATIONS/OBLIGATIONS**
1. Compliance with law
  2. Latent defects
  3. ADA compliance
  4. Certificate of occupancy (temporary and permanent)
  5. Subordination, nondisturbance, and attornment agreement (SNDA) from lender, ground lessor, and/or owner (for subtenant)
  6. Insurance (owner and tenant obligations)
  7. Asbestos/Toxic materials representation (e.g., it is/isn't present, owner will/will not remove it)
  8. Hazardous materials
  9. General liability obligations for owner/tenant (e.g., for space, common area)
  10. Constructive eviction (conditions for)
  11. Zoning restrictions
- X. MISCELLANEOUS**
1. Arbitration or other alternative dispute resolution
  2. Verification of square footage
  3. Brokers (e.g., identity, who pays)
  4. Audit rights
  5. Tenant's right to audit CAM/operating expenses
  6. Owner's right to audit gross sales
  7. Binding/Nonbinding
  8. Binding provisions in an otherwise nonbinding letter of intent

*This checklist is based on a checklist in the September 1999 edition of the Commercial Lease Law Insider.*

**APPENDIX “D”**  
**Biography of Research Material**

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4. Devlin, Christopher J. “How Binding Are Letters of Intent?” *Maine Bar Journal*, Sept. 1995.
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6. Greenwald, Dennis L. and Asimow, Michael. *California Practice Guide: Real Property Transactions*, Chapter Four, 1997. (Forms Attached).
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9. Jolley, Rhonda G. and Thompson, Chris. “What Do You Really Mean? Drafting Letters of Intent.” *State Bar of Texas Advanced Real Estate Drafting Course*, 2008, available at [www.reptl.org](http://www.reptl.org).
10. Middleton, Linda. “Contemplated Written Agreements - Contract or Memorial.” *Baylor Law Review*, 1974, Pg. 132.
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