

TERM SHEETS, HEADS OF AGREEMENT, DEAL MEMOS, LETTERS OF INTENT, MOU's – ARE THEY WORTH THE PAPER THEY'RE WRITTEN ON?

By Leanne Montibeler, Solicitor

First appeared in TalentPay Compliance Review, December 2012

Scenario

You are in the process of negotiating with a celebrity to appear in an advertising campaign. The negotiations have been ongoing for months and you are (finally) getting somewhere. You have agreed on some of the important details, such as the talent fee and the media. But there are some issues you are still working through. You wonder if there's a way to lock down the points that have been agreed so far. You approach your lawyer and ask the question – 'Is there such a thing as a preliminary agreement?'

The short answer is 'yes'. These agreements are generally known as a 'Memorandum of Understanding', 'Letter of Intent', or 'Heads of Agreement'. Some advertising agencies might recognise this as a 'Term Sheet' and this article will use the phrase 'Term Sheet' to refer to these types of documents generally. Essentially, a Term Sheet documents what has been agreed from negotiations, generally with a view to formalising a final, more comprehensive agreement at a later stage.

However, there are some 'urban myths' about Term Sheets, particularly around whether or not they are legally binding. Although this will always depend on the unique circumstances of each case, set out below is some general guidance to consider.

Are Term Sheets legally binding?

An agreement requires certain essential elements to ensure it is legally binding and enforceable. Relevantly, amongst other things, there must be:

- 1) Consideration (i.e. price or payment, "something for something");
- 2) Intention to create a binding agreement (this can be presumed or the agreement can expressly say the parties intend to be bound); and
- 3) Certainty of language and completeness of terms (i.e. the Term Sheet must be sufficiently clear and certain to actually be binding in practice)

In many cases 1) and 2) above can be easily satisfied. Where a Term Sheet often comes unstuck is in relation to 3).

As a Term Sheet is drafted and signed at a preliminary stage, it is common for it to include vague phrases such as "to be agreed", "on the usual terms", "when necessary", "when practical", "at a fair price" or "subject to contract" because the parties haven't fully contemplated all the details yet.

Such language is however problematic from a legal perspective, as it could signal that the agreement is incomplete or is too vague to be enforceable. If on an objective read of the Term Sheet it is not clear what the parties' obligations actually are, then there is unlikely to be a valid or binding agreement.

This is also the case where the Term Sheet leaves out key, essential terms (for example, the fee), to be decided at a later date. If this occurs, then not only is the agreement uncertain and incomplete, it could also signal a lack of intention of the parties to be bound. The Courts have

in the past been unlikely to conclude that parties intended to be bound by agreements if there are numerous and significant areas which the parties have failed to reach agreement.

The result is that although you have a written agreement, you might not be able to rely on it if a dispute arises, such as if the other party refuses to follow its terms or wants to re-consider it. Sometimes, this may suit you commercially as it means you also have an “out” if circumstances change. But what if you want to make it binding?

Unfortunately, without completeness and certainty of language, you could run into problems. If you use a Term Sheet, be aware that great care needs to be taken to fully and properly record the parties’ intentions if you want to rely on the agreement and have the parties bound by it. If in doubt, obtain advice to draft the Term Sheet clearly and precisely.

If some elements of the deal are uncertain, it might be appropriate to have a mechanism in the Term Sheet to deal with such elements if the parties are unable to agree – such as a binding dispute resolution clause (which sets out the process you will follow if there is a dispute), or a clause which makes it an obligation for the parties to negotiate in good faith.

Generally speaking, the obligation of good faith requires the parties to cooperate in a reasonable way to achieve the contract objectives. This doesn’t mean that the parties need to compromise their own commercial interests but overall they should negotiate honestly and sincerely and give genuine consideration to proposals that are made and received, rather than engage in improper or unfair tactics. Offers and counter-offers should also respect the material terms already agreed in the Term Sheet.

Despite the legal uncertainty that can arise, there are still practical and commercial benefits for having a Term Sheet. For example, it is a good way to ‘get down on paper’ what has been agreed so far and can help set parameters within which to base further negotiations. It also can give comfort to the parties as there is an impression that the parties are committed to concluding the negotiations. It can assist the later drafting process of a formal agreement as the major terms are neatly contained in one document (rather than a series of email chains).

If you are concerned about ensuring your agreement is binding, then it is preferable to finalise all terms into a full and final agreement as soon as possible – so keep those negotiations flowing!

Contact us

If you would like further information about term sheets, and how this may affect you or your clients, please contact any of our experts below. We can provide tailored legal and practical advice to assist you.

Leanne Montibeler
+61 2 8935 8805
leanne.montibeler@anisimoff.com.au

Heidi Bruce
+61 2 8935 8806
heidi.bruce@anisimoff.com.au