

**LETTERS OF INTENT
ARE THEY WORTH THE TIME AND EFFORT?**

The more time taken to develop a letter of intent (LOI), the less time it takes to complete the final documents. The goal is to summarize the business deal without imposing obligations on the parties, unless specifically intended.

Always assume the other side will interpret an ambiguous phrase in their favor. So draft for clarity, even if it means a longer LOI.

The process is also an opportunity for the parties determine if they can work out contentious issues effectively. Discuss the tough issues early, before the lawyers raise them and potentially kill the deal.

Outline of a well drafted letter of intent for a leasing or sales transaction:

Parties:

Correctly identify the parties. If the parties are corporations, LLCs or other entities, verify their names and determined it they are qualified to do business in the state where the property is located. In California you would use California Business Search at <http://kepler.ss.ca.gov/list.html>.

Property:

While a legal description is not necessary in an LOI, the LOI should describe the property in sufficient detail so that a stranger off the street could identify the property. It could include street address, square footages, floor levels, parking areas, improvements, even personal property which is part of the deal.

Economic terms:

For a lease

- Commencement date and delivery date
- Term
- Security deposit, amount, form, burn-down
- Guaranties
- Pass-through and direct expenses paid by tenant (e.g; triple net, full service)
- Rent, including abatement, escalations and adjustments
- Build out obligations, including allowances

- Landlord's other delivery obligations (systems in good working order, water tight structure, cold or warm shell, compliance with laws, free of hazardous materials, ADA compliant)
- Specific use provisions if the use involves hazardous materials or is otherwise atypical

Retail specific provisions

- Location
- Percentage Rent
- Anchor tenant open and doing business
- Timing of delivery of space
- Exclusivity and radius clauses
- Infrastructure and parking requirements.

For an acquisition/sale

- Purchase price and adjustments
- Deposits and timing
- Due diligence periods and closing deadlines including extension rights
- Conditions to closing such as due diligence reviews and inspections, land use entitlements, financing, completion of construction, leasing commitments
- Reference any critical seller's representations and warranties and how long they will survive
- AS IS statements

Conditions to Commitment:

Spell out in short-hand form the conditions to signing the formal documents. These may include:

- finalizing the formal documentation
- lender or board approvals
- due diligence reviews
- financing
- construction cost estimates
- environmental clearances
- land use entitlements

Assignment:

State whether the formal agreement may be assigned to affiliates and successors with consent of the other party. In a lease, indicate whether there will be recapture and rent sharing provisions.

Lease Options:

Spell out extension, expansion, purchase and termination options, as well as rights of first offer. State that any fair market rent determination shall be made by arbitration. Specify whether there is a minimum or maximum fair market rent.

Lease build out obligations:

This is the area where many letters of intent and even final leases fall short. Clearly state which party is engaging the architect and contractor, specify what any allowance may be applied to, state any construction fee to be charged by the landlord. Specify if the tenant must improve all of the premises or if it may build out the space in phases. If the tenant has chosen its architect and/or contractor, get them approved in the LOI. Will the tenant's build out obligations be secured by a bond or letter of credit? Consider defining substantial completion. Define what improvements must be removed at the end of the term, such as showers and internal stairwells.

If the tenant is a public company and the lease may be defined as a build to suit lease, have the tenant engage its accountants early in the process so the lease can be structured to reduce certain accounting classification risks.

Specify binding obligations:

Specify any obligations which are binding upon signing of the LOI. These typically include confidentiality provisions and a no-shop or exclusivity period.

Non-Binding Language:

State and restate and then state again that the parties do not intend the LOI or any actions by the parties in furtherance of the purposes of the LOI to create a binding obligation on behalf of either party (other than the specified ones such as confidentiality). Provide that neither party has any obligation to continue to negotiate or work towards a binding obligation and that either party may withdraw from the negotiation at any time for any reason. Put non-binding language in the opening and closing paragraphs and in **ALL CAPS AND IN BOLD** above the parties' signatures.

Reserved Rights:

Even though an LOI may be non-binding, there have been cases where the courts have held that parties to a LOI have a duty to act in good faith to negotiate a binding commitment. So, if you plan to continue to shop around or shop the property after the LOI is signed, then say that clearly in the LOI.

Traps for the unwary:

From time to time, a client asks me to prepare a LOI which is silent or ambiguous as to whether it is binding or not, typically because the client wants the other party to be bound contractually without realizing it. I recommend against such practice. After all, a LOI memorializes the "intent" of both parties, and if one party does not intend to be contractually bound, tricking them into it simply invites litigation.

And my goal is to keep clients focused on their business and out of court.

The article above was prepared by Helen Sedwick of Bennett Valley Law.

After more than 20 years of practicing law with major firms in San Francisco, Helen Sedwick founded her own firm, Bennett Valley Law, in 2007. She continues to specialize in commercial real estate transactions, primarily sales and acquisitions, leasing, entity formation, financing and management. Clients include developers, investors, start up companies, bio-tech companies, solar technology companies, wineries, restaurant franchisees and owners, and individuals. For more information, please visit www.bennettvalleylaw.com.

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