

THE ARIZONA INVESTOR

- A LEGAL NEWSLETTER FOR ARIZONA'S REAL ESTATE INVESTORS -

NOVEMBER/DECEMBER 2012

The "Letter of Intent" – Might It Constitute a Contract?

By Marc Maher, Esq.



A "letter of intent," ("LOI") sometimes referred to as a "status letter" or "agreement to agree" is a tool often used by brokers and attorneys to aid their respective clients at the onset of a potential purchase and sale transaction. The LOI serves two purposes: (1) it is a cost effective way for the parties to get a feel for each other's position in a non-binding fashion, and (2) it memorializes material deal points between a seller and buyer without the added time and expense associated with crafting full blown contracts with supplemental exhibits. Such material deal points may include the identity of the parties, a property's identity, the desired sales price, and the time and conditions of payment, to name just a few items.

It is common for the terms of an LOI to be negotiated back and forth. For example, a buyer's attorney may draft an original LOI containing the following points: (1) \$2.5M purchase price; (2) close of escrow of January 15, 2013; (3) closing conditioned on the seller increasing the occupancy rate to 90%; and (4) closing conditioned on the seller resigning 12-month leases with those tenants whose leases are set to mature within the current quarter. The seller's attorney may fire back an amended LOI redlining (that is, amending) deal points "(3)" and "(4)" contained in the original LOI. This volley often goes back and forth a few times until either the parties cannot arrive at a meeting of the minds on the basic deal points (and each party correspondingly goes their own way), or the parties finalize an LOI that each are willing to sign.

So, What Is The Problem?

Contrary to the wishes of at least one of the parties, an LOI may be deemed binding, and treated as an enforceable contract. This may be problematic because one party may reasonably believe that a contract has been reached (by virtue of the major deal points being hammered out in the signed LOI), and the other party (against whom the LOI is being enforced) may reasonably believe that negotiations, in the post-signing period, have failed.

But, The Document Is Titled "Letter of Intent." Doesn't That Make It Non-Binding?

The Arizona Supreme Court held that the nature of an instrument is determined by the effect the law gives to its terms, and not by the term that parties have designated the instrument. *Whalley v. George*, 52 Ariz. 27, 80 P.2d 449 (Ariz. 1938). In other words, just because a document is labeled as a "letter of intent" does not mean that it will be treated as such.



(P) 623.434.7100

(F) 623.434.7101

www.RosserLawGroup.com

*"Protecting your interests without
compromising your transaction"*

When Might A “Letter of Intent” be Treated As An Enforceable Contract?

An LOI might be treated as an enforceable contract when the following occurs: (1) the statute of frauds is satisfied; (2) the elements of a contract are met, and (3) there is no provision in the LOI memorializing that the LOI is non-binding.

- Statute of Frauds: In Arizona, a contract for the sale of real estate is not actionable (*i.e.* enforceable by court action) unless it satisfies the statute of frauds. The statute of frauds requires that the agreement, or some memorandum thereof, be in writing, and signed by the party to be charged. A.R.S. § 44-101(6). More specifically, the writing must contain the following elements: (1) identification of the parties, (2) description of subject matter of contract, (3) purchase price, and (4) time and conditions of payment to constitute a sufficient memorandum of the agreement. *T.D. Dennis Builder, Inc. v. Goff*, 101 Ariz. 211, 213, 418 P.2d 367, 369 (Ariz. 1966). LOI’s are, by definition, in writing, and often contain the elements specified above. Thus, they often meet the requirements of the statute of frauds.
- Elements of a Contract: For a valid contract to exist there must be mutual assent (*i.e.* offer acceptance) and consideration. Often, LOI’s contain enough detailed information for each of these elements to be ascertained. Therefore, and per *Whalley*, referenced above, if it walks like a contract, and it talks like a contract, it’s a contract regardless of whether it is titled as an LOI.
- Memorializing the Non-Binding Nature of the LOI: If the LOI does not clearly state that it is deemed non-binding by the parties, then, if the other elements referenced above are met, the possibility exists that the LOI will be deemed an enforceable contract.

Whether you are acquiring or disposing of investment grade real estate, it is important that any letters of intent that are used are properly crafted to identify the major deal points, but also tempered with the appropriate provisions that make it clear to all that the respective letters are non-binding. As transactional real estate attorneys, we can help you draft and/or review such letters so that your interests are adequately protected. Please do not hesitate to contact us if you would like to schedule a consultation to discuss how we may be of service.

This article is of a general nature and reflects current statutory and case law as of the date of first publication. Further, this article reflects only the opinion of the author, and is not intended as definitive legal advice; you should not act upon it without seeking independent legal counsel.

Marc Maher is a transactional real estate attorney and counselor whose practice focuses on helping single-family and multi-residential real estate investors and real estate brokers. He can be reached at (623) 434-7100 or MMaher@RosserLawGroup.com. © 2012 Rosser Law Group



1523 W. Whispering Wind Drive
Suite 250
Phoenix, Arizona 85085

To: