

DELAWARE SUPREME COURT PROVIDES GUIDANCE TO DEALMAKERS ABOUT ‘NEGOTIATION IN GOOD FAITH’ PROVISIONS IN LETTERS OF INTENT, TERM SHEETS AND OTHER PRELIMINARY AGREEMENTS

The Delaware Supreme Court provided important guidance to dealmakers about “negotiate in good faith” provisions in letters of intent, term sheets and other preliminary agreements in its recent *SIGA Technologies v. PharmAthene, Inc.* decision.¹

Parties sometimes include “negotiate in good faith” provisions in preliminary agreements to advance the negotiation process by “nailing down” the fundamental deal terms and deferring until later, when the definitive agreement is negotiated, negotiation of the remainder of the deal terms. Including a “negotiate in good faith” provision in a preliminary agreement counters the general rule that preliminary agreements are not legally binding on the parties.

The *SIGA Technologies* decision, which is consistent with prior court decisions,² held that including a “negotiate in good faith” provision in a preliminary agreement has the following effects:

- The parties are required to engage in “good faith negotiation” of the definitive agreement - a party cannot “renounce the deal” or “abandon the negotiation”. This is a somewhat subjective “facts and circumstances” test, but a party will be required to show that it, for example, spent time participating in negotiation sessions, made counterproposals to deal terms proposed by the other party that were responsive to the other side’s proposals, and otherwise intended to come to agreement with the other party on deal terms.
- “Good faith negotiation” does not mean that a party is required concede the other side’s positions on proposed deal terms, as parties can legitimately have differences of opinion on deal terms and fail to come to agreement on them, while still proceeding in good faith.
- However, a party is prohibited from proposing deal terms that deviate from those specified in the preliminary agreement when negotiating the definitive agreement, as those specified deal terms are considered to have been “settled” and not subject to further negotiation.

In summary, including a “negotiation in good faith” provision in a letter of intent, term sheet or other preliminary agreement obligates the parties to reasonably negotiate the definitive agreement, which will consist of the deal terms specified in the preliminary document (which cannot be deviated from without mutual agreement of the parties), along with other deal terms agreed upon by the parties in the course of negotiation of the definitive agreement.

¹ 2013 WL 2303303 (Del. Supr., May 24, 2013).

² See, e.g., *Shann v. Dunk*, 870 F. Supp 460, 467-468 (N.D.N.Y.1994); *L3 Communications Corp. v. OSI Systems, Inc.*, 2005 WL 712232, *5 (S.D.N.Y. 2005).

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