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The Letter of Intent in International Syndicated Financing: An Analysis of the English and American Law from a Sovereign Borrowers’ Perspective

Alfredo G. Romero*

This article attempts to examine the legal nature of the letter of intent in syndicated credits and the possible legal actions to be taken against the failure of the lender or arranger to finalize the financing. The article will focus on sovereign borrowers’ syndicated loans. Inasmuch as State agencies accept the terms and conditions of a credit, they must go through a bidding process to select the best tender and also request legal approvals from different State entities. In this respect, the letter of intent will represent the arranging and financing proposal from the arranger or lender subject to the bidding process and correspondent approvals. Therefore, when this instrument is formally delivered to a sovereign borrower, it ignites the process that results in important internal legal and practical consequences for such a particular borrower.

First, the article will provide an introduction to indicate the general objective of the essay. Second, the article will define the letter of intent and explain the role it plays in the course of a loan syndication. Third, the article will explain the particular cycle of approvals from different State entities required in sovereign lending in order to obtain a final authorization that enables the sovereign borrower to issue a mandate to the lender or arranger. This is important for our legal analysis of the letter of intent because this pre-contractual document exposes what will be authorized and thereby be the basis of the mandate. We will also understand that in sovereign borrowing a great responsibility exists for sovereign borrowers when contracting indebtedness inasmuch as they are dealing with State indebtedness. Fourth, the article will focus on the legal nature of the letter of intent in order to establish possible enforceability of this pre-contractual agreement. Finally, after studying American and English cases and literature in respect to the interpretation of the wording of the document as well as possible enforceable obligations, the article will try to identify some legal actions that sovereign borrowers could take against the lender or arranger’s failure to complete a syndicated transaction as offered in a letter of intent.

* Mr. Romero obtained a J.D. from the Catholic University in Caracas, Venezuela, and an M.A. from Georgetown University, Washington, D.C. Mr. Romero is admitted to practice law in Venezuela and works for ARM Consultants, SC.
I. Introduction.

Before a business or financial transaction is formally set up, preliminary negotiations should come about and some written or oral understanding will establish the frame for concluding an agreement between the parties. This preliminary instrument which "reflects preliminary agreements or understandings of one or more parties to a future contract" is what is regularly denominated as a letter of intent.

In general, bankers or businessmen do not pretend to give legal force to this "agreement to agree." However, in the case of syndicated finance, arrangers do require a unilateral commitment from the borrower to guarantee exclusivity to the arranger and to reimburse costs and expenses derived from the fund raising process. Understandably, the promisor of an activity, which depends on many variable circumstances, would not like to become involved a formal commitment before the offer is definitely secured. Thereby, precontractual agreements are intended to be some kind of "gentleman's agreement" without legal enforceability for the lender. Nevertheless, the promisor of an activity offered in a letter of intent should be aware that the intention of a non binding agreement is clearly expressed in the document. Many authors argue, that in principle, English and American law excludes lender liability with respect to letters of intent when those letters are drafted in such a way that contractual liability depends on the signature of a future contract. Despite this fact, there could be different interpretations of the wording and the English and the American courts could define a letter of intent as enforceable even when there are phrases that imply that it is not. On the other hand, circumstances may exist where a borrower could be able to claim damages when expressed duties such as "best endeavours" or implied obligations such as good faith have been breached. The legal effects of letters of intent may be more remarkable in the case of sovereign borrowers. Borrowing States, unlike corporate borrowers, have to go through a long and tedious process of bidding rounds and approvals by government dependencies, the Congress and/or the Central Bank before signing any commitment in connection with an external indebtedness.

If, after going through all the above-mentioned processes, an authorization to contract debt is finally met and the lender decides not to lend, the sovereign borrower has already lost time and money. Additionally, the sovereign borrower may not have enough time in accordance with the law to apply for a new authorization for a different lending proposal for the same purpose. The applicable Venezuelan laws explain this situation.

2. See id. at 5-6.
4. Id. at 726.
Besides the Annual Budget Act, which regulates State annual income and spending, an Indebtedness Act exists which is enacted every year. This Act authorizes the Executive Branch to contract debt in the correspondent year for a specific maximum amount. The Annual Indebtedness Act is enacted by order of the Public Credit Act. Either the Annual Indebtedness Act or the Public Credit Act establishes that before signing any commitment with respect to public debt, the Executive Branch has to request the opinion of the Central Bank and the Congress. The Annual Indebtedness Act lists the specific projects and the specific amount of indebtedness in relation to that project to be raised for that fiscal period. However, there is a two year period in which to materially formalize the indebtedness e.g. sign the credit agreement—because the process of required approvals could alone take a year or more. If the financing terms and conditions are modified, it is almost impossible to find a different financing proposal and obtain new authorization by going to the same process again.7

Having referred to the restrictions of the sovereign borrower when deciding to raise financing, the liability of the "arranger,"8 is important in respect of a financing offer when, because of failure to execute the offer, it causes damages to the sovereign borrower as a consequence of the borrower's reliance on the offer. Accordingly, we will focus on the legal nature of this financing offer or "credit memo"9 and the possible legal actions that the borrower - in our case a sovereign borrower - might take against the arranger or lender for failure to complete the offered financing. In English law, a letter of intent containing a term sheet or financing offer could be interpreted as a contract by the courts and consequently be subject to contractual liability. In order to avoid this, lawyers incorporate the phrase "subject to contract" into the letter of intent. By including these words a letter of intent becomes a document containing preliminary agreements that are not binding until a future contract is signed. In principle, the English courts have held that this phrase is enough for a letter of intent to be considered non-obligatory. In this respect, Ralph B. Lake argues that "parties to instruments governed by English law have an almost unqualified ability to remove any doubt as to intentions, by the use of the phrase 'subject to contract'."10 American law, on the other hand, has a different approach. For American courts, the objective intention of the parties is more important than the wording of the document. American courts determine what the parties have intended to agree in the letter by analyzing their expressed intention.11 In spite of the differences of both systems, in general terms, the applicable English law principle is similar to American law principle.

As observed earlier, in sovereign financing, a letter of intent, in order to be accepted by the borrower, needs several approvals from different governmental entities. To approve the terms and conditions of a financing proposal the responsible public official must be aware of

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10. Lake & Draetta, supra note 1, at 94.
11. Id. at 94-96.
the financial advantage and disadvantage that those terms and conditions may generate for the State. It is possible that before accepting a loan offer, the government employee might have excluded other offers through a bidding process. For example, in the case of Venezuela, the Ministry of Finance in combination with the end user of the funds normally has to refuse other letters of intent prior to presenting the term sheet before the Central Bank and the Congress for approval. In this respect, the public official in charge of the process, if not careful, might become personally negligent for signing prejudicial agreements on behalf of the State. Sovereign borrowers' public officials must be aware of the above situation, even more so in developing countries where usually a strong political opposition to external indebtedness exists. Major external debt transactions are cautiously observed by all governmental entities and especially by the political opposition in the Parliament.

In sovereign lending, the financial arranger of the transaction is normally a sophisticated company. The financial arranger should be aware of the government requirements involved in this kind of transaction. An experienced lender or arranger, who has participated in several sovereign international credits, is conscious of a sovereign borrower's responsibilities in an external indebtedness transaction. In this respect, some best endeavours and good faith standard is expected from the arranger or lender in order to raise the funds. As we will see below, American and English cases may legally support the above situation. For example, Hoffman v. Red Owl Stores, an American case, although referring to a different situation, supports the argument that reliance on a proposal is a determinant issue to oblige the lender in relation to a letter of intent. In reference to this case, Trevor A. Mills argues that "if one party made a promise that the other party reasonably relied on and, as a result, significantly altered its position, there is an enforceable promise if it is in the interest of equity to enforce the promise."

As mentioned earlier, the case law in the United States implies that the intention of the lender is more important than the sole meaning of the document's wording. In Itek Corp. v. Chicago Aerial Indus. Inc., it was held that in order to define the intention of the letter of intent, the court must analyze the circumstances that surrounded the negotiations. Although in less proportion, English courts will also consider the surrounding circumstances to define the legal nature of the letter of intent. In the case of sovereign lending, particular circumstances must be taken into account that might lead one to suppose that a firm obligation from the lender exists when he submits a letter of intent. This is even more evident when the lender or arranger wins a bid among other prospective lenders or arrangers to finance the sovereign borrower.

12. See Gurria-Trevino, supra note 6, at 390. See also Guillermo V. Soliven, Syndicated Bank Credits: A Developing Country's Perspective, in CURRENT ISSUES OF INTERNATIONAL FINANCIAL LAW 326 (David G. Pierce et al. eds., 1985).
Even though in principle letters of intent under American and English law are nonenforceable when they contain wording that conditions the agreement to a future contract, the lender has to be aware—more in American law than in English law—that the wording has to be specific enough in order to state the objective intention not to provide the letter of intent with contractual liability. In a current American case, Lazard Freres & Co. v. Protective Life Ins. Co., a New York federal court stated that in a case of purchase and sale of bank debt, commitment letters may be enforceable even though the commitment letter is subject to a future documentation. Referring to an Arkansas case, Sterling Faucet Co. v. First Municipal Leasing Corp., Michael L. Weissman states “that these cases demonstrate the need for careful drafting of letters and related materials which may induce a prospective borrower to believe that there is a commitment to lend when no commitment is intended.”

II. Definition and Purpose of the Letter of Intent.

The letter of intent in syndicated financing is the “first serious paperwork generated in the loan approval process ... prepared by the loan officer ... to commit the lender to a lending facility.” The concept letter of intent is thereby employed in this paper to define the document used in syndicated loans, which reflect preliminary understandings that will be further documented in a credit contract. However, in credit transactions, this document has different names, such as: mandate letter, commitment letter, term sheet, financing proposal, and credit offer. In general, whichever denomination is chosen, the instrument is the same. The letter of intent contains a summary of the financial and legal terms and conditions for credit. This financing proposal, when agreed upon, will be expressed and detailed in a loan agreement.

A letter of Intent may begin as follows (see Schedule I):

Ladies and Gentleman:

We are pleased to confirm our willingness to use our reasonable best efforts in accordance with our customary practice on your behalf to form a syndicate of lenders to make funds available to you under a revolving credit agreement containing the terms and conditions outlined below, among others. We would be prepared, as a member of the syndicate, to make a loan commitment of $50,000,000.

22. See Hillman, supra note 9, at 11.
In this example, the first paragraph of a letter of intent expresses a general intention, but it also sets forth a general idea of the financial and legal terms and conditions. By expressing the intention “to make funds... under a revolving credit agreement”, the paragraph proposes a general idea of the financial structure. Also, an important legal condition is established by indicating a willingness to provide financing on the basis of “reasonable best efforts”. Below, we will analyze the importance of this last phrase.

Schedule I shows a term sheet where both “terms and conditions” and the “purpose” of the credit are listed. Regularly, the term sheet of a syndicated loan would enumerate the following: (i) major issues related to the financial conditions of the credit, such as amount, name of the borrower(s), creditor(s) and agent(s), maturity, availability, interest, fees, and other expenses; (ii) major legal terms and conditions, such as a summary of covenants, tax payment conditions, governing law, jurisdiction, and currency option; and (iii) the purpose of the credit (e.g to finance working capital). As mentioned above, the specification of these terms and conditions will be further incorporated into the Loan Agreement. After the terms and conditions are presented, a request from the lender or arranger to the borrower is made in order for the borrower to express acceptance of such terms and conditions. In our Schedule I example, the last paragraph reads:

If these terms and conditions are acceptable to you, please so indicate by executing and returning to us the enclosed copy of this letter. The commitment set forth herein will expire on March 8, 1991, unless we have received your acceptance on or before that date.

Once this request is made, a representative of the borrower will sign the letter expressing his acceptance of the offer. From this moment, the arranger will be authorized to begin the syndication arrangement for raising the required funds. The letter of intent is then divided in two phases. First, in the offer letter phase, the offer is submitted by the financing arranger or lender for the borrower’s consideration of the terms and conditions of the loan. In this first phase, there is a unilateral intention from a party (the lender or arranger) to raise funds on behalf of another party (the borrower). This offer, the offer letter, is signed by the offeror (the lender or arranger) and contains a request to the borrower to confirm acceptance of the offer by signing one copy and sending it back to the lender. The borrower, by signing and returning the letter, is issuing a “mandate” to the lender or arranger to arrange financing according to the proposed conditions. Accordingly, the second phase, the mandate letter, comes into place as a response to the financing offer. The formal appearance of the letter of intent arises when signed by both parties.

Schedule II demonstrates another sample of a letter of intent addressed to a sovereign borrower. In this case, two different letters are present. One is the offer letter and the other

25. LAKE & DRAETTA supra note 1, at 134. See also TONY RHODES, SYNDICATED LENDING: PRACTICE AND DOCUMENTATION (2d ed. 1996); See also Soliven, supra note 12, at 338.
27. UNITAR, supra note 23, at 104-05.
28. LAKE & DRAETTA, supra note 1, at 134.
document - whose format is actually given as an attachment (Exhibit A) to the offer letter - is the mandate letter. The latter document begins as follows:

Reference is made to your letter to us dated July 22, 1994, (the "Letter") relating to your proposal to arrange financing in the amount of $38,511,373 for the Republic of Ruritania in connection with the Occidental Coastal Region Project in Ruritania. The Republic of Ruritania (the Borrower) hereby confirms its acceptance in all respects of such proposal.

Unlike the offer letter, which encloses the unilateral intention of the lender, the mandate letter contains a confirmation from the borrower with respect to those terms and conditions the offer has indicated. When this first document (the offer letter) is presented to the borrower, the prospective arranger or lender proposes to raise funds on behalf of the borrower. When the borrower answers the letter accepting the conditions, the arranger begins to structure the financing on behalf of the borrower. These two phases are important for the analysis of the letter of intent in sovereign lending because most of the time, the sovereign borrower requires a bidding process in order to decide which is the best offer with respect to its terms, conditions and bank qualifications. The document presented in the bidding round is the offer letter with its enclosed terms and conditions.

For a better analysis of the letter of intent process, we must understand the syndication process as a whole. The syndication process can be divided into two phases: (1) the mandate phase; and (2) the loan agreement phase. From a sovereign borrower's perspective, these two phases may further be divided. The mandate phase consists of the following steps: (i) the borrower issues an invitation to different banks to bid for the arranger's role; (ii) interested banks present an offer document; (iii) the borrower organizes a bidding round; (iv) the sovereign borrower chooses a bank as arranger; and (v) the borrower submits a mandate letter to the designated arranger. The loan agreement phase will be divided into (i) negotiation and (ii) signature.

With respect to the mandate phase - which is the focus of our analysis - Figure 1 below shows the five steps this preliminary process involves. First, the borrower sends an invitation to all banks - or some specific banks - to participate in a bidding round with the purpose of arranging financing for a government project or program. Second, interested banks present their proposals or offer letters. Each offer letter contains particular terms and conditions that, besides the bank's qualifications, would be the basis upon which the sovereign borrower determines which is the best proposal. Third, the sovereign borrower

29. See Davies & Halliday, supra note 8, at 182.
32. For further details about the mandate process, see Hurn, supra note 24, at 23-26.
33. See generally UNITAR, supra note 23, at 104-09.
organizes a bidding round. Fourth, an arranger is designated in accordance with the terms of its offer. Finally, the borrower delivers a mandate to the arranger to begin the process of syndication and raise the expected funds. From that moment, the arranger begins to contact other lenders and prepares the loan documentation which will be negotiated further with the borrower and finally signed.  

Figure 1

34. For more information about the legal aspects of the syndication process from a sovereign borrower's perspective, see Soliven, supra note 12, at 336-43. See also Papanicolau, supra note 6, at 48-50. See UNITAR, supra note 23, at 104-09. For a case study of the borrowing process in Sweden, see Lars Andren & Bengt Karde, The Raising of a Syndicated Euroloan Facility: A Case Study of Legal Aspects in SOVEREIGN BORROWERS 247-57(Lars Kalderen & Qamar S. Siddiqi eds., 1984).
III. Internal Legal Process of Approval of Indebtedness by Sovereign Borrowers: Essential Role of the Letter of Intent in this Process. (Venezuelan and Mexican Law)

After presenting a general picture of the mandate process and before analyzing the legal nature of the letter of intent, we will look at the specific legal process of some developing countries for the approval of State indebtedness. The government, when it contracts debt, does so on behalf of the State. The debt one government administration contracts today will probably be paid by the next administration or administrations and are eventually paid for by all citizens of the country. Therefore, some laws limit the government from acquiring finance by requiring authorization from different entities, such as the Parliament, and by establishing ceilings on the amount of indebtedness contracted and executed in the annual budget. In some countries, the Constitution establishes the conditions and restrictions to obtaining government financing and in other countries, specific indebtedness acts control government financing.

In the case of Mexico, the Federal Public Debt Act establishes the legal framework for obtaining sovereign financing. In most cases, the law requires that a "foreign borrowing controlling agency" (FBCA) authorize and control any public indebtedness. For instance, any Mexican federal public entity, before officially or informally negotiating any international finance, must obtain the authorization of an FBCA, which in that specific case is the Public Credit Secretary (Secretaria de Hacienda y Credito Publico). The Public Credit Secretary will control the correct utilization of the funds provided by public indebtedness. On the other hand, before any annual fiscal period commences, the federal government must present an Income Act to the Parliament that reflects the expected national income of the specific year. Accordingly, this Act must express the amount of "net indebtedness" needed - either external or internal - to finance the national budget of that year.

In the case of Venezuela, indebtedness is much more restricted than in Mexico. The constitution provides a general regulation for public indebtedness and, as in Mexico, the Public Credit Act requires the authorization of an FBCA (the Ministry of Finance) and establishes that the government must request Parliamentary approval of the net indebtedness needed for the year. However, an Indebtedness Act also obliges the government to

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35. In this respect, for some borrowing countries' representatives, points of view, see Papanicolaou, supra note 6, at 47-52; Soliven, supra note 12, at 326-49; Gurria-Trevino, supra note 6, at 389-95 (Mexico).
37. See Gurria-Trevino, supra note 6, at 389.
39. See id. art. 7.
40. Id. art. 10.
41. See generally James Otis-Rodner, La Inversion Internacional en Paises en Desarrollo, 403-04 (1993); see also Brewer-Carias, supra note 36 at 75-96.
42. See Venez. Const. tit. VII, ch. 1, art. 231.
request authorization from the Central Bank, the Congress, and the Council of Ministers for each specific credit to be obtained on behalf of the State.\textsuperscript{43} The Venezuelan Indebtedness Act is an annual act subordinated to the Public Credit Act, which lists all projects and programs with the amounts to be financed by public debt. The Public Credit Act, on the other hand, establishes the legal process of authorizations, which must be obtained by the Ministry of Finance, before contracting any internal or external debt.\textsuperscript{44} Figure 2 below shows that in the case of Venezuela, a tedious bureaucratic procedure is required before the mandate letter is given. First, the Ministry of Finance (or the end user of the funds in combination with the Ministry of Finance) invites banks to bid for leading the arrangement of the loan. Second, banks submit their offer letters. Third, the best tender is selected after a bidding round after which the Ministry of Finance requests the approval of the offer letter from the Central Bank (4), the Congress (5), and the Council of Ministers (6). Finally, after the Council of Ministers (led by the President of the Republic) approves, the President of the Republic authorizes the Minister of Finance and other officials involved to deliver the mandate.

\begin{figure}[h]
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\includegraphics[width=\textwidth]{figure2}
\caption{Approval of financial terms and conditions and selection of arranger or lender (Case of Venezuela)}
\end{figure}

\begin{footnotesize}
\begin{itemize}
\item 43. See BREWER-CARIAS, supra note 36, at 78,85,87,91.
\end{itemize}
\end{footnotesize}
It is important to notice that in the case of Venezuela, there is a maximum period of two years from the date the Indebtedness Act becomes legally valid in which to sign the loan agreement. If, after this time, the loan agreement is not signed, the authorization is lost and a new authorization has to be obtained in the next Annual Indebtedness Act. The whole process has to start from the beginning. From my working experience at the Ministry of Finance, I can say that the authorization process in Venezuela could take a year or more before the loan agreement can be signed. Suppose that the whole process is completed and the mandate letter is given. The designated arranger says that he has used his best and reasonable efforts and it has not been possible to raise the funds. The normal action that a typical borrower will take is to request another bank to arrange financing for him. Nevertheless, in the case of a sovereign borrower such as Venezuela, when the designated arranger decides to abandon the transaction, there may not be enough time to go through the whole process from the beginning. Moreover, the indebtedness authorization will be lost with the possibility of higher financial costs for the project or program.

At this moment, the sovereign borrower would look at the letter of intent. It would find, at first glance, that no contractual obligation exists in connection with the letter of intent because there is a "subject to contract" provision which conditions the enforceability of the agreement until a formal contract is signed. When the borrower looks for a firm commitment in order to claim specific performance and/or damages, it discovers that the lender or arranger is only promising a credit on the basis of "best endeavours" or "best efforts". Does it mean that there is no cause of action for the borrower? In order to analyze this situation, we will focus on the legal nature of the letter of intent and consider several issues in connection with the wording of this document.

IV. Legal Nature

In English and American law, freedom of agreement prevails. Prima facie letters of intent in syndicated finance are, for the courts of these countries, not contracts if parties clearly express their intention of not having a binding agreement. In this respect, letters of intent represent, on one hand, a mere proposal from the lender or arranger to arrange financing and, on the other hand, a preliminary acceptance from the borrower of certain legal and financial terms and conditions in order for the arranger to raise the expected funds in the financial market. In general terms, letters of intent constitute a "mere negotiation in contemplation of a contract coming into existence at some future date." However, as will be explained below, in syndicated loans, letters of intent are intended to be binding at least in relation to two issues. First, they contain a commitment from the borrower to pay costs and expenses to the lender or arranger in regard to the arrangement of the credit. Second, they include a best endeavours obligation by the lender or arranger to collect money required by the borrower.

From a legal perspective, letters of intent are ambiguous and obscure documents. They lie in an "unclear gray zone". Many times lawyers do not even participate in drafting these

46. LAKE & DRAETTA, note 1 at 10-11.
documents. Bankers believe that lawyers begin to participate from the loan agreement and beyond. Actually, letters of intent come into the picture for commercial reasons and they are not intended to be enforceable documents. "In this respect the use of letters of intent provides a convenient excuse to leave lawyers out of the negotiating process..."47 The mandate establishes the platform for beginning the preliminary process of raising the money. Such a process basically consists of contacting banks, preparing a term sheet to outline the conditions of the credit for prospective lenders, producing the information memorandum, and negotiating the loan agreement.48 In other words, a letter of intent constitutes an assurance to the arranger that the borrower intends to obtain financing according to a price and under general financial and legal terms and conditions, but excludes the lender from any firm or specific commitment. The volatility of the international financial market is one of the reasons why lenders assume that these offer letters - returned to the lender as a mandate letter - are not final commitments.49 When the arranger receives the mandate from the borrower, the former will begin the marketing of the loan in order to achieve the required financing.50 Market expectations in relation to a borrower entity might vary from one day to another. In the case of sovereign lending, "country risk" and "sovereign risk"51 and "sovereign risk"52 may prevent the government from repaying public debt. For instance, the Mexican peso devaluation in 1994 had an important negative effect on debt transactions in most of Latin America (the "tequila effect"). As a general reaction to the crisis, financial investors preferred to shift their financial investments

47. Id.
49. See Gunter Dufey & Ian H. Giddy, THE INTERNATIONAL MONEY MARKET (1978). For an example of a syndicated loan transaction to United Airlines (UAL) which fails inasmuch as "adverse events" affected the "market's attitude", see Peter Lee, UAL: Inside the Fiasco of the Decade, in EUROMONEY, Nov. 1, 1989, at 58. Rodney Ballek, a Citibank executive responsible for the deal said, "the deal fell apart, not because of fundamental flaws in structure or pricing, but because of a litany of adverse events affecting the market's attitude to leveraged deals in general and airline financings in particular." Id. at 67.
52. "Sovereign risks arise only in transactions with a sovereign, such as lending, whereas country risks involve the whole host of credit risks peculiar to transacting business in a particular nation." Daniel W Heleniac, Sovereign Risks, in CURRENT ISSUES OF INTERNATIONAL FINANCE LAW 85 (David Pierce et al. eds., 1985).
53. For details about political risk in sovereign lending, see Anatole Kaletsy, THE COSTS OF DEFAULT 7-11 (1985).
to other areas of the world, such as Asia or Eastern Europe.\textsuperscript{54} Events like this could cause a syndicated loan transaction to fail. Accordingly, before delivering a formal offer, arrangers have to test the market first and then secure the funds to be provided. In order to do that, arrangers need to have a guideline of the conditions the borrower is willing to accept. They require an acceptance from the borrower of the business terms which are going to be represented by a mandate letter.\textsuperscript{55}

In spite of the above, according to English and American law, a document is not a contract just because it is denominated as a "letter of intent" or because the lender believes that the document is not legally enforceable. In an English case, \textit{Wilson Smithett & Cape (Sugar) Ltd. v. Bangladesh Sugar & Food Indus. Corp.},\textsuperscript{56} it was held that the particular label for identifying the document (letter of intent) was not an indication of its legal nature. The wording of the letter of intent, expressing the objective intention of the parties, is the crucial factor for the courts to determine if the document is intended to be contractually enforceable or not. Another important element courts would consider is the surrounding circumstances of the transaction. In general, English courts will look at the purpose of construing the document, at the document itself, at the surrounding circumstances, and at what happened whenever the document was brought into existence.\textsuperscript{57} Similarly, Canadian courts will examine "the document's purpose, its construction, the parties' conduct and the surrounding circumstances."\textsuperscript{58} However, American courts have a wider spectrum when the subject-matter is letters of intent. In the United States, good faith has been regularly added to the obligations deriving from pre-contractual agreements. In a New York case, \textit{Teachers Ins. and Annuity Ass'n of America v. Tribune Co.},\textsuperscript{59} the following elements were considered by the court in examining letters of intent: (1) the language of the document; (2) the context of the negotiations; (3) open terms not included in the preliminary


\textsuperscript{55} Id. at 39.

\textsuperscript{56} See \textit{Wilson Smithett & Cape (Sugar) Ltd. v. Bangladesh Sugar & Food Indus. Corp.}, 1 Lloyd's Rep. 378 (A.B. 1985). This case refers to a supply of sugar. The buyers issued a letter of intent with the purpose of accepting the terms and conditions of a selling offer. A paragraph of the letter stated, "We are pleased to issue this letter to you for supply of the following materials... All other terms and conditions will be as per your... offer dated 12.6.1981... You are advised to submit security/deposit performance bond... within seven days from the date of issue of this letter of intent..." \textit{Id.} Justice Leggat stated, "The fact that it has the particular label that it has does not brand it at the outset as a contractual document or as a non contractual document." \textit{Id.}

\textsuperscript{57} Id. Justice Leggat said, "It is common ground that when I come to look at the document styled by the defendants 'letter of intent', I must look for the purpose of construing it at the document itself, at the surrounding circumstances, and what happened when it was brought into existence." \textit{Id.}

\textsuperscript{58} Mills, supra note 15, at 358.

agreement; (4) partial performance by any of the parties; and, (5) customary practice. Also, American courts will consider whether the defendant has "failed as a matter of law to negotiate in good faith."60

A. THE 'SUBJECT TO CONTRACT' PROVISION.

According to the English courts, in order for a letter of intent not to be a contract, an express intention by the parties ("consensus at idem") must be included in the wording of the document.61 In English law, the phrase "subject to contract," (See Schedule III) is sufficient to reflect that the document is a pre-contractual agreement rather than a contract itself. There are other possible formulas, such as "subject to formal agreement"62 "subject to suitable agreements to being arranged,"63 and "subject to a proper contract."64 In our sample letter of intent in Schedule I the following clause is used: "The financing contemplated in this letter is conditioned upon the preparation, execution and delivery of legal documentation in form and substance satisfactory to us and our counsel...". Also, in Schedule II, which is a transaction governed by New York law, the second paragraph reads "XYZ's commitment is subject to the negotiation, execution and delivery of mutually acceptable definitive loan documentation ...". The language of these two examples seems to be common to American lawyers. Unlike the English courts, where objective interpretation of the wording of the document is essential, the intention of the parties is rather decisive for American courts.65

In English law, the phrase "subject to contract" has been accepted as the "term of art"66 to indicate that the parties have subjectively intended to have a non-binding "agreement to agree."67 Lake argues that "[a] significant difference in American and English law in the analysis of letters of intent ... is that parties to instruments governed by English law have an almost unqualified ability to remove any doubt as to intentions by the use of the phrase 'subject to contract.'"68 In Chillingworth v. Esche,69 Sangant LJ said that "the words 'subject to contract' or 'subject to formal contract' have ... acquired a definite ascertained legal meaning--... they are words appropriate for introducing a condition, and it would require a very strong and exceptional case for this clear prima facie meaning to be displaced."70 Thus, this formula is essential for avoiding legal enforceability, and in the absence of such an express intention of the parties, letters of intent would be defined by

60. See Lazard Freres & Co., supra note 59.
61. See Mills, supra note 15, at 357-58.
62. See id. at 360.
63. LAKE & DRAETTA, supra note 1, at 70.
64. Chillingworth v. Esche, 1 Ch. 97 (1924).
65. For an analysis of the English and American courts' interpretation, see LAKE & DRAETTA, supra note 1, at 67-75.
66. Id. at 69.
67. See Winn v. Bull, 7 Ch. D. 29 (1877); Rosstdale v. Denny, 1 Ch. 57 (1921); LAKE & DRAETTA, supra, note 1 at 69-70.
68. See LAKE & DRAETTA, supra note 1, at 94.
69. Chillingworth v. Esche, 1 Ch. 97 (1924).
70. Id. at 114.
English courts as binding agreements.\textsuperscript{71} \textit{Branca v. Cobarro}\textsuperscript{72} represents a major English case in this respect. The Court of Appeals held that there was a binding agreement even though a clause of the agreement said “this is a provisional agreement until a fully legal-\stackrel{z}{ised} agreement, drawn up by a solicitor and embodying all the conditions herewith stated, is signed.”\textsuperscript{73} The motive of the agreement was the selling of a mushroom farm where the defendant agreed to sell and the plaintiff agreed to deposit some money as part of the price.\textsuperscript{74} The plaintiff withdrew from the transaction and claimed his deposit back on the ground that there was no binding agreement.\textsuperscript{75} After analyzing the wording of the above mentioned clause, Lord Greene M.R. held that the agreement between the defendant and the plaintiff was intended to be a legally enforceable contract.\textsuperscript{76} The phrase “provisional agreement” and the condition “until” meant that a new contract would eventually be signed to replace the preliminary agreement.\textsuperscript{77} However, while this new contract had not come into place the “provisional agreement” had legal force.\textsuperscript{78} On the other hand, the fact that the future contract - which was supposed to replace the provisional one - was said to be a “fully legalized agreement” did not mean that the provisional agreement was not enforceable.\textsuperscript{79} In fact, the provisional agreement was enforceable and contained legally binding commitments for the parties.

\textbf{B. THE “SURROUNDING CIRCUMSTANCES”.
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In accordance with the above, “gentleman’s agreements,” or even informal business agreements among family members\textsuperscript{80} would be regarded as legally binding and enforceable contracts if no indication to the contrary is made by including the “magic phrase”, “subject to contract.” Nevertheless, this is not necessarily an absolute truth. There is an exceptional English case, \textit{Alpenstow Ltd. v. Regalian Properties Ltd.},\textsuperscript{81} where the phrase “subject to contract” was not considered sufficient to identify the document as non-binding. In this case, an agreement for a real estate transaction was identified as binding even though the clause “subject to contract” was included.\textsuperscript{82} In this case, Nourse J, referring to

\begin{footnotesize}
\begin{enumerate}
\item[72.] \textit{Branca v. Cobarro}, KB 854 (1947).
\item[73.] \textit{Id.} at 854.
\item[74.] \textit{Id.}
\item[75.] \textit{Id.}
\item[76.] \textit{Id.}
\item[77.] \textit{Id.}
\item[78.] \textit{Id.}
\item[79.] \textit{Id.}
\item[80.] Snelling \textit{v. Snelling Ltd., 1 All E.R.} 79 (1972).
\item[81.] \textit{Alpenstow Ltd., 1 W.L.R.} at 721.
\item[82.] Chillingworth, 1 Ch. at 97.
\end{enumerate}
\end{footnotesize}
the above quoted statement of Sangant L.J in *Chillingworth v. Esche*,\(^83\) held: “[i]n my judgment this is a case where there is a very strong and exceptional context which must induce the court not to give the words ‘subject to contract’ their clear prima facie meaning, and I so hold”\(^84\). This decision suggests that, although for English courts, the phrase “subject to contract” will in principle prevent agreements from being legally binding, there is a possibility that exceptional circumstances might make courts treat subject-to-contract-letters-of-intent as legally binding agreements.

Despite the fact that the “subject to contract” provision is extremely relevant for avoiding legal enforceability, courts might not confine themselves to the simple task of just checking whether the phrase is printed in the document to determine the legal nature of the agreement. As mentioned earlier, even English judges may consider other elements, such as the purpose of the document, the document itself, and the surrounding circumstances. We will now focus on this last element, as its inclusion in the analysis of the legal nature of the letter of intent reflects a departure from the classical common law approach which limits the analysis of the agreement to the frame of the document. As noted above, in an English case, *Wilson Smithett & Cape (Sugar) Ltd. v. Bangladesh Sugar & Food Indus. Corp.*,\(^85\) it was held that when the courts “come to look at the document”, they “must look” among other things “at the surrounding circumstances.”\(^86\) In *Alpenstow Ltd. v. Regalian Properties Ltd.*,\(^87\) the circumstances related to the fact that the agreement in question replaced and cancelled a previous legally binding agreement and created an exceptional context to induce the court not to give the “subject to contract” provision its prima facie meaning. In *Chillingworth v. Esche*,\(^88\) it was said that “there might be other circumstances” besides the words “subject to contract”\(^89\). Actually, courts look at the surrounding circumstances in order to identify the intention of the parties. In another English case, *Kleinwort Benson Ltd. v. Malaysia Mining Corp. Bhd.*,\(^90\) the judge said that “the court’s task is to ascertain what common intentions should be ascribed to the parties from the terms of the documents and the surrounding circumstances.”\(^91\) There is another English case, *Foley v. Classique Coaches Ltd.*,\(^92\) where the surrounding circumstances of the negotiations were also important to reach a decision.

\(^83\) Chillingworth v. Esche, 1 Ch. 97 (1924).

\(^84\) Alpenstow Ltd., 1 W.L.R. at 732.

\(^85\) Wilson Smithett & Cape Sugar Ltd., 1 Lloyd’s Rep. at 379.

\(^86\) Id.

\(^87\) Alpenstow Ltd. v. Regalian Properties Ltd., 1 W.L.R. at 730. Justice Nourse said, “Speaking generally, you would expect to find the words ‘subject to contract’ at the preliminary stage of a negotiation, not as here, some four to five months on. You would not expect to find them, as you do here, in a detailed and conscientiously drawn document which admittedly cancelled and replaced a previous binding agreement. I can well see that the question may not previously have arisen in circumstances such as these.” Id.

\(^88\) Chillingworth, 1 Ch at 111.

\(^89\) Id.


\(^91\) Id. at 386.

\(^92\) Foley v. Classique Coaches Ltd., 2 KB 1 (C.A. 1934).
For American courts, the intention of the parties is essential for determining the nature of the agreement; therefore, the surrounding circumstances play a key role for American judges. In *Itek Corp. v. Chicago Aerial Indus. Inc.*, the circumstances surrounding the negotiations determined that the parties intended to be bound by the letter of intent.

**C. INTENDED BINDING OBLIGATIONS DERIVING FROM THE LETTER OF INTENT.**

1. **Obligations of the Borrower.**

   Even though in most cases letters of intent are intended not to be firm commitments, mandate letters in syndicated loans are actually written in a certain way that constitute binding agreements with respect to certain issues. The borrower, when signing and delivering the mandate, is obliged from this moment to pay fees and expenses to the lender for the arrangement of the loan. This obligation of the borrower continues regardless of whether the credit is finally granted or not. In Schedule I, the clause titled “Expenses” shows that the borrower, upon signing the offer and returning it to the lender, agrees to pay expenses and fees “incurred in the negotiation, preparation and execution” of the loan. Moreover, the clause points out that “these expenses are reimbursable promptly on demand after execution of the loan documentation or if the documentation is not executed by April 30, 1991 after that date.” Even if the loan is not formalized, the expenses and fees would still be owed to the lender. Schedule II is even more specific about this matter. By making the borrower return a different letter (the “mandate”), the lender requires the borrower through this mandate letter (see Schedule II, Exhibit A) to expressly include that he “agrees to pay Arranger, XYZ and the Lenders’ reasonable out of-pocket costs and expenses... regardless of whether any loan documents are agreed to and signed by the lenders and the Borrower and regardless of whether any loans are actually made.”

2. **Obligations of the Lender.**

   Another binding commitment is the obligation of the lender or arranger to use his best endeavours or best efforts in order to finalize the financing arrangement as offered to the borrower. Moreover, at least for American courts, there is an implied obligation of good faith to finalize agreements referred to in letters of intent. These obligations are abstract obligations that are difficult to enforce inasmuch as they reflect uncertain and unspecific legal concepts. For example, a best endeavours clause provides for an abstract provision without specific measure or standard. Its determination will depend on a subjective interpretation by the courts.

**D. BEST ENDEAVOURS OR BEST EFFORTS.**

With respect to the borrower’s obligation to pay fees and expenses, there does not seem to be any doubt that there is an obligation to pay for the financial service the lender is providing. In relation to the best endeavours obligation, it appears to be difficult for the

94. “Best endeavours” is the expression commonly used in England while “best efforts” is used in the United States.
plaintiff to prove a breach of such an obligation inasmuch as there is no specific standard at which to look.\footnote{95} In an English case, \textit{Bower v. Bantam Inv. Ltd.},\footnote{96} an injunction was refused because there was no specific obligation to use best endeavours to develop a marina project. Goff J said "I ask myself, could anything be less specific or more uncertain? There is absolutely no criterion by which best endeavours and practicability are to be judged."\footnote{97} In a few words, the judge argued that best endeavours duties cannot be obligations because they do not represent something specific to do or fulfill.\footnote{98} However, Karamanolis argues that "best efforts" imply a certain direction to the bank to implement "professional judgment, technical skills and specialist personnel."\footnote{99} But, again, this appreciation is still too subjective in the sense that it is discretionary for the bank to use its particular technique and judgment and to designate the employees it believes are adequate for managing the transaction. Therefore, the best endeavours or best efforts provision gives the lender or arranger a unilateral consideration of what he may or may not do to raise the corresponding funds. Ultimately, courts will make a case-by-case analysis focusing on the kind of promise and the relation of such a promise to the promisor's implicit skills.

There might be no difficulty for courts to enforce best endeavours obligations if the lack of diligence is obvious. In an American case, \textit{Grossman v. Lowell},\footnote{100} a best efforts duty of a purchaser to find a loan was breached because the purchaser made very few attempts to pursue the expected results (three telephone calls and one mortgage application). But again, the analysis of the best efforts duty depends on each particular situation. The question will always arise: What is the level of efforts required? (e.g. How many calls, meetings or letters should one make in order to comply with the best efforts provision?)

In financial services, a certain best efforts standard could be identified. For instance, the syndication of a loan incorporates a process which invokes a certain sequence of steps and implies specific activities such as inviting banks to participate in the loan (marketing the loan), assisting the borrower in preparing the information memorandum, and drafting and negotiating loan agreements.\footnote{101} The arranger should possess specific technical skills and experience for managing the syndication process. According to this, we ask ourselves what is the level of efforts required by the promisor (the arranger)? The common test for American courts in cases when a promisor offers special skills and experience to others who lack it is to ask "what efforts a third person - a person possessing those skills - would use if that person were in the promisor's place."\footnote{102} The syndication business is a particular area which involves specialized banks. Normally, all syndicated credit transactions have similar characteristics and specialized banks follow a certain pattern. Thus it appears that the test would certainly proceed for these transactions. A standard of best efforts could be defined by analyzing the customary practice of persons involved in that business.

\footnotesize{95. \textsc{Donaldson}, \textit{supra} note 48, at 83. \textit{See also} \textsc{Dufey} \& \textsc{Giddy}, \textit{supra} note 49, at 251. 
97. \textit{Id.}
98. \textit{Id.}
99. \textit{See} \textsc{Karamanolis}, \textit{supra} note 36, at 63.
101. \textit{See} \textsc{UNITAR}, \textit{supra} note 23 at 107; \textit{see} \textsc{Clark}, \textsc{et al.}, \textit{supra} note 48, at 410-11; \textit{see also} \textsc{Davies} \& \textsc{Halliday}, \textit{supra} note 8, at 182.
102. \textsc{Allan Farnsworth}, \textsc{Farnsworth on Contracts} 9 (1990).}
E. GOOD FAITH.

Even though the terms good faith and best efforts might be mistakenly seen as synonyms, they are different concepts which imply different duties. Whereas best efforts obligations are related to the concept of diligence of the promisor, good faith is connected with honesty and fair dealing. Good faith obligations exist in American law. The United States Uniform Commercial Code establishes that either contracts or other duties regulated by this Code impose "an obligation of good faith in its performance or enforcement." Moreover, American courts have begun to define letters of intent as enforceable whenever there is a lack of good faith to use best efforts to finalize the contract. English courts, on the other hand, are reluctant to impose any liability in tort for breach of contract. Accordingly, duties of good faith and fair dealing in contractual obligations are rarely considered by these courts. In the case of pre-contractual agreements, the situation would be even more strict as they are not intended to be binding agreements. In an Arkansas case, Sterling Faucet Co. v. First Mun. Leasing Corp., the court held that a letter of intent was enforceable and represented a binding commitment even though it contained a phrase that indicated the commitment was conditioned on further documentation being "satisfactory in substance and form to all parties." The court stated that there was a lack of good faith from the lender to decide if credit documents were satisfactory. Cases such as this show the importance of drafting letters of intent with express and detailed language to assure that the borrower is clear that there is a non binding commitment from the lender or arranger. In this regard, Weisman suggests the following wording:

This letter sets forth proposed terms for discussion purposes only, and is not a commitment or an offer to lend.

As mentioned earlier, the borrower accepts the terms and conditions of the offer letter by returning a mandate letter to the lender or arranger. At this moment, the borrower counts on the lender or arranger to raise the money required, and the lender might incur losses for the borrower if the transaction fails. In an American case, 999 v. CIT Corp., $1 million in damages were awarded to a borrower who alleged that the lender had made a firm commitment to lend. Lack of good faith is the basis for court decisions in cases like this. If it is proved that the borrower has "reasonable expectations" that the financing, will be provided, a binding agreement could be considered to exist. The existence of reasonable expectations would derive from the language of the mandate which would express

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103. See id. at 8; LAKE & DRAETTA, supra note 1, at 178; ROY GOODE, COMMERCIAL LAW 542, 574 (1995).
106. GOODE, supra note 103, at 109; see also Parker Hood, Lender Liability Under English Law, in BANKS, LIABILITY, AND RISK 33 (Ross Cranston ed., 1995).
108. Id. at 9.
109. See Weisman, supra note 21, at 2-3.
110. Id. at 3.
111. 999 v. CIT Corp., 776 F.2d 886 (9th Cir. 1985).
that a firm commitment has been made by the lender. In another American case, Hoffman v. Red Owl Stores, Inc.,\(^{113}\) the court awarded damages to the borrower because it was decided that there was substantial reliance on the offer of the lender. However, the decision was based on the fact that one party, a small company, was not as sophisticated as the other, a bank. Promissory estoppel was the legal action used to enforce good faith and the argument was that the bank's promise made the other party act in a certain way with the expectation that the promise would be fulfilled.\(^{114}\)

In Itek Corp. v. Chicago Aerial Indus., Inc.,\(^{115}\) and Thompson v. Liquichemica of America, Inc.,\(^{116}\) it was held that good faith represents a contractual obligation when parties have undertaken to use best efforts to prepare and conclude a contract. In this respect, parties must act in good faith in order to use best efforts to achieve a result. In Thompson v. Liquichemica, the judge stated that "unlike an 'agreement to agree', which does not constitute a 'closed' proposition, and consequently is not an agreement at all, an agreement to use best efforts is a closed proposition, discrete and actionable. Such an agreement does not require that the agreement sought to be achieved, but does require that the parties work to achieve it actively and in good faith."\(^{117}\)

In a recent American case, Lazard Freres & Co v. Protective Life Ins. Co.,\(^{118}\) the United States District Court for the Southern District of New York held that commitment letters in bank debt transactions can constitute legally binding obligations and the "execution of a binding preliminary agreement requires a party to continue good faith efforts to finalize a contract."\(^{119}\) In this case, a condition in the commitment letter existed which established that the agreement was subject to the "preparation, review and execution of documentation acceptable to Lazard and Protective."\(^{120}\) In spite of this, the court decided that this "condition precedent" was excused as the defendant "failed as a matter of law to negotiate in good faith."\(^{121}\) This case provides an important basis in the United States for identifying letters of intent as binding agreements if good faith efforts have not been fulfilled. With respect to this case, the New York law firm of Paul, Weiss, Rifkind, Wharton and Garrison suggests the following clause in order to express more clearly a non-binding intention:

\[
[T]his \text{ commitment letter creates no binding obligations whatsoever, and the parties intend to be bound only after closing documentation has been agreed upon and executed by both parties.}^{122}\]

\(^{112}\) Weissman, supra note 21, at 6-7.

\(^{113}\) Hoffman v. Red Owl Stores Inc., 133 N.W. 2d 267 (Wis. 1965).

\(^{114}\) See Mills, supra note 15, at 383-87.


\(^{117}\) Id. at 366.


\(^{119}\) Id.

\(^{120}\) Id.

\(^{121}\) Id.

\(^{122}\) See Paul et al., supra note 59, at 495.
The same New York law firm states:

Based on our experiences, parties executing commitment letters generally intend to be bound to proceed in good faith towards closing and to negotiate in good faith closing documentation. Parties do not intend to give each other 'free options' to walk away from the deal under the guise of failing to agree on definitive documentation.\textsuperscript{123}

Unlike the United States, English law takes a different approach regarding letters of intent. This system of law identifies the letter of intent either as a contract or as an "agreement to agree", which is not enforceable. No intermediate solution exists. However, in the United States, the courts' interpretation is wider. In the case mentioned, it might be said that there is a binding agreement to negotiate in good faith.\textsuperscript{124} But in many cases, depending on the circumstances, courts have also taken the all-or-nothing approach. Moreover, a letter of intent has been held as enforceable in one situation and as not enforceable in a similar situation. In any case, the decision will rely on the particular cases and no specific prediction can be made. Therefore, lawyers should use very clear wording which denotes specifically the intention of the parties.

V. Legal Actions and Remedies for the Sovereign Borrower.

The borrower would incur a great loss if the arranger bank came to him and said, "Sorry, we thought we could do it but..."\textsuperscript{125} On the other hand, the arranger, besides demanding at least reimbursement of costs and expenses, will deny any liability and will refuse to pay the borrower for losses and damages as a consequence of the syndication failure.\textsuperscript{126} Normally, the arranger, who has signed a letter of intent which includes the respective wording that excludes contractual liability, will retract from any obligation to the borrower. Considering this situation, what legal actions could the borrower take?

The first important issue to examine is if the promise to arrange financing, contained in the letter of intent, involves contractual liability. As we have pointed out above, the wording of the document will play an essential role for determining the legal nature of the document. In the event the "subject to contract" provision appears, then a strong likelihood of a non binding commitment is present. However, the surrounding circumstances of the transaction should also be observed in order to define the objective intention of the parties. As we have mentioned earlier, this is more accentuated by American courts than by English courts. If the letter of intent is a binding agreement, remedies will be those of breach of contract.\textsuperscript{127}

Nevertheless, even though the promise to complete the syndicated financing is not binding, there remains an obligation upon the lender to use its best endeavours to com-

\textsuperscript{123} See id.
\textsuperscript{124} See Mills, supra note 15, at 385; see also Thompson, 481 F. Supp. 365.
\textsuperscript{125} DUFEY & GIDDY, supra note 49, at 247; see also Lee, supra note 49, at 64, for a case where the share price of a borrower greatly declined when the loan collapsed.
\textsuperscript{126} For an example of a $7.2 billion syndicated loan to United Airlines which failed and arrangers refused to accept its responsibility, see Lee, supra note 49, at 58.
\textsuperscript{127} For an explanation about remedies for breach of contract, see Goode, supra note 103, at 115-132. See also RICHARD TUFFARO, LENDER LIABILITY LITIGATION: RECENT DEVELOPMENTS 29-34 (1987).
plete the transaction. In this respect, it should be ascertained whether the bank has execut-
ed the arranging activity with a sufficient degree of diligence to fulfill the best endeavours
obligation. Another issue to observe is whether there was bad faith on the part of the
arranger by not finalizing the financing. As previously explained above, to determine bad
faith on the part of the defendant, the plaintiff must prove “reasonable expectations” or
“substantial reliance” in the defendant’s promise. If these claims proceed, the remedy
would be reliance damages. In the United States, promissory estoppel could be a possi-
bility when it is proved that the borrower relied on the lender’s promise. Besides English
law’s promissory estoppel being “fundamentally” different from the United States’, a cause
of action for promissory estoppel exists in the latter while not in the former. Negligent
misrepresentation might be another cause of action. This concept requires that: (i) a rep-
resentation is made; (ii) the defendant has particular skills that made the plaintiff reason-
ably rely on an express promise; and (iii) there was damage caused to the plaintiff as a con-
sequence of the reliance to the defendant. In this respect, Mills states that “a letter of intent could be characterized by a plaintiff as a representation made by the defendant to bargain in good faith.”

Another cause of action, though unlikely to succeed, is fraud. There is a case, Kas v. Chase Manhattan Bank, N.A., where after a syndicated loan arrangement collapsed, plaintiff sued the defendants for fraud and misrepresentation. The plaintiff alleged they purchased some shares of UAL Corporation after relying on the defendant’s fraudulent representation contained in a financing letter of intent the defendants asserted in their letter of intent that they were “highly confident” to arrange financing to the management group (Airline Acquisition Corporation) which was interested in acquiring UAL. Because of the defendant’s failure to raise financing, UAL stock suffered an important decline in price, and consequently the plaintiff incurred losses. The complaint was dismissed, as there were insufficient arguments to prove “conscious behavior” by the lender to constitute fraud. The judge stated that “intending to participate in a risky transaction is not the equivalent of intending to perpetrate a fraud.”

Inasmuch as this essay attempts to focus on the legal nature of the letter of intent, we
will not concentrate on the analysis of the lender’s liability. In considering the existence of a contractual promise to lend in a letter of intent, study of the “amorphous concept” of lender liability can be analysed. At least, it is important to understand that, in general, remedies for lender liability would be limited to damages. This means that specific perfor-

130. See Mills, supra note 15, at 371. See also LAKE & DRAETTA, supra note 1 at 193-95.
132. LAKE & DRAETTA, supra note 1, at 196.
134. Id. at 3.
135. Id.
136. Id. at 6.
137. Hood, supra note 106, at 15, states that “lender liability is a somewhat amorphous concept.”
138. For English law, see CRANSTON, supra note 90. For United States law, see WEISSMAN, supra note 21; TUFFARO, supra note 127.
mance is not applicable. Accordingly, the damages that can be claimed would be, for instance, higher interest, and the costs and expenses incurred by the borrower for having to arrange a different loan.¹³⁹

VI. Conclusion.

We have observed in this essay that, legally speaking, letters of intent are abstract documents which are made in order to regulate the pre-contractual scenario of a business transaction. In English and American law, the intention of the parties is the main issue to define the legal nature of agreements. Generally speaking, letters of intent are not intended to be binding agreements. For either English or American courts, the language of the document will be the key factor in defining the intention of the parties. However, the surrounding circumstances are also taken into consideration, even more so in the case of American law, where judges have been less attached to the wording and have rather stepped a little aside from the the written agreement to look for the objective intention of the parties.

In syndicated loans, letters of intent set up the terms and conditions of the credit while establish at the same time an obligation from the borrower to pay certain fees. On the other hand, letters of intent express an obligation upon the arranger to exercise its "best endeavours" to finalize the financing. Borrowers should be aware of the legal nature of the document they are willing to sign. Regularly, lenders will say that letters of intent contain a unilateral obligation from the borrower to carry the costs and expenses of the preliminary process, even if positive progress is not achieved by the lender. The latter, however, would not be willing to commit itself more than in a "best endeavours" basis.

Borrowers must understand that the "best endeavours" obligation of the lender is an unspecific term which is intended to leave the determination of the standard of efforts to the lender's own means. However, even on a best efforts basis, arrangers assume a significant risk when issuing funding commitment letters.¹⁴⁰ Institutions, such as those involved in the syndicated financing business, have specific expertise in this matter, which causes borrowers to rely on them. Besides that, the customary practice of the business might create certain expectations from those institutions to utilize some standard of efforts for completing the syndicated credit. Therefore, lenders should be aware that even though the completion of the transaction is subject to "best efforts", these duties can be enforced by the borrower by analyzing the customary practice and defining a standard of diligence.

Moreover, a loss in reputation for banks can follow as a consequence of a syndicated loan collapse. The United Airlines syndicated finance's failure as explained in Kas v. Chase

¹⁴⁰ In Kas, supra note 133, the judge stated that "[i]n fact, the UAL transaction is an excellent illustration of the significant risk financial institutions assume in issuing funding commitment letters. The UAL transaction failed because of defendants' inability to obtain financing, and rather than attaining prestige and market leadership, defendants were blamed for the financial 'fiasco of the decade.'" 1991 WL 275754, at 3.
Manhattan Bank, N.A. is an important example. Referring to this case, where well-recognized banks such as Citibank and Chase Manhattan were the main actors, a Euromoney article pointed out that, "the collapse of the $7.2 billion United Airlines buyout loan is a story of error upon error, of proud reputations suddenly tarnished." As a matter of fact, besides arrangers' interest in finishing the deal and charging their commission, there is a pressure upon them not to damage their reputation if the deal falls down. In this sense, arrangers would use their best efforts to complete the syndicated loan. Nevertheless, from the point of view of borrowers and more importantly, sovereign borrowers, the question is not just one of reputation if a syndicated loan collapses. A borrower would be affected by material losses if another financing is not efficiently achieved to replace the original one. Furthermore, in the case of sovereign lending, the failure of a credit might lead to the failure of a State project development, which will consequently affect the socioeconomic welfare of a country.

Letters of intent must establish conditions and obligations which are clearly understandable to the borrower and the lender. Specifically, sovereign borrowers, before accepting a financing proposal, should be aware of the conditions the proposal contains. Moreover, sovereign borrowers must negotiate a letter of intent which provides better warranties for finalizing the financing. For instance, Gurria-Trevino suggests sovereign borrowers should avoid "best effort offers" because they imply a non-specific commitment from the lender. However, based on the volatility of the financial market, only desperate banks would accept committing themselves to a syndicated loan arrangement on an unconditional basis before analyzing the market's appetite for the loan. Accordingly, sovereign borrowers, such as entities responsible for State indebtedness, must choose experienced and well-known financial institutions which are concerned about not threatening their prestige by signing letters of intent for unsuccessful syndicated credits. Definitely, regarding the volatility of the financial markets, it would be also convenient for sovereign borrowers and more specifically for FBCAs to alleviate their long and complicated internal legal process of authorization.

141. Kas, supra note 133, at 1.
142. See Lee, supra note 49, at 58.
143. Gurria-Trevino, supra note 6, at 391.
144. See Papanicolaou, supra note 6, at 48.
145. See supra Part III, § 2.