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LETTER OF INTENT UNDER INDIAN LAWS – IS IT LEGALLY ENFORCEABLE?

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(This article has been co-authored by the team of LexCounsel and VFS Global)

LexCounsel Team:

By: Seema Jhingan, Partner
(sjhingan@lexcounsel.in)

Neha Yadav, Senior Associate
(nyadav@lexcounsel.in)

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Execution of valid contracts is a prerequisite to creation of any legally binding rights and obligations among the executing parties. However, before moving on to detailed definitive contract(s), parties often enter into a letter of intent so as to agree and specify upfront the key terms of the proposed transaction. The idea is to identify and address any major commercial issues between the parties, and at the same time demonstrate their commitment to the transaction.

What then is the legal effect of a letter of intent? Executed at a pre-contractual stage, is it a legally binding document or is it only a means to capture and reflect the intention of the parties on the basic structure of the transaction?

It is a well settled legal position under Indian laws that an agreement to 'enter into an agreement' is neither enforceable nor does it confer any rights upon the parties. It is also a well settled principle of law that a letter of intent generally indicates a party's intention to enter into a contract with the other party in future. A letter of intent is not intended to bind either party ultimately to enter into any contract. Such non-binding letter of intent can however also take a hybrid form where parties agree to be bound by certain identified provisions such as confidentiality; exclusivity; costs/expenses; governing law/jurisdiction etc.

Ordinarily, if a letter of intent or any other contractual document expressly confirms that no contractual obligations are created between the parties, then there is an assumption that no valid and binding contract has been created between the parties. However, if the language of the letter of intent or such contractual document is not clear in this regard, then the question of whether a binding contract has been concluded thereby or not remains

VFS Global:

Mr. Venkatesan Narayanan,
Head Legal & General Counsel
NarayananV@vfsglobal.com

LexCounsel, Law Offices C-10,
Gulmohar Park New Delhi 110 049,
INDIA. Tel.:+91.11.4166.2861
Fax:+91.11.4166.2862

Recommended by:



the subject matter of judicial assessment on a case to case basis. During such assessment, the intention of the parties, the nature of the transaction, the language employed in the letter/document, subsequent conduct of the parties and ancillary facts and circumstances, usually need to be looked at.

For instance, in *Rajasthan Co-op Dairy Federation Ltd Vs. Maha Laxmi Mingrate Marketing Service Pvt. Ltd.*¹, the Supreme Court observed as under:

“The Letter of Intent merely expresses an intention to enter into a contract..... There was no binding legal relationship between the appellant and the respondent 1 at this stage and the appellant was entitled to look at the totality of circumstances in deciding whether to enter into a binding contract with respondent 1 or not.”

The Hon'ble Punjab and Haryana High Court observed in a case² with respect to binding nature of letters of intent that, if various steps had been taken for awarding the contract and considerable amounts spent, then a legitimate expectation was created that in the absence of any adverse factor, the contract would be awarded.

Also relevant is the case of *Dresser Rand S.A. vs. Bindal Agro Chem Ltd. and K.G. Khosla Compressors Ltd*³, in the specific facts whereof, one of the disputing parties had invited global tenders for supply of various equipment and materials, and the other disputing party (viz., the bidder) had sent a letter offering to supply the same. Resultantly, letters of intent were issued in favour of the bidder. However, later, the bidder was informed that the tenderer would instead purchase the tendered equipment and materials from a third party, thus giving rise to a dispute between the tenderer and the bidder. One of the issues considered by the Hon'ble Supreme Court of India while adjudicating the dispute was whether the letter of intent was a contract binding the parties and it observed as under:

“...it clear that the letter of intent is only a prelude to the purchase order and not itself the purchase order... ..Clause (M) made it clear that the Letters of Intent were being issued subject to necessary approvals being given by the Authorities of the Indian Government. These provisions clearly indicate that the Letters of Intent were only a step leading to purchase orders and were not, by themselves, purchase orders.....It is now well-settled that a Letter of Intent merely indicates a party's intention to enter into a contract with the other party in future. A Letter of Intent is not intended to bind either party ultimately to enter into any contract.”⁴

Further, by necessary implication, non-binding or conditional agreements/letters of intent remain subject to revocation at the instance of either party, or automatic cancellation upon non-fulfilment of the condition(s) on which their performance is contingent.

Also, specifically with respect to letters of intent issued by Government authorities, such letters may be cancelled by the concerned authorities if there is a supervening public interest involved. To this end, reference may

be drawn to the Hon'ble Supreme Court of India's observations in the case of *Madhya Pradesh Mathur and Ors. v. DTC and Ors*, (2006) 13 SCC 706⁵, reproduced below:

"...once public interest is accepted as the superior equity which can override individual equity the principle would be applicable even in cases where a period has been indicated for operation of the promise. If there is a supervening public equity, the Government would be allowed to change its stand and has the power to withdraw from representation made by it which induced persons to take certain steps which may have gone adverse to the interest of such persons on account of such withdrawal. Moreover, the Government is competent to rescind from the promise even if there is no manifest public interest involved, provided no one is put in any adverse situation which cannot be rectified...the Government could change its industrial policy if the situation so warranted and merely because Resolution was announced for a particular period, it did not mean that the government could not amend and change the policy under any circumstances."

The above discussions and observations also find place in another notable judgment of the Hon'ble High Court of Gujarat⁶. In the specific facts of this case, the tender issuing authority had cancelled the tender process in which a bidder had been identified as the highest bidder, which bidder had also been issued a letter of intent pursuant to selection of bids. The bidder challenged such cancellation by the tenderer *inter alia* on the ground that since a letter of intent had been issued in its favour, the bidder was entitled to a letter of allotment and award of the underlying contract in its favour. The Hon'ble High Court observed as under:

"The letter of intent issued by the Respondent was merely an expression of intention and imparting an information that the Petitioner stood highest bidder and on receipt of CRZ clearance, the formal letter of allotment would be issued. However, the Petitioner had not cooperated in the meantime for obtaining CRZ clearance and before any formal letter of allotment is issued, the earlier tender process stood cancelled. Even while cancelling the earlier tender process, the Respondent Port Trust neither acted arbitrarily nor it would amount to any malafide exercise of discretionary powers..... The Respondent is well within its rights to take such a decision in the year 2010 keeping in mind the larger public interest...The letter of intent issued by the Respondent Port Trust on 12.01.2006, at best, can be said to be an agreement to issue the allotment letter and to execute the lease document in favour of the Petitioner subject to fulfilment of certain conditions. However, in absence of issuance of allotment letter, the said letter of intent cannot be enforced in the Court of law.... Such a letter of intent is not intended to bind either party ultimately to enter into any contract..."

In T. S.Venkatesa Iyer's 'The Law of Contracts & Tenders', it is stated:

"By giving a letter of intent, a party cannot be said to have intended to agree or do anything in order to give rise to a binding contract."

In Cheshire, Fifoot and Furmston's Law of Contract (Twelfth Edition, Pg. 43), it is stated:

“A letter of intent is a very commonly employed commercial device by which one party indicates to another that he is very likely to place a contract with him.”

It would, therefore, appear that the chances of enforcing a non-binding agreement/letter of intent are ordinarily low. However, as discussed hereinabove, judicial determination of letters of intent remains subject to the specific facts of each case and the provisions of the respective letters.

Parties often consider a letter of intent which sets out the crux of the transaction, a practical and easy to enter document to assess upfront, the broad pros and cons of the transaction and arrive at broad commercial understanding agreeable to all. So, in cases where a letter of intent is being entered into and is intended to be non-binding, care should be taken that the letter of intent clearly states that it does not constitute any contractually binding relationship between them. The parties also should not act upon the letter of intent (or initiate any work pursuant to it) as if they had legally binding agreement, to avoid possible disputes in future.

It is therefore advisable for executing parties to protect their interest by entering into definitive agreement prior to initiation of contract work to avoid long protracted litigation to prove the very legality of their contractual arrangements.

Endnotes

¹ Civil Appeal No. 2679 of 1992, Decided on 17.09.1996

² Bhoruka Power Corporation Limited v. State of Haryana and Ors, AIR 2000 P&H 245.

³ AIR 2006 SC 871

⁴ Also reiterated in M/s. KaramchandThaper & Bros (C.S.) Ltd., v. M/s. M.P. Power Trading Co. Ltd 2012 ELR (APTEL) 1185; Nikhil Adhesives Limited thro' DharmeshbhaiDhirajbhaiPandya v. Kandla Port Trust 2011 GLH (2) 283. Also see Rajasthan Co-operative Dairy Federation Ltd. v. MahaLaxmiMingrate Marketing Service Pvt. Ltd. AIR 1997 SC 66; Speech and Software Technologies (India) Pvt. Ltd. v. Respondent: Neos Interactive Ltd (2009) 1 SCC 475.

⁵ Also see Shrijee Sales Corporation and Anr. v. Union of India 1997(89)ELT452(SC); Pawan Alloys and Casting Pvt. Ltd. v. U.P. State Electricity Board and Ors. (AIR 1997 SC 3910)

⁶ Refer Nikhil Adhesives Limited thro' DharmeshbhaiDhirajbhaiPandya v. Kandla Port Trust, 2011 GLH (2) 283.

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