

LITIGATION & DISPUTE RESOLUTION (LDR)

Preliminary agreements in Australia – are they enforceable?

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Preliminary agreements are common precursors to complex commercial contracts, and take the form of documents such as heads of agreement, letters of intent and memoranda of understanding, to name a few. They are also used in the context of conveyancing of properties, sale of business and supply of goods or services.

The enforceability of the preliminary agreements has been a long standing and persistent issue in Australian law. Whether these agreements are enforceable will turn upon a number of principles laid down by Australian authorities.

They are generally not enforceable if they amount to no more than a mere 'agreement to agree'. However, there are numerous cases where the courts have found such agreements to be binding.

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When will preliminary agreements be binding?

In the seminal case of *Masters v Cameron* (1954) 91 CLR 353, which was decided in the highest court in the Australian court hierarchy – the High Court of Australia, it was held that only certain categories of preliminary contracts will be binding.

The Court noted that in circumstances where the negotiating parties have reached agreement upon contractual terms, but have decided that the substance of their negotiations will be dealt with in a formal contract, the agreement may belong to one of three classes:

- the parties have reached finality in arranging all the terms of their bargain and intend to be immediately bound

to the performance of those terms, but at the same time propose to have the terms restated in a form which will be fuller or more precise but not different in effect;

- the parties have completely agreed upon all the terms of their bargain and intend no departure from or addition to that which their agreed terms express or imply, but nevertheless have made performance of one or more of the terms conditional upon the execution of a formal document; or
- the intention of the parties is not to make a concluded bargain at all, unless and until they execute a formal contract.

The Court held that preliminary agreements falling into the first two classes will be binding, however, preliminary agreements belonging to the third class will not be enforceable because there is no intention by the parties to be bound.

Accordingly, the enforceability of a preliminary agreement that satisfies the basic requirements of a legally binding contract (such as the terms of the contract being sufficiently certain and complete) will ultimately turn upon whether the parties intended to be bound.

How do courts determine the intention of parties?

The issue of whether the parties intended to be bound by the preliminary agreements is to be determined objectively.

In determining the parties' intention, the courts will consider the wording of any correspondence exchanged between the parties, the nature of the negotiations, the history and behaviour of the parties and the circumstances giving rise to the dispute generally (see generally *Pavlovic v Universal Music Australia Pty Ltd* [2015] NSWCA 313 and *Feldman v GNM Australia Ltd* [2016] NSWSC 920).

The recent case of *Nurisvan Invest-*

ment Ltd & Anor v Anyoption Holdings Limited [2017] VSCA 141 is a useful example of how the courts ascertain the intention of the parties. The Court in that case noted that the use of expressions in the heads of agreement such as 'the Vendor wishes' and 'the parties wish' demonstrated that there was no present obligation on the parties, only an expression of what they wished to do in future.

The terms in the agreement also left much to be negotiated. On that basis, the Court concluded that the heads of agreement did not constitute a binding contract between the parties, and amounted to no more than an agreement to negotiate in good faith to reach a final contract.

Conclusion

Parties to negotiations must clearly express their intention when entering into a preliminary agreement.



If the preliminary agreement is not intended to be legally binding, parties should not simply rely on a 'subject to contract' term contained in the agreement. Instead, it is prudent to clearly state that none of the parties intend to be bound by the agreement (or any part thereof), and that the provision of the agreement does not constitute a formal offer, nor does its 'acceptance' constitute a binding agreement between the parties.