

**BARBADOS.**

**[Unreported]**

**IN THE SUPREME COURT OF JUDICATURE**

**COURT OF APPEAL**

**Civil Appeal No. 19/2001**

**BETWEEN:**

**WILLIAM E. LOCKE JR**

**(Appellant)**

**AND**

**BELLINGDON LIMITED**

**(First Respondent/First Defendant)**

**EASTERN RESORTS LIMITED**

**(Second Respondent/Second Defendant)**

**PARADISE BEACH LIMITED**

**(Third Respondent/Third Defendant)**

**SANDALS RESORTS INTERNATIONAL LIMITED**

**(Fourth Respondent/Sixth Defendant)**

**Before: The Hon. Sir David Simmons, K.A. B.C.H., Chief Justice, the Hon. Errol Chase, C.H.B., Justice of Appeal, and the Hon. Colin Williams, Justice of Appeal**

**2002: October 2, 3, 4, 7, 8 & December 6.**

**Dr. R.L. Cheltenham Q.C., Mr. G.C. Turney Q.C. of R.G. Mandeville and Co., and Mr. Alrick Scott for the Appellant.**

**Mr. R. Mahfood Q.C. and Mr. Ramon Alleyne of Clarke, Gittens & Farmer for the First and Second Respondents.**

**Sir Henry Forde Q.C. and Mr. Brian Clarke of Clarke, Gittens & Farmer for the Third and Fourth Respondents.**

**JUDGMENT**

SIMMONS C.J.: This appeal may be referred to as "William E. Locke Jr. v. Bellingdon Limited No.2". Twice in this year the Court of Appeal has heard and determined appeals involving these parties. The first appeal was against certain interlocutory orders relating to security for costs pending appeal and the quantum of a cross-undertaking as to damages.

[2] In this appeal, interesting and important aspects of the law of contract fall for consideration. These include construction of an agreement, the legal nature and effect of a Letter of Intent in [1] commercial transactions, the doctrine of "subject to contract", communication of acceptance, the concepts of "fundamental breach" and "breach of a fundamental term" and repudiatory breach of contract. These several matters arise because the appellant (Locke) appeals the decision of Payne J who, at the trial, refused his claims for specific performance and various injunctions in respect of an alleged agreement for the sale and purchase of shares in two companies together with a promissory note which evidenced and acknowledged an inter-company debt.

The Parties

[3] Locke is an American businessman. Bellingdon Limited (Bellingdon), the first respondent, is a company registered and incorporated in the Isle of Man. The other parties are: Eastern Resorts Limited (Eastern), the second respondent, a U.K. company; the third respondent, Paradise Beach Limited (Paradise), a Barbados registered company and the owner of a very desirable piece of beach land on which stands the former Paradise Beach Hotel on the West Coast of Barbados, and Sandals Resorts International Limited (Sandals) is the fourth respondent. It is not registered as a company in Barbados but is alleged to be the ultimate beneficial owner of the shares in Paradise. Two directors of Sandals, namely, Gordon "Butch" Stewart and Patrick Lynch, were original defendants in the action but were struck out of the action by Payne J on October 4, 1999. There was an inter-company debt of \$11 million owed by Paradise to Bellingdon and this was acknowledged by a promissory note from Paradise to Bellingdon.[2]

## The Facts

[4] For some time prior to March 16, 1999, Locke had been interested in purchasing the Paradise Beach Hotel site located adjacent to the junction of three important highways with a beach frontage of approximately 900 metres. The legal vehicle by which Locke intended to purchase the site was not by purchase of the land but, rather, by purchase of the shares in Paradise and the inter-company debt acknowledged by the promissory note. On March 16, 1999, Locke therefore sent a Letter of Intent (the Letter) to Patrick Lynch of Sandals.

[5] In that Letter provision was made for Locke to conduct a due diligence exercise and, with the co-operation of the respondents, he commenced that exercise. Lynch signed the Letter on April 16, 1999 but did not return it to Locke. Locke had not paid an initial deposit of US\$100,000 and, according to Lynch, that was the reason why he did not return the Letter to Locke. On the other hand, Locke's evidence was that he did not pay the deposit because, in a telephone conversation with Lynch on March 25, 1999, Lynch had waived the requirement for payment of the deposit if he (Locke) undertook to complete the due diligence exercise within 2 to 3 weeks. The terms of that telephone conversation were disputed by Lynch and Locke, each of whom gave a different version of the conversation in evidence. The trial judge was therefore called upon to make a finding as to which version of the conversation he accepted and, suffice it to say at this stage, the trial judge accepted Lynch's version.[3]

## The Pleaded Cases

[6] The substantive pleadings on which the trial was contested were a re-amended Statement of Claim and an amended Defence. It was the appellant's case that Paradise and Sandals had offered to sell him all of the shares in Paradise together with the promissory note for a total sum of US\$19 million.

According to the re-amended Statement of Claim, sale and purchase were to be effected by a "two-stage process". Stage 1 was for the parties to negotiate and agree the terms of the Letter and, in accordance with the Letter, three events were to take place. First, the property was to be taken off the market in consideration of a deposit of US\$100,000 paid to an agreed escrow agent; secondly, Locke was to carry out a due diligence exercise against the respondent companies within 60 days "to enable a stock purchase agreement to be concluded within a further 30 days" after the initial period of 60 days. Thirdly, the appellant alleged that "upon conclusion of the stock purchase agreement the purchaser was to pay a further sum of US\$900,000 making a combined deposit of US\$1,000,000."

Stage 2 was not pleaded but, in the course of argument, Locke's Counsel told us that the second stage was "a mere formality concerned with the date of the deposit and the date of closure."

[7] In view of their centrality to this appeal we think it useful to refer to other parts of the pleadings. Thus, Locke alleged that he had discharged or was in the course of discharging "the condition of expeditiously carrying out his due diligence when the defendants ceased to perform their obligation to provide materials and information requested by the Plaintiff. The Plaintiff was ready and [4] willing to deposit the sum of \$100,000 but was prevented from so doing by Patrick Lynch in an oral conversation between the Plaintiff and Lynch on or about March 25, 1999." It was pleaded that the Letter, oral negotiations and correspondence passing between the lawyers for both sides "resulted in an agreement which the defendants were bound to perform..."

[8] The agreement was particularized and alleged to have been made in writing through the Letter itself and correspondence between the lawyers; in so far as the agreement was oral, the agreement was said to have been made on March 25, 1999; in so far as the agreement could be inferred from conduct, Locke pleaded that the conduct was his expeditiously carrying out his due diligence and the defendants assisting with it. One important particular pleaded was that the defendants had expressly waived any requirement for payment of a deposit of US\$100,000 "based on the defendants' assurance that the plaintiff's offer of US\$19,000,000 was accepted by the defendants and would be honoured by them provided that the due diligence was expeditiously carried out."

[9] In addition, Locke purported to plead, quite imperfectly, a series of legal doctrines, for example, an implied term, waiver, estoppel, part performance and a collateral contract. Finally, it was alleged that on or about April 29, 1999, the respondents unlawfully repudiated the Letter and the alleged agreement "which had subsisted until then" while Locke was carrying out the due diligence exercise.

[10] As Locke saw it, all of the elements of a binding contract had been agreed except for the "date of performance" which could not be negotiated because of repudiation by the respondents. He therefore sought from the trial judge a Declaration that there was a valid and [5] subsisting agreement between himself and Bellingdon for the sale of the shares in Paradise as well as specific performance of the alleged agreement for the sale and purchase of the shares in Eastern and/or Paradise and consequential injunctions restraining the directors of the respondents from dealing with the shares.

[11] In response to Locke's allegations, Bellingdon, Eastern and Paradise in their Amended Defence pleaded the Letter of Intent in its entirety and contended that, upon its true construction, it did not constitute a binding or concluded agreement between the parties for the sale and purchase of the shares. Moreover, they alleged that, even if there was an agreement, it was not enforceable in law and that Locke had failed to comply with a fundamental term of the agreement, that is to say, to make the deposit of US\$100,000 and this deposit was a prerequisite to any further negotiations. In so far as the deposit had not been paid, these respondents claimed that they were entitled to treat the agreement as at an end for breach of a fundamental term. They denied the purported pleas of collateral contract, waiver, implied term, part performance and estoppel.

[12] Locke in his amended reply contended that, if the deposit of US\$100,000 was a fundamental term, it was waived by the conduct of the respondents who encouraged, participated in and co-operated with him in carrying out the due diligence exercise.

## The Decision of the High Court

[13] The trial judge made four (4) findings. First, he found that there was a concluded and binding agreement between Locke and Bellingdon for

the sale of the shares and the promissory note for a total purchase price of US\$19 million. Secondly, he found that Locke had repudiated that agreement by reason of his failure to pay the deposit [6] of US\$100,000 which was a fundamental term of the agreement. Bellingdon and Paradise were therefore discharged from the agreement because of Locke's repudiation. Thirdly, Payne J found that the failure to appoint an escrow agent was a matter of detail and not material to Locke's obligation to pay the US\$100,000. Finally, and not germane to this appeal as it turned out, the trial judge held that Sandals had acted as agent for Bellingdon and Paradise, two disclosed principals which had themselves acted by their human agents, Stewart and Lynch.

[14] In the result, Payne J granted the Declaration prayed for by Locke that there was a concluded and binding agreement between himself and Bellingdon but refused him the other relief sought.

#### The Appeal and the Respondents' Notice

[15] By his Notice of Appeal, Locke contends that the trial judge erred in law in holding:

- (i) that the agreement had been repudiated by Locke when he failed to pay the deposit of US\$100,000;
- (ii) that the payment of such deposit was a fundamental term of the agreement as found by the judge to exist. He also contends that the true nature of the deposit was that it was money paid to keep the property off the market "and was a good faith deposit".
- (iii) that the appointment of an escrow agent was a matter of detail.

The grounds of appeal filed against Sandals were not pursued before us.

[16] On their part, the respondents filed a Respondent's Notice alleging that the trial judge was wrong to have found a valid and subsisting [7] agreement for the sale and purchase of the shares and the promissory note constituted by the Letter of Intent. They say that if there was an agreement, it was merely an agreement to negotiate in good faith towards the signing of a stock purchase agreement and did not constitute an agreement enforceable in law.

#### The Letter of Intent

[17] The crucial document in this litigation is the Letter of Intent and it is important that we set it out fully in this judgment. Though its clauses were not numbered, we have numbered them for ease of citation. The following were the terms of the Letter of Intent:

"The purpose of this letter is to indicate the basis upon which Locke Property Company (the "Purchaser") is prepared to acquire from Bellingdon Limited, an Isle of Man company (the "Seller"), all the outstanding capital stock of Paradise Beach Ltd. (the "Company") and a promissory note of the Company payable to the Seller in the principal amount of approximately US\$11 million (the "Note"). The Company's assets consist of a 251,000 SF hotel situated on 30 acres (the "Property") located at Paradise Beach in Barbados, as identified in the attached site plan.

- (1) Purchase Price: US\$19 million payable in immediately available funds at closing, based on the assumption that the Company owns the Property free and clear of all liens and encumbrances and that there are no liabilities of the Company that will not be discharged prior to the closing at the Seller's expense, except the Note. Of the total Purchase Price, approximately \$8 million will be payable for the capital stock of the Company and approximately \$11 million will be payable for the Note.
- (2) Stock Purchase Agreement: The parties, upon execution of this letter of intent, shall immediately commence negotiations of a Stock Purchase Agreement which, when executed, shall be the agreement between the parties hereto.
- (3) Closing Date: Within 30 days after expiration of the Due Diligence Period.
- (4) Deposit: Upon acceptance of this letter, as consideration for your keeping the Company and its assets off the market as set forth on page 4 below, we will deposit with an agreed upon escrow agent, the amount of US\$100,000 as a good faith deposit, refundable to us only if you refuse to enter into a Stock Purchase Agreement or are unable to convey ownership of the Company and its assets on the terms contemplated by this letter. Upon execution of a Stock Purchase Agreement, we will deposit an additional US\$900,000 with the escrow agent. The deposit shall be held in escrow by the escrow agent in an interest-bearing account with interest credited to the Seller at closing, unless the Purchaser is entitled to a return of the deposit under the terms of this letter or under the terms of the Stock Purchase Agreement. The [8] \$1,000,000 combined deposit shall be credited against the Purchase Price, and the balance of the Purchase Price shall be paid upon closing.
- (5) Delivery of Documents: Within ten (10) days after the Seller's acceptance of this letter, the Seller shall make available to us documents in the Seller's files including but not limited to:

(Reference was then made to Exhibit "A" which was a check list of various matters comprising the Due Diligence exercise)

1. Due Diligence: Purchaser's obligation to buy the Company is contingent upon Purchaser's satisfactory review and approval of those matters set forth on Exhibit A attached hereto and made a part hereof and such other contingencies as may be contained in the Stock Purchase Agreement to be executed by the parties. Purchaser shall have 60 days from the date Seller signs this letter ("Due Diligence Period") to perform its due diligence. It is understood that Purchaser shall have reasonable access to the Property, the Company, its assets and all records and other information pertaining thereto in Seller's possession for purposes of our diligence. In the event Purchaser is not satisfied with the results of its examination in its sole and absolute discretion, the Purchaser shall be entitled to terminate this letter or the Purchase Agreement if it has been executed prior to the end of the Due Diligence Period, and the \$900,000 deposit, if it has been paid at that time, shall be returned to the Purchaser. The \$100,000 deposit shall, under such circumstances, be retained by the Seller unless the Seller has refused to enter into the Stock Purchase Agreement or the Purchaser's due diligence has revealed that the Seller is unable to convey the Company and its assets on the terms

contemplated by this letter.

2. Representation of Seller: The Seller's acceptance of the terms of this letter shall be deemed a warranty and representation by the Seller that the Seller owns the Company (and the Company owns the assets) heretofore mentioned and that the Seller has the power and authority to execute a Stock Purchase Agreement and convey 100% ownership of the Company and the Note.

3. Confidentiality: You and we agree to keep this letter of intent confidential and to maintain the confidentiality of all information disclosed to either of us in the due diligence process.

(9) This letter of intent constitutes an agreement by you and us to negotiate in good faith toward the signing of the Stock Purchase Agreement consistent with the terms of this proposal, but the obligations of the Purchaser to purchase are subject to the execution of the definitive Stock Purchase Agreement. Upon your acceptance of this proposal, you shall take the Company and its assets off the market and not solicit or accept any offers nor engage in any discussion concerning the sale of the Company other than the transaction contemplated by this letter. In return, we shall promptly commence our due diligence.

This letter shall terminate and be of no further force or effect if it has not been accepted by you and returned to us on or before 5.00 p.m. March 19, 1999.

We look forward to working with you on this matter and stand ready to immediately take action upon your acceptance of this proposal.”[9]

[18] The Issues:

I. Was there a concluded contract?

(a) The legal status of a Letter of Intent

The first and overriding issue on this appeal is whether there was a valid, binding and concluded contract between the parties for the sale and purchase of the shares and the promissory note. The determination of this issue will necessitate a consideration of (a) the law relating to Letters of Intent and (b) actual construction of the Letter of Intent itself. The respondents say that the Letter of Intent amounts to no more than an agreement to negotiate in good faith towards the signing of a stock purchase agreement and was not, itself, an agreement enforceable in law. Locke, on the other hand, says that the Letter of Intent was a full and complete document embodying all of the terms agreed.

[19] The legal effect of the common commercial practice whereby the parties to a transaction exchange Letters of Intent on which they act pending the preparation of a formal contract is still a matter very much in its evolution in parts of the Commonwealth. Some jurisdictions, notably England and Canada, have tended to treat these Letters as mere agreements to negotiate not resulting in concluded binding agreements on the premise that they are too uncertain to have any binding force. It seems to make no difference that the Letter may contain a duty “to negotiate in good faith”. Counsel in this appeal cited and discussed two decisions of high authority in England – Courtney & Fairbairn Ltd. v. Tolani Brothers (Hotels) Ltd. [1975] 1 WLR 297 (C.A.) and Walford v. Miles [1992] 2 A.C. 128 (H.L.). It must be said, however, that the latter has been much [10] criticised in academic writings and in Chitty on Contracts (28th Edition 1999) paras. 2-127 and 2-128. In Courtney & Fairbairn Ltd v. Tolani Brothers (Hotels) Ltd., the defendants, who wanted to develop a site, discussed their plans with the plaintiffs who were building contractors and in a position to obtain development financing. It was proposed that the plaintiff should introduce a development financier and be engaged to do the construction work. When the plaintiffs found such a financier they wrote to the defendants. In their letter they inquired whether, if their introduction led to an acceptable financial arrangement, the defendants would instruct their quantity surveyor “to negotiate fair and reasonable sums” for the project based on certain agreed estimates of cost and overheads and a profit margin of 5%. The defendants replied to the plaintiff agreeing “to the terms specified...” A financier for the projects was introduced by the plaintiff but the defendants engaged a different contractor from the plaintiffs to do the work.

[20] The English Court of Appeal held that there was no agreement between the parties since there had been no agreement on such a fundamental matter as the price in a building contract or the manner in which price was to be calculated. Specifically, the Court held that the law of contract does not recognize a contract to negotiate and where a fundamental matter was left to be negotiated, there was no contract.

[21] In the course of his judgment, Lord Denning MR disagreed with a dictum of Lord Wright in Hillas & Co. Ltd. v. Arcos Ltd. (1932) 147 L.T.503 at 515 where Lord Wright had said:[11]

“There is then no bargain except to negotiate, and negotiations may be fruitless and end without any contract ensuing; yet even then, in strict theory, there is a contract (if there is good consideration) to negotiate though in the event of repudiation by one party the damages may be nominal, unless a jury think that the opportunity to negotiate was of some appreciable value to the injured party.”

Lord Denning described this dictum as a “tentative opinion”. He held that “if the law does not recognize a contract to enter into a contract (when there is a fundamental term yet to be agreed) it seems to me it cannot recognize a contract to negotiate. The reason is because it is too uncertain to have any binding force.....It seems to me that a contract to negotiate, like a contract to enter into a contract, is not a contract known to the law.” Lord Diplock and Lawton LJ concurred in that statement of the law. See also Parker J in Von Hatzfeldt-Wildenburgh v. Alexander [1912] 1 Ch.284.

[22] The decision in Courtney & Fairbairn Ltd was followed in the English Court of Appeal in Mallozzi v. Carapelli S.p.A [1976] 1 Lloyd's Rep.407 where the Court overruled the first instance decision of Kerr J who had followed the dictum of Lord Wright in Hillas & Co. Ltd v. Arcos Ltd (supra). In other cases since Mallozzi v. Carapelli, courts in England have taken the position that an agreement to negotiate cannot constitute a legally enforceable contract – See, for example, Nile Co. for the Export of Agricultural Crops v. H.&J.M. Bennett (Commodities) Ltd [1986] 1 Lloyd's Rep.555; Voest Alpine Intertrading G.m.b.H. v. Chevron International Oil Co. Ltd. [1987] 2 Lloyd's Rep.547; Star Steamship Society v. Beogradska Plovidba [1988] 2 Lloyd's Rep.583.[12]

[23] Most recently, at the highest level of the House of Lords, Lord Ackner has stated the position in England. In *Walford v. Miles* (supra), defendants who were husband and wife owned a photographic business which they wished to sell. In 1986 the plaintiffs, who were brothers and one of whom was an accountant, heard that the business might be for sale at £2 million. The brothers were keen to buy the business and in March 1987 the plaintiffs agreed to buy "subject to contract". An oral agreement was made on March 18, 1987 between one of the plaintiffs and Mr. Miles that if the plaintiffs obtained a "Letter of Comfort" from their bankers indicating a willingness to provide financing of £2 million, the Miles' would terminate negotiations with any third party. The bank duly provided the "Letter of Comfort" but on March 30, 1987 solicitors for Mr. and Mrs. Miles wrote to the plaintiffs stating that the defendants had decided to sell the business to another company.

[24] The plaintiffs claimed that there was a binding preliminary contract namely, that in return for providing the Letter of Comfort, the Miles' had bound themselves to a "lock-out" agreement which would give the plaintiffs an exclusive opportunity to reach agreement with the defendant. One of the arguments for the plaintiffs was that there was an implied term in the contract that the defendants "would continue to negotiate in good faith with the plaintiffs."

[25] The House of Lords doubted that such a term could be implied and held that a duty to negotiate in good faith was meaningless.

Lord Ackner said at p.138:

"Before your Lordships it was sought to argue that the decision in *Courtney's Case* [1975] 1 WLR 297 was wrong. Although the cases in the United States did not speak with one voice your Lordships' attention was drawn to the decision of the United States' Court of [13] Appeal, Third Circuit, in *Channel Home Centers, Division of Grace Retail Corporation v. Grossman* (1986) 795 F.2d 291 as being "the clearest example" of the American cases in the appellant's favour. That case raised the issue whether an agreement to negotiate in good faith, if supported by consideration, is an enforceable contract. I do not find the decision of any assistance. While accepting that an agreement to agree is not an enforceable contract, the Court of Appeal appears to have proceeded on the basis that an agreement to negotiate in good faith is synonymous with an agreement to use best endeavours and as the latter is enforceable, so is the former. This appears to me to be an unsustainable proposition. The reason why an agreement to negotiate, like an agreement to agree, is unenforceable, is simply because it lacks the necessary certainty. The same does not apply to an agreement to use best endeavours."

[26] Mr. Mahfood Q.C. put before us some materials from Canada which support the English position. An article entitled "Letters of Intent and the Canadian Approach to Good Faith Bargaining Obligations: So Close, So Far" appears in Volume II of the *Banking and Finance Law Review* (1995-96) at pages 360-363.

[27] The author of the article, Trevor Mills, writes that:

"Canadian courts currently take an all-or-nothing approach to letters of intent: they are either a complete contract to consummate a transaction containing all essential terms, or they are not legally binding...."

The author found the approach of Canadian law to letters of intent to be virtually identical to the English approach and he noted that a contract to bargain in good faith is not recognised in those jurisdictions.

He says:

"Most letters of intent will not be enforced because they are agreements to negotiate in good faith. Canadian law views such agreements as agreements to agree and only agreements to complete a transaction are enforceable."

[28] Dr. Cheltenham Q.C. for Locke invited us to hold that the Letter of Intent was full and complete. He argued that it contained all of the essential terms, and he urged on us that "the fact that a Stock [14] Purchase Agreement was to be concluded was no bar to holding that an enforceable contract had come into existence. The essential terms and all the other things had been agreed. Negotiations on the essentials were at an end. What remained outstanding were non-essentials."

[29] He cited the American cases of *McCarthy v. Tobin* [1999] 429 Mass.84 and *Goren v. Royal Investments* [1987] 25 Mass. App. Ct.137.

[30] In *McCarthy v. Tobin*, an offer to purchase real estate described the property and the price to be paid, deposit requirements and the time and place for closing on a pre-printed form (OTP). That document required that the parties execute another document viz., a Standard Form Purchase and Sale Agreement, "which, when executed, shall be the agreement between the parties hereto". There was also a type-written insertion headed "Subject to a Purchase and Sale Agreement satisfactory to Buyer and Seller" and, finally, above the signature line was written: "NOTICE: This is a legal document that creates binding obligations..." Both vendor and purchaser signed the pre-printed form (OTP) and the issue was whether it constituted a binding contract.

[31] *Abrams J*, delivering the judgment of the Court of 7 judges held that the OTP represented a firm offer, the acceptance of which bound the parties to sell and purchase the real estate. The terms of the Notice on the pre-printed form (OTP) weighed heavily with the Court.

[32] In *Goren v. Royal Investments Inc.*, the Court was again asked to consider in what circumstances a writing, which by context or by its terms contemplated a more formal agreement, may nonetheless be [15] held to be a binding contract. In this case, vendors and purchasers of real estate both signed a document headed "Offer to Purchase" which provided for the sale and purchase at a price of \$762, 000. There were other clauses one of which provided that "A mutually acceptable Purchase and Sale Agreement shall be executed within 4 weeks of acceptance of this offer". However, before such an Agreement could be signed, the vendor received a higher offer and called off the deal with the first purchaser on a dubious excuse.

The trial judge found that the "offer to purchase" document contemplated that the parties would exercise good faith in attempting to negotiate and

draft the ultimate Purchase and Sale Agreement but the vendors did not act in good faith.

[33] On appeal, Kass J held that all significant economic issues were resolved in the preliminary agreement and the case therefore fell into that category of cases where execution of a more formal instrument was hardly more than a formality – a kind of “polished memorandum”.

The Court of Appeal, however, expressly accepted that parties are free to sign a document whose effect is not to create a binding contract. Kass J at p.142 says in rather picturesque language:

“This is not to say that parties to a preliminary agreement may not provide that they do not intend to be bound until the transaction is buttoned up by a more detailed and formal agreement. There is commercial utility in allowing persons to hug before they marry.”

[34] With great respect to Dr. Cheltenham, we are not persuaded that these cases are of great significance. On their own facts, they merely reiterate established principles of the common law. The Notice in *McCarthy v. Tobin* stated on its face that the document was a legal document creating “binding obligations”. Both parties [16] signed to it. Kass J in *Goren v. Royal Investments Inc.* held that all of the essential issues were resolved in the preliminary agreement and nothing more was required to consummate the bargain than a “polished memorandum”. Such a finding is entirely in harmony with the law in Barbados and the Commonwealth. It was basically a question of construction.

[35] Mr. Mahfood submitted that a Letter of Intent will be enforceable only if agreement has been reached on all of the essential terms and if the essential terms can be determined with a reasonable degree of certainty. But a Letter of Intent that is an agreement to agree will not be enforceable if essential terms are missing or cannot be determined with certainty.

[36] (b) Construing the Letter of Intent

Was the Letter of Intent a complete document embodying all of the essential terms of the transaction? It seems to us that it must be realized that this was a transaction about the sale of shares and not a sale of land (as was the situation with the Massachusetts cases). The Stock Purchase Agreement contemplated by a transaction of this magnitude would have involved the settlement of a large number of matters which would, themselves, have required negotiation.

[37] In such a transaction it would be usual to negotiate and then agree the representations and warranties, the indemnities, covenants, default events (and remedies therefor), existing contracts, disclosures by the vendors, resignations of directors and the appointment of new directors and the myriad of matters which agreements for the sale of shares contemplate and embody. Frankly, [17] we do not think that the execution of the Stock Purchase Agreement was a mere formality.

[38] We are bolstered in that view by the first few lines of clause (6) which made Locke’s obligation to purchase “contingent upon satisfactory review and approval” of a long list of matters comprising Exhibit “A” and “such other contingencies as may be contained in the stock purchase agreement to be executed by the parties.” (emphasis supplied)

The word “contingencies” clearly implies uncertainty, something unforeseen or a future occurrence.

[39] In Barbados, the Court of Appeal has previously had experience of a case with similar issues. *Apthorp v. Niblock* (1976) 28 W.I.R. 23 is a useful case. It was concerned with the status of an agreement for the sale of shares. The facts were these: The plaintiffs sought against the first defendant specific performance of an agreement to sell to them his shares in the second defendant company and an injunction restraining him from disposing of his shares otherwise than to the plaintiffs. The plaintiffs relied on a letter of February 12, 1975 from them to the first defendant as containing the terms of a valid binding contract for sale of the shares. The first defendant had endorsed on the letter the words “I agree to these terms” and signed his name. The first plaintiff wrote a cheque for the amount of the deposit and handed it to the first defendant. The letter contained a clause providing for subtraction from the purchase price the total of all liabilities, actual and contingent at the date of completion; a clause that the usual warranties and indemnities customary on a sale of shares will be given; a clause providing that a formal contract for [18] sale of the shares would be drawn providing for completion on April 1, 1975.

[40] The issue between the parties was whether there was a binding contract between them.

The Court of Appeal held, reversing the trial judge, that there was no concluded contract. In so far as the agreement purported to provide for the giving of warranties and indemnities by persons who were not parties to it, it envisaged further negotiation. The very nature of contingent liabilities was such as to require further investigation, negotiation and inquiries to ascertain the sum ascribable as contingent liabilities.

Douglas CJ held that the question whether or not the letter amounted to a valid and binding contract depended upon the intention disclosed by the language used by the parties. In that case, agreement on the warranties and indemnities to be given by the vendors of the company and the quantification of the contingent liabilities went to the very heart of the matter. He therefore held that the clear intention of the parties was to settle the details of the agreement reached in outline by negotiating the warranties and indemnities and by finding a formula to quantify the contingent liabilities.

[41] Dr. Cheltenham relies upon the House of Lords decision in *W.J. Rossiter v. Miller* (1878) 3 App.Cas.1124. That was a case involving the sale of land where several persons interested in the sale authorized one of their number to sell it. A prospective purchaser made inquiries as to the sale of certain lots and he was told by the agent of the sellers that he must purchase subject to the conditions stated on the plans. One of those conditions was that a [19] purchaser should execute a contract containing the conditions. The offeror then offered to purchase the lots at a price which he named. The agent promised to lay that offer before “the proprietors” and later informed the offeror that his offer had been accepted. He also informed the offeror that he had instructed his solicitors to forward the agreement for purchase and that he had taken into account the offeror’s intention to start building on the land soon. In fact, none of the conditions required a purchaser to build. The offeror wrote back indicating that he could not be bound to build at any given time or at all and that the subject had better be reconsidered. The agent replied that the sale was without condition but the offeror declined to complete the purchase.

[42] Lord Cairns LC held that upon a true construction of the documents there was a completed contract between the parties and no formal deed needed to be executed. He therefore ordered specific performance of the contract.

[43] It is our opinion that this case is of no great assistance to us. A contract for the sale of land is very different from a contract for the sale of shares in a company and, in the former, it is well settled that the essentials of the contract of sale are agreement on the parties, the price and the property (the 3 P's). Indeed, *Rossiter v. Miller* is an authority on the adequacy of the contents of a note or memorandum under the Statute of Frauds and for the view that the word "proprietors" was a sufficient description of sellers of real estate.

[44] It is a question of construction, in the light of all the surrounding circumstances, whether the parties have agreed upon all the terms of the contract, and merely desire the agreement to be expressed in more formal language; or whether the execution of a further [20] document is, as it were, a condition precedent to the creation of any contractual obligations and thus, whether the parties are still in negotiation and further terms have yet to be agreed.

[45] To be a good contract there must be a concluded bargain, and a concluded contract is one which settles everything that is necessary to be settled and leaves nothing further to be settled by negotiation between the parties.

[46] We have thoroughly reviewed the law in three jurisdictions and, in our opinion, the weight of authority and learning in England and Canada strongly suggests that an agreement to negotiate in good faith is not enforceable in those jurisdictions. And an agreement which requires further negotiation and agreement on essential matters is not enforceable in Canada, England or the United States.

[47] We also think that it is necessary to scrutinize the wording of the actual clauses in the Letter of Intent with a view to determining the presumed intention of the parties. Payne J reproduced the Letter of Intent in his decision but neglected to construe any of its clauses to determine its true nature and legal effect. Instead, he examined *Walford v. Miles* and *Apthorp v. Niblock*, and distinguished them holding that, in *Walford v. Miles*, Lord Ackner had said that the negotiations were conducted expressly under the umbrella of "subject to contract" and in *Apthorp v. Niblock*, the key issue was that the company being sold was a going concern.

[48] He concluded that "in the case before me, the company being acquired merely owns a piece of real estate the purchase of which is the ultimate goal of the Plaintiff (Locke)." The learned trial judge then said that he could not think of any warranties or indemnities [21] which could not be resolved "within the terms of the Letter of Intent, nor were any suggested."

[49] Dr. Cheltenham argues that the trial judge was right to distinguish *Walford* and *Miles* and *Apthorp* and *Niblock* as he did. As we interpret the latter case, the basic core of the decision was not the fact that the company was being sold as a going concern but the fact that the warranties and indemnities in the agreement for sale were yet to be determined by the parties. There was therefore sufficient uncertainty to lead to the conclusion that no binding agreement for the sale of shares came into being. Additionally, of course, Williams J emphasised that a true construction of the agreement suggested that it fell within the category of "subject to contract" cases.

[50] We disagree with the conclusion of the trial judge. It was vital to construe the terms of the Letter of Intent to see if such a construction gave a clue to its true nature and effect.

#### Important Clauses in the Letter of Intent

[51] We think that there are clauses which point the way to a determination of the true nature and effect of the Letter of Intent. We bear in mind that what Locke and Lynch say were their actual intentions and the evidence of their motives is irrelevant upon a construction of the agreement. And we bear in mind also the principle of construction of contracts that the meaning of a promise should depend on how it was reasonably understood by the promisee. We therefore turn now to an analysis and construction of some of the clauses in the Letter of Intent.[22]

#### 1. Clause (2)

This clause states that "The parties, upon execution of this letter of intent, shall immediately commence negotiations of a Stock Purchase Agreement which, when executed, shall be the agreement between the parties hereto."

Nothing could be more plain than that the substantive agreement between the parties was intended to be the Stock Purchase Agreement which had to be negotiated. It was not to be a formal memorandum memorializing certain business points. The terms of the Stock Purchase Agreement themselves required negotiation.

#### [52] (ii) Clause (4)

Under this clause the purchaser Locke was required to deposit "with an agreed escrow agent US\$100,000 as a good faith deposit" as consideration for the vendors keeping the company Paradise off the market. Upon execution of the Stock Purchase Agreement, he was required to pay the substantial part of the deposit i.e. US\$900,000 to the escrow agent.

In the usual way, a substantial deposit representing a percentage of the purchase price, becomes payable on execution of an agreement between the parties. Thus it seems to us that the substantial sum of \$900,000 was only to be paid when the agreement between the parties (i.e. the Stock Purchase Agreement) was ready for execution.

#### [53] (iii) Clause(6)

The purchaser's obligation to buy the company was contingent upon his satisfactory review and approval of the several matters constituting the due diligence exercise and such other contingencies as might be contained in the Stock Purchase Agreement. In other words, Locke was under

no obligation to purchase until a later stage [23] in the transaction when unforeseen matters might be revealed. The Letter of Intent does not impose any obligation upon Locke to buy upon execution of it. It postpones that obligation to the date of execution of the Stock Purchase Agreement.

[54] (iv) Clause (9)

This is a crucial clause. Under this clause, the Letter of Intent “constitutes an agreement by you and us to negotiate in good faith toward the signing of the Stock Purchase Agreement consistent with the terms of this proposal, but the obligations of the Purchaser to purchase are subject to the execution of the definitive stock purchase agreement.”

[55] In our view the language of this clause is pellucidly clear. First, the Letter of Intent is an agreement to negotiate in good faith towards another agreement. Secondly, the obligations of the purchaser to purchase are to be deferred and are made subject to the Stock Purchase Agreement.

To the extent that the Letter of Intent envisaged a further agreement but did not use the well-known phrase “subject to contract”, we have to construe this clause carefully.

[56] We must determine as a matter of construction and in the light of all circumstances whether the parties have agreed to all of the essentials of the contract and merely wish the contract to be expressed in more formal language or, alternatively, whether the execution of the further document is a condition precedent to the creation of contractual obligations.

[57] Where parties who have been in negotiation reach agreement upon terms of a contractual nature and also agree that the matter of their negotiation shall be dealt with by a formal contract, the case may [24] belong to any of three classes. In *Masters v. Cameron* (1954) 91 CLR 353, Dixon CJ in the High Court of Australia explained at p.360 that:

“It may be one in which 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. Or, secondly, it may be a case in which 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, thirdly, the case may be one in which the intention of the parties is not to make a concluded bargain at all, unless and until they execute a formal contract.”

In each of the first two cases there is a binding contract... ..Cases of the third class are fundamentally different. They are cases in which the terms of agreement are not intended to have, and therefore do not have, any binding effect of their own.”

[58] The solution of the question depends upon the intention disclosed by the language used by the parties, and no special form of words is essential to ensure that there shall be no contract binding upon the parties before the execution of their agreement in its ultimate form. No magic formula of words is necessary to suspend contractual liability although phrases such as “subject to contract” or “subject to the preparation of a formal contract” have become hallowed in usage.

[59] Such phrases postpone the incidence of liability until a formal document has been drawn up. It is not unusual, and it is certainly well recognised in contract law, that where there is documentation exchanged between parties with regard to the sale of property, those parties should be able to protect themselves by the use of suitable [25] language from being bound by the negotiations which they are pursuing.

[60] Sir George Jessel MR in *Winn v. Bull* (1877) 7 Ch.D.29 explained the legal effect and operation of such language in a well-known passage. He said:

“It comes, therefore, to this, that where you have a proposal or agreement made in writing expressed to be subject to a formal contract being prepared, it means what it says: it is subject to and dependent upon a formal contract being prepared. When it is not expressly stated to be subject to a formal contract it becomes a question of construction, whether the parties intended that the terms agreed on should merely be put into form, or whether they should be subject to a new agreement the terms of which are not expressed in detail.”

[61] Williams J held in *Apthorp v. Niblock* that the words “subject to contract” had acquired a settled meaning in negotiations. They were included in an agreement to show that the agreement was not binding. In that case, a true construction of the letter led to the conclusion that the agreement was only ‘provisional’ and not binding. The Court of Appeal held that since the agreement in *Apthorp v. Niblock* provided for a formal contract to be drawn up, on the facts of that case, it was equivalent to a “subject to contract” clause and had no binding legal effect.

[62] In the circumstances, as we construe those clauses of the Letter of Intent, we are of opinion that their insertion in the Letter of Intent has the same effect as an agreement that is made “subject to contract”. Such an agreement is rendered nugatory and is not binding upon the parties.

[63] Therefore, on the first issue on this appeal it is our judgment that the Letter of Intent did not constitute a binding and valid concluded contract between the parties because the intention of the parties as disclosed by their language is not sufficiently certain and, moreover, contractual responsibility was postponed.[26]

#### Communication of Acceptance

[64] There is a further reason why we hold that no concluded agreement existed. Clause (9) of the Letter provides:

“This Letter of Intent shall terminate and be of no further force or effect if it has not been accepted by you and returned to us on or before 5.00 p.m. March 19, 1999.”

Under that clause signature and return of the Letter of Intent were required. It was signed but never returned. It was common ground that the date of March 19, 1999 was waived or changed to accommodate the realities of the time differences between the Caribbean and Europe but there was a dispute as to whether payment of the actual deposit was also waived. One of the issues of fact was Lynch's testimony that he told Locke on March 25, 1999 that he would not return the Letter until the US\$100, 000 was paid. He claimed that he did not in fact return the Letter because Locke did not pay the primary deposit.

[65] Plainly, unless the Letter was accepted and returned in accordance with the Letter, the agreement came to an end. Lynch's evidence was to the effect that the respondents were not going to be bound unless they had a deposit and Locke was not going to get back the signed Letter unless they had a deposit "because if we didn't have a deposit, we didn't have a deal". Locke confirmed at p.183 of the Record that Lynch refused to give back the Letter.

[66] The respondents contend that, as a matter of law, there was no acceptance of Locke's offer and therefore no concluded agreement. This issue was raised on the pleadings and argued in the court below – (See p.490 et. seq.) Payne J did not deal with this issue in his decision.[27]

[67] Chitty on Contracts (28th Edition) states at paragraph 2-058:

"An offer which requires the acceptance to be expressed or communicated in a certain way can generally be accepted only in that way. Thus if the offeror asks for the acceptance to be sent to a particular place, one sent elsewhere will not bind him."

The rules governing communication of acceptance mark down that point in time when both parties become aware that each of them is now relying upon the existence of an agreement between them.

[68] In our judgment, the fact that the Letter prescribed a method of communicating acceptance, that is by signature and return, observance of that mode of communicating acceptance was essential to complete the agreement. See also *Holwell Securities Ltd. v. Hughes* [1974] 1 All.E.R. 161 per Lawton LJ who at p.166 suggests that an offeror can expressly specify that acceptance must reach him.

[69] *Eliason v. Henshaw* (1819) 4 Wheaton 225 is cited in some books as authority for the proposition that acceptance must be communicated in the manner required by the offeror. Thus, where Eliason offered to buy flour from Henshaw, requesting that an answer be sent to him at Harpers Ferry by the wagon which brought the offer and Henshaw accepted by sending a letter to Georgetown, the U.S. Supreme Court held that Eliason was entitled to refuse the purchase. Washington J at p.228 expressed the rule thus:

"It is an undeniable principle of the law of contracts, that an offer of a bargain by one person to another, imposes no obligation upon the former, until it is accepted by the latter, according to the terms in which the offer was made. Any qualification of, or departure from, those terms, invalidates the offer, unless the same be agreed to by the person who made it."

[70] The authors of Anson's Law of Contract (27th Edition) are of the view that "the same rules probably apply in English law" - (p.50). We do not accept that return of the signed Letter was waived and, on [28] the simple ground that the Letter was not returned as stipulated, we are fortified in our judgment that no binding and concluded contract came into existence.

[71] Were we a final Court of Appeal, our decision on the first issue would be enough to dispose of this appeal. However, in the event that we are wrong and higher authority finds a concluded contract, it becomes necessary that we adjudicate the second contentious issue on the appeal, that is to say, was the trial judge correct in holding that the respondents, through Lynch, were entitled to repudiate the contract because of a breach of a fundamental term of that contract by Locke? We now proceed to determine this issue *ex abundante cautela*.

## II. Was there Repudiation?

[72] Clause (4) of the Letter of Intent made provision for the payment of a total deposit of US\$1 million. That deposit was payable in two tranches. First, upon acceptance of the Letter of Intent as consideration for keeping Paradise and its assets off the market, Locke promised to deposit US\$100, 000 "as a good faith deposit" with an agreed escrow agent. Later, upon execution of the Stock Purchase Agreement, Locke promised to deposit a further sum of US\$900,000. As it turned out, Locke never paid the US\$100, 000.

The trial judge held that the deposit of US\$100, 000 was a fundamental term of the concluded agreement which he found and, in so far as Locke had refused or neglected to pay that part of the combined deposit, he had repudiated the agreement and the respondents were entitled to treat the agreement as at an end.[29]

## The Evidence

[73] Some treatment of the evidence is necessary. Locke said in his evidence that on March 23, 1999, he had a conversation with Patrick Lynch who told him that Sandals had received an offer substantially higher than the US\$19 million offered by Locke and he would have to review the matter with "Butch" Stewart.

[74] Another and very important conversation followed on March 25, 1999. Locke was in Barbados and he telephoned Lynch in Jamaica. The trial judge summarized this conversation at p.660 of the Record. We reproduce that part of the decision verbatim.

"This is the plaintiff's account of the conversation: Mr. Lynch told him that he had reviewed the matter with Mr. Stewart who agreed to honour the agreement with the plaintiff despite the higher offer from another party. Further, Stewart said that he would like to see the due diligence expedited and the 10% deposit made. Stewart was not interested in the relatively small US\$100, 000 deposit and he did not want to wait some sixty (60) days before the 10% deposit was paid. It was therefore agreed that the plaintiff would arrange for his accountant to come to Barbados the following week to expedite the due diligence and move matters expeditiously along to the payment of the 10% deposit. Meanwhile, the plaintiff need not pay the US\$100, 000 deposit otherwise required in the signing of the Letter of Intent. Mr. Phillipson, the Defendant's Attorney-

at-Law joined Mr. Lynch at some stage and confirmed that the Letter of Intent had been sent to the Isle of Man for signature.

The plaintiff said that pursuant to this oral and collateral agreement, he immediately engaged the services of Arthur Andersen, chartered accountants, attorneys-at-law in Barbados and other consultants and proceeded with the co-operation of the Defendants to expedite the due diligence at considerable expense.

Mr. Lynch's account of this telephone conversation is quite different. He said that Mr. Locke inquired about the return of the Letter of Intent signed by the vendors and he made it clear to Mr. Locke that he was required to pay the deposit, that the document would not be returned until the US\$100,000 deposit was paid, and that there was no deal without a deposit. He said that the arrangements made for the due diligence were done purely to facilitate the plaintiff."<sup>[30]</sup>

[75] Payne J did not accept Locke's evidence about the conversation which was itself pleaded as an oral agreement. He said that it seemed to him "improbable" that the parties, "especially in the light of the negotiations that led to the provision of the deposit clause in the Letter of Intent for a payment of US\$100,000, would waive the deposit during the conversation of March 25, 1999". It was the opinion of the trial judge that "that would create the unsatisfactory situation where not only would there be no deposit for two weeks, but there would meanwhile be nothing in writing as to this fundamental term."

The Telephone Conversation of March 25, 1999

[76] In our opinion the telephone conversation of March 25, 1999 went to the heart of the issue of repudiation. The terms of that conversation were disputed. So that, as we have indicated earlier, essentially the trial judge was required to make a choice as to which account of that conversation was the more probable. He saw and heard the two principal witnesses, Locke and Lynch. He preferred Lynch's account. Nothing has been demonstrated to us by Counsel for Locke that convinces us that the trial judge's preference was wrong. It was a question of fact and there was an evidential basis to support the trial judge's finding. He was entitled to make a finding that the deposit had not been waived on the evidence before him.

[77] Locke in his evidence agreed that the matter of the deposit was discussed several times and he finally agreed with Lynch a first deposit of "US\$100,000 virtually non-refundable". (p.169 of the Record).[<sup>31</sup>]

Locke's own Attorneys-at-Law, Hale and Dorr of Massachusetts, in a letter of March 8, 1999 to Sandals' Jamaican Attorney-at-Law, Mr. Ian Phillipson, pointed out that they had provided "that the first instalment of the deposit would be payable upon execution of the letter of intent as is desired by Sandals" (our emphasis).

[78] It seems to us clear that Locke well knew that the payment of US\$100,000 was an initial front-loaded part of the deposit payable on signing the Letter of Intent and not upon execution of the Stock Purchase Agreement and that, in his own words, that initial part of the deposit was "virtually non-refundable."

Lynch's evidence on this point was that Locke accepted that there should be an initial non-refundable deposit but he negotiated the amount, which was ultimately agreed at US\$100,000 (pages 339-340 of the Record).

[79] It seems to us that even if Locke was labouring under the misapprehension that payment of the initial \$100,000 had been waived by the respondents, the telephone conversation of March 25, 1999 ought to have persuaded Locke to err on the side of caution by reviewing his position on the initial deposit. The onus was on Locke to make the payment; so if he was ready willing and able to do so, the said telephone call of March 25, 1999 should have prompted him to raise with Lynch the question of identifying the escrow agent and, if the respondents did not cooperate in agreeing such agent, to take steps to anticipate and avoid any blame in that regard.

[80] Further, there was documentary evidence, albeit after Locke's failure to pay the initial deposit and when litigation was probably contemplated, which suggested that the initial deposit was an important consideration for the parties. Lynch telefaxed Locke on [32] May 14, 1999, and, inter alia, reminded him that he was "supposed to pay an earnest deposit of US\$100,000 which you have not done....At all times material I have made it abundantly clear that we will not remove the property from the market unless we obtain some agreed consideration for so doing."

[81] Lynch's position was that the due diligence exercise had cost Sandals legal and accounting fees in order to provide the information necessary to conduct the due diligence exercise. When Locke replied to that letter on July 29, 1999 he maintained for the first time that the payment of US\$100,000 had been waived by Lynch in consideration of his expediting the due diligence exercise.

Lynch insisted that payment of the initial deposit as a requirement of the agreement had not been waived.

[82] The respondents pleaded that the deposit was a fundamental term to which Locke replied that it was not and, if it was, it was waived. That was an issue joined on the pleadings which the judge was obliged to resolve. Locke's case as pleaded was that he was prevented from performing the agreement even though he was ready and willing to pay the US\$100,000.

The judge accepted Lynch's evidence as he was entitled to do. The point about waiver was argued before Payne J – (see pages 503 et seq and pages 641-656). Dealing with the case as pleaded and presented, the trial judge found no waiver.

The Law

[83] Repudiation is a drastic action which should only be held to arise in clear cases of a refusal to perform contractual obligations, where the matter goes to the root of the contract. In considering whether there has been a repudiation of a contract by one party, which is a [33] question of fact, it is necessary to examine that party's conduct as a whole and ask the question: 'does that conduct indicate an intention to refuse

performance of the contract or abandon the contract?' Clearly, the conduct of the repudiating party must be evaluated objectively. The guiding principle is that enunciated by Lord Coleridge CJ in *Freeth v. Burr* L.R.G.C.P. 208 at 213. The Lord Chief Justice said, and it is still the law:

"In cases of this sort, where the question is whether the one party is set free by the action of the other, the real matter for consideration is whether the acts or conduct of the one do or do not amount to an intimation of an intention to abandon and altogether to refuse performance of the contract."

[84] It is all a matter of construction. The court must construe the language used by the light of the contract and the circumstances of the case to see whether there was a renunciation of the contract. The entire circumstances must be looked at – Lord Selborne LC in *Mersey Steel and Iron Co Ltd v. Maylor, Benzon & Co*, 9 App.Cas.434.

[85] For conduct to be characterized as repudiatory, the breach or threatened breach must go to the root or core of the contract and it follows that a threatened or anticipatory breach will amount to repudiation if it relates to a fundamental term going to the root or core of the contract.

[86] Counsel for Locke submits that the payment of the initial deposit was not a fundamental term. It did not go to the root or core of the contract. Mr. Mahfood argues the converse proposition.

[87] In *Bunge Corporation v. Tradax S.A.* [1981]2 All.E.R. 513, Lord Scarman said at p.543:

"The first question is always, therefore, whether, on the true stipulation and the contract of which it is part, [34] it is a condition, an innominate term, or only a warranty. If the stipulation is one which on the true construction of the contract the parties have not made a condition, and breach of which may be attended by trivial, minor or grave consequences, it is innominate, and the court (or an arbitrator) will, in the event of dispute, have the task of deciding whether the breach that has arisen is such as the parties would have said, had they been asked at the time they made their contract, 'It goes without saying that, if that happens, the contract is at an end!'"

[88] In *Suisse Atlantique Societe d'Armement Maritime S.A. v. NV. Rotterdamsche Kolen Centrale* [1967] AC 361, Lord Upjohn, in luminous words, spoke of the confusion in the use of the phrases "fundamental breach" and "breach of a fundamental term". He was of opinion that they are different in nature even though they have been used interchangeably. He said at pp. 421-422:

"...there is no magic in the words "fundamental breach"; this expression is no more than a convenient shorthand expression for saying that a particular breach or breaches of contract by one party is or are such as to go to the root of the contract which entitles the other party to treat such breach or breaches as a repudiation of the whole contract. Whether such breach or breaches do constitute a fundamental breach depends on the construction of the contract and on all the facts and circumstances of the case....The innocent party may accept that breach or those breaches as a repudiation and treat the whole contract as at an end and sue for damages generally or he may at his option prefer to affirm the contract and treat it as continuing on foot in which case he can sue only for damages for breach or breaches of the particular stipulation or stipulations in the contract which has or have been broken.

But the expression "fundamental term" has a different meaning. A fundamental term of a contract is a stipulation which the parties have agreed either expressly or by necessary implication or which the general law regards as a condition which goes to the root of the contract so that any breach of that term may at once and without further reference to the facts and circumstances be regarded by the innocent party as a fundamental breach and thus is conferred on him the alternative remedies at his option that I have just mentioned." [35]

His Lordship was reiterating his discussion on this matter in *Hong Kong Fir Shipping Co. Ltd. v. Kawasaki Kisen Kaisha Ltd.* [1962] 2 Q.B. 26.

[89] The danger of giving a stipulation a label as a "condition" or "warranty" was pointed out by Lord Wilberforce in *Bunge Corporation v. Tradax* at p.541. His Lordship was at pains to explain the decision in *Hong Kong Fir*. That case concerned an obligation of seaworthiness, breaches of which had occurred during the course of a voyage. The Court of Appeal held that this obligation was not a condition the breach of which entitled the charterer to repudiate. Breaches could be various, ranging from the trivial to the grave and even to the serious but not fatal.

[90] Lord Wilberforce advised that in determining the nature of such a stipulation two questions should be asked: "first, what importance have the parties expressly ascribed to the consequence of breach? and, second, in the absence of expressed agreement, what consequence ought to be attached to it having regard to the contract as a whole?"

[91] In this appeal, in order to determine whether the deposit was a fundamental term going to the root of the contract, the starting point must surely be to assess the nature of the deposit. It seems to us that a deposit is the security for completion of the contract and a guarantee of its performance. If that is so, it would seem axiomatic that it is an essential stipulation going to the root of the contract and breach of it would entitle the innocent party to treat the contract as at an end. [36]

[92] *Goulding J in Myton Ltd. v. Schwab-Morris* [1974] 1 All.E.R. 326 examined the legal status of a deposit in a case involving the lease of land. He said:

"If payment of a deposit was not a condition precedent to the obligation to grant the lease, it was at any rate, in my judgment, a term of so radical a nature that the defendant's failure to comply with it would entitle the plaintiff company to renounce further performance. The same argument that the clause was a condition precedent, goes far to show that if it is now such a condition, then it is at any rate a fundamental term in the sense that I have indicated....It was not a mere instalment; it was to be an earnest for the ability and willingness of the defendant to complete."

Fox LJ in *Damon Cia Naviera SA v. Hapag-Lloyd International SA* [1985] 1 A.E.R. 475, expressly approved Goulding J's opinion.

Similarly, in *Millichamp v. Jones* [1983] 1 All.E.R. 267, Warner J at p.274 held that a deposit "is in general to be taken as a fundamental term of the contract, breach of which entitles the vendor, if he so elects, to treat the contract as at an end and to sue for damages....".

[93] Dr. Cheltenham submitted that upon the true construction of clause (4), the deposit of US\$100,000 was not a guarantee of performance of the agreement and could not be a fundamental term. Rather, he argued, it was the consideration for keeping the property off the market. And he goes further and says that to the extent that the due diligence exercise commenced and the respondents co-operated in that exercise, the trial judge ought to have held that it was Sandals that repudiated the agreement by not returning it. There is some attractiveness in such a construction of the first sentence of clause (4). That sum was part of the total deposit of US\$1 million, the balance of US\$900,000 being payable upon execution of the Stock [37] Purchase Agreement. Counsel therefore argues that, taken by itself, it could not be a fundamental term.

[94] The words of that first sentence of clause (4) purport to incorporate in the agreement the notion of a "lock out agreement". However, we doubt whether it can be said that the words created a "lock out agreement" properly so called. The language of the clause did not, in our view, specify a fixed period of time during which "the lock out agreement" was to subsist and, to that extent, it does not satisfy the test for such an agreement. It would flounder as an agreement for lack of certainty as to its duration.

[95] In *Walford v. Miles* (supra) Lord Ackner at p.139 "D" saw no objection in principle to a situation "whereby A, for good consideration, should not achieve an enforceable agreement whereby B, agrees for a specified period of time, not to negotiate with anyone except A in relation to the sale of his property." Later at "F", His Lordship explained the nature of this kind of agreement. He said:

"But I stress that this is a negative agreement in B by agreeing not to negotiate for this fixed period with a third party, locks himself out of such negotiations. He has in no legal sense locked himself into negotiations with A. What A has achieved is an exclusive opportunity, for a fixed period, to try and come to terms with B, an opportunity for which he has, unless he makes his agreement under seal, to give good consideration."

[96] Our construction of the first part of clause (4) relating to the payment of US\$100,000 is that that sum became payable upon acceptance of the Letter of Intent. Locke knew that Lynch had signed the Letter of Intent on April 19, 1999. In our view, once the Letter of Intent was signed by Lynch, there was an obligation upon Locke to make the initial deposit. The provision that it was to be paid "as a good faith deposit" only exemplifies, in our judgment, [38] that it was a stipulation of great importance to the parties and was of such importance that, once it had been paid, the respondents were obliged to keep the property and its assets off the market. This was an obligation sounding in honour between businessmen and, of course, was not legally enforceable, for that very reason as well as the reasons stated above. Its payment even before the due diligence exercise commenced made commercial sense because, in a transaction of this magnitude, the due diligence exercise would, in our view, necessarily have entailed a large amount of investigation of the records of the companies. And, as Lynch said in his letter of May 14, 1999, his companies would have been put to the expense of retaining lawyers and accountants.

[97] What were the consequences of failure to pay the initial deposit? Under Clause (4) of the Letter of Intent the initial deposit was refundable only if the respondents refused to enter into the Stock Purchase Agreement or were unable to convey ownership of the companies. But the Letter was silent as to the consequences of default by Locke. So, applying Lord Wilberforce's second question in *Bunge Corporation v. Tradax* (supra) we think that the parties must have contemplated the end of the deal if Locke failed to show the colour of his money. We have to apply an objective test and ask whether Locke's conduct, objectively determined, showed an intention not to perform the contract. This issue being one of fact, citation of other decided cases on other facts is hardly helpful or, indeed, necessary.

[98] Nevertheless, the appellant placed great reliance upon *Afovos Shipping Co. v. Pagnan & Pagnan* [1983] 1 WLR 195. There, the first part of clause 5 imposed upon the respondent charterers a [39] primary obligation to pay the "said hire" (which by clause 4 had been fixed at a monthly rate and pro rata for any part of a month) punctually and regularly in advance by semi-monthly instalments in the manner specified, which involved a minimum of 42 and a maximum of 54 instalments during the period of the charter. Lord Diplock held that failure to comply with the primary obligation by delay in paying one instalment was incapable in law of amounting to a "fundamental breach" of contract by the charterers. The reason for Lord Diplock's decision was that such delay in payment of one half-monthly instalment would not have the effect of depriving the owners of substantially the whole benefit which the parties intended the owners to obtain. His Lordship explained that even though failure to pay punctually was made a breach of condition it was not thereby converted into a fundamental breach and the doctrine of anticipatory breach applied only to fundamental breaches.

[99] This case does not avail the appellant Locke. Dr. Cheltenham also cited two others - *Woodar Investment Development Ltd. v. Wimpey Construction U.K. Ltd.* [1980] 1 WLR 277 and *Forsling v. Bechely Crundall* (1922) S.C.H.L. 173.

[100] In *Woodar Investment*, the plaintiffs agreed to sell 14 acres of land to the defendants. The completion date of the sale was set at 2 months after the granting of outline planning permission or February 21, 1980, whichever was earlier. The defendants were to pay a price of £850,000 and, on completion, a further £150,000 to third parties who had no legal connection to the plaintiffs. The market became unfavourable to the defendants and they sought to rescind the agreement which was a right allowed for by the agreement but in circumstances which did not exist. The defendants honestly [40] believed that they were entitled to rescind. The plaintiffs claimed that the conduct of the defendants amounted to repudiation. By a majority of 3:2 the House of Lords held that the defendants' conduct did not amount to repudiatory breach because a party who took action relying simply on the terms of the contract in question and not manifesting by his conduct an ulterior intention to abandon it was not to be treated as repudiating it.

[101] *Woodar* in fact shows the kind of good faith conduct that does not amount to repudiation. In that case there was no finding of fact as to repudiation. What the parties did was to bring an action for interpretation of the contract – see the judgment of Lord Wilberforce.

[102] In *Afovos Shipping* (supra), the court reasoned that the breach was not an actual breach going to the root of the contract. Anticipatory breach did not apply since this doctrine only applies to breach of a fundamental term. And all that Forsling decides is that where the conduct of one of the parties to a contract has been such as would lead a reasonable person to the conclusion that he does not intend to perform his part of the obligation, the other party to the contract, whatever in fact may have been the actual intention of the former, may treat such conduct as an intimation that the contract has been repudiated.

[103] We think that Locke's conduct, objectively determined, did evince an intention not to perform the contract.

## Appointment of an Escrow Agent

[104] Then, it was also argued before us that Payne J erred in holding that the appointment of an escrow agent was a matter of detail and not fundamental to the agreement. Under clause (4) of the Letter, both [41] the initial and the second deposits were to be made to "an agreed upon escrow agent". None was ever agreed. Indeed, the evidence shows that the parties never raised this matter inter se during the conversation of March 25, 1999 and it was reasonable for the trial judge to have accepted Lynch's evidence that if the appointment of an escrow agent had to be made it was a simple matter of agreeing a bank. Today's communications technology has brought about the death of distance and, clearly, if the parties had reached the stage of appointing an escrow agent, they could have telephoned, telefaxed or e-mailed each other with a nomination. In all the circumstances of this case and, having regard to our comments at para.79 on this matter, we do not believe that the appointment of an escrow agent was a matter of any great moment. We cannot accept that the agreement should have failed because the parties, in the circumstances of this case, did not get around to agreeing an escrow agent.

[105] We see no compelling reason to interfere with the trial judge's finding that, in effect, the respondents took the action to treat the contract as at an end by their acceptance of the breach committed by Locke. The respondents could not be treated as repudiating the agreement.

[106] We hold therefore that the initial deposit of US\$100,000 was a fundamental term and we agree with Payne J that its breach would have entitled the respondents to treat the agreement (such as it was) as at an end.[42]

## Appeal against Sandals

[107] On the third day of hearing, October 4, 2002, Dr. Cheltenham abandoned the appeal against the fourth respondent, Sandals. The consequence of this decision resonates in costs.

## Disposal

[108] The appeal against all four respondents is dismissed. Each of the respondents will have its costs certified fit for two Attorneys-at-Law. The Notice of the first, second and third respondents is allowed with costs on the same basis as before.

[109] We are deeply indebted to Counsel on both sides for their industry, skill and erudition in the presentation of the arguments and their generous assistance to us in wading through the sea of paper that constituted the record of appeal of more than 1100 pages. [43]

## Chief Justice

Justice of Appeal Justice of Appeal