

MARCH, 2015

## VALIDITY OF PRELIMINARY CONTRACTUAL ARRANGEMENTS

By the Italian Energy & Infrastructure  
Department

Carlo Montella  
[cmontella@orrick.com](mailto:cmontella@orrick.com)

Andrea Gentili  
[agentili@orrick.com](mailto:agentili@orrick.com)

Marcello Montesor  
[mmontesor@orrick.com](mailto:mmontesor@orrick.com)

This document constitutes an unofficial report. Consequently, nothing contained herein may serve as or be considered a legal opinion, provide the basis for or be used for the purposes of extraordinary corporate transactions, or as a reference by anyone or their legal counsels for purposes other than a general analysis of the issues examined herein.

This document may be reproduced on condition that the relevant title and date are quoted next to the following information: Orrick, Herrington & Sutcliffe (Europe) LLP, Newsletter.

The United Sections of the Italian Supreme Court (*Corte di Cassazione a Sezioni Unite*) recently issued a remarkable ruling in relation to the validity of Italian law preliminary agreements contemplating the subsequent execution of further preliminary agreements (the so called “*preliminare di preliminare*”), by decision no. 4628/2015 (the “**Decision**”).

In particular, the Decision addresses the enforceability under Italian law of a binding arrangement whereby the parties agree, subject to certain conditions precedent, to enter into a subsequent preliminary agreement, which in turn contemplates the execution of a final agreement.

This brief note is aimed at summarizing the main contents of the Decision, which we believe is also relevant for acquisition transactions (both share and asset deals), where typically a preliminary binding arrangement such as a letter of intent, a binding offer or a term sheet (collectively, the “**Preliminary Binding Arrangement**”) is executed as a first step of the acquisition process whereby the parties agree upon the key terms and conditions of the transaction and undertake to reflect them into a more detailed sale and purchase agreement (the “**SPA**”), which in turn provides for the execution of a transfer deed as the ultimate step of the transaction.

Concerns were risen on the enforceability of the undertaking to execute the SPA as provided under the Preliminary Binding Arrangement, based on the argument (expressed by certain Italian scholars and case law in respect of subjects having contractual structure and process similar to the one of M&A deals) that Italian law would not contemplate the “*undertaking to undertake*” to perform a certain obligation in the future<sup>1</sup>. By leveraging on these arguments, in a typical acquisition transaction a party to a Preliminary Binding Arrangement (more likely the vendor) could infer that – although the conditions to the execution of the SPA (e.g., positive outcome of the due diligence) have been met – it has no enforceable contractual obligation to proceed with signing on the agreed terms, thereby trying to escape liability. This means that the non-breaching party could attempt to seek restoration of the damages so incurred only by claiming “pre-contractual” liability of the other party (which is weaker remedy when compared to a full “contractual” liability).

<sup>1</sup> See, among others, decision no. 8038/2009 of the Italian Supreme Court.

By following a different approach, the Decision<sup>2</sup> clarifies that an acquisition process which contemplates the execution of two preliminary agreements and a final agreement is contractually valid and enforceable, to the extent that the parties thereto have an interest to progressively define the contents of the deal by entering into subsequent agreements which provide for increasingly specific terms and conditions. We believe that such requirement can be regarded as met in standard acquisition transactions, where typically the parties first execute a Preliminary Binding Arrangement (setting forth the general terms of the transaction), then a detailed SPA and, ultimately, a final transfer deed whereby the transaction is consummated. All such agreements have structural features distinguished from each other and are aimed at progressively define the terms and conditions of the transaction, thereby ensuring that each of them serves a different purpose in its context.

Based on the Decision's interpretation, where a Preliminary Binding Arrangement is executed and, at a later stage, one of the parties does not comply with its undertaking to execute the SPA, the non-defaulting party can fully rely on the contractual enforceability of the Preliminary Binding Arrangement and, therefore, claim compensation for breach of contract. To this end, it would certainly be advisable determining in a Preliminary Binding Arrangement the amount of liquidated damages which would become payable by the party in breach of its obligation to execute the SPA, so as to minimize the room for disputes in that respect.

In light of all the above, we believe that from investors perspective the Decision establishes a significant step forward towards certainty of full enforceability of the Preliminary Binding Arrangements, provided of course that the aforementioned required "progression" of contents and regulations is ensured when drafting the relevant transaction documents.

---

<sup>2</sup> Note that the Decision was adopted by the most important Italian court having jurisdiction over civil law matters, and therefore it constitutes a precedent which (although in principle always subject to overruling) can certainly influence subsequent case law.