When does a conversation become a contract?

Introduction

Intention to create legal relations is an essential component of contract formation. A useful reminder of the approach the courts will take when considering the issue of intention to create legal relations is provided by the judgment of the High Court in the case of MacInnes v Gross[1].

Contract formation: intention to create legal relations

The court must objectively consider the words used by and the conduct of the parties to ascertain whether they intended to create legal relations[2]:

1. Where there is an express agreement, in a commercial context, the onus of demonstrating that there was a lack of intention to create legal relations is on the party asserting it, and it is a heavy one[3].

2. Where there is no express agreement, the onus is on the party claiming a binding agreement had been made to prove there was an intention to create legal relations[4].

3. One factor relevant to the issue of contractual intention is the degree of precision with which the agreement is expressed. Vagueness/uncertainty may be a ground for concluding the parties did not reach any agreement at all[5].

MacInnes v Gross

In this High Court case, Mr MacInnes, an experienced investment banker and employee of Investec, sought €13.5m pursuant to an alleged oral contract said to have been made over dinner with Mr Gross. Gross was the 1st defendant; an Austrian national and the principle figure behind the "RunningBall" group of companies. His shares in the group were owned by a 2nd defendant (previously called HTG Ventures).

According to MacInnes, he and Gross agreed at that dinner in March 2011 that MacInnes would personally provide services to Gross and/or the 2nd defendant with the aim of maximising the return on the sale of RunningBall, and would in exchange receive remuneration which gave him 15% of the difference between the actual sale price and the "*lower of SFr 100 million or eight times 2011 EBIT*" (earnings before interest and tax) (the target price).

Following dinner, MacInnes emailed Gross and wrote about various aspects of the RunningBall business, which included advice that "*the terms proposed by Unibet/Kambi*

[1] *MacInnes v Gross [2017] EWHC 46 (QB). All further references are to this citation.*
[2] Along with the other general principles relating to contract formation as set out in the judgment of Lord Clarke in *RTS Flexible Systems Ltd v Molkerei Alois Müller GmbH & Co KG [2010] UKSC 14*
[3] *Chitty on Contracts, 32nd Edition, 2-168*
[4] *Assuranceforeningen Gard v IOPC Fund [2014] EWHC 3369 (Comm)*
[5] *Chitty on Contracts, 2-147 and 2-194*

were unattractive" and he also expressed delight that the parties were "*agreed on headline terms*". That is, he "*would be able to elect a strike price for options for 15 per cent of RunningBall at the lower of SFr 100 million or eight times 2011 EBIT*". The email made no reference to the sale of RunningBall, the actual purchase price, or proceeds of sale.

Some 9 months later, when a possible sale of Runningball to Perform Group Limited began to materialise, MacInnes emailed Gross, forwarding his earlier email and stating that he was "*conscious that [their] agreement [which] set the strike price at the lower of SFr 100m and eight times 2011 EBIT, based on the Kambi deal…had worked in [his] favour*". MacInnes thought Gross "*expected the multiple to produce a similar result to the SFr 100m but to give [MacInnes] some protection if [Runningball] did not hit the 2011 forecast*". However, MacInnes noted that the "*fair thing was that it correlated [his] potential reward directly to the value [he] delivered in persuading [Gross] against the Kambi deal*". MacInnes said he thought it was important that the parties were "*completely aligned*" going forwards. Gross replied that they needed to make a "*proper contract*".

MacInnes was increasingly side-lined in the negotiations with Perform and the judge found that he was, by April 2012, "*entirely peripheral both in respect of the sale and any continued role at RunningBall*". The basic terms of the sale were: (a) €20m cash; (b) €50m worth of shares in Perform, which could not be sold for at least 12 months; (c) deferred consideration depending on the subsequent performance of the company between €31m-€50m.

After the sale of the business, MacInnes demanded payment for €13.5m as the "*objective market value of his services*" according to the formula, relying on the alleged contract between the parties. The question for the court to determine was whether a binding contract was reached between the parties over dinner in March 2011.

The court held that although it was indeed possible for a binding contract to come into existence, for example, over dinner in a restaurant, the highly informal and relaxed setting required close scrutiny of whether there was an intention to create legal relations. It held in this case that no binding contract was made. There was:

1. No intention to create legal relations;

2. No agreement on the critical issue as to the nature of MacInnes' remuneration: "*the terms of the alleged contract were both too complex and too uncertain to be enforceable*";

3. No binding agreement as to the relevant parties or the relevant workscope.

Furthermore, the fact that the discussions took place in English, a language that was not Gross's first language, sent a further note of caution in considering whether or not a binding agreement was reached.

MacInnes' use of the words "*on headline terms*" was strongly indicative that, at least at that point in time, there was no intention to create legal relations. Rather, it suggested that matters remained to be finalised, presupposing the preparation of a formal contract. This conclusion was borne out by MacInnes' later email which demonstrated he did not himself believe that there was a binding agreement between the parties. The best that could be said was that there was a basis for a future agreement. Gross's reply showed that he did not consider an agreement to have been reached.

Other evidence to support the Hon. Mr Justice Coulson's conclusion included:

1. Neither MacInnes nor Gross said to anyone else that they had reached a final and binding agreement at dinner;

2. At no time did MacInnes ever produce a written contract or draft; and

3. The agreement was manifestly not recorded in MacInnes' own email following the dinner and the key phrase "*a strike price for options*" supports Gross's case as to the proposal under discussion. The reasonable observer would not understand MacInnes' email to provide for commission being paid by reference to the difference between proceeds of sale and a target price and indeed Gross thought the proposal related to the share options.

In light of the above, the court found that there was no intention to create legal relations and, therefore, no binding contract.

Words of warning

It is a common misconception that contracts cannot be formed through an informal conversation. However, as The Hon. Mr Justice Coulson warned: "*A contract can be made anywhere, in any circumstances*"[6]. What is essential to establishing the formation of a contract, amongst other things, is that there is an intention to create legal relations and certainty of terms. To this end, it is always advisable for parties to an agreement to seek legal advice and have a written contract drawn up to accurately reflect the parties' positions, to avoid disputes arising.

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[6] Para 81 of *MacInnes v Gross*