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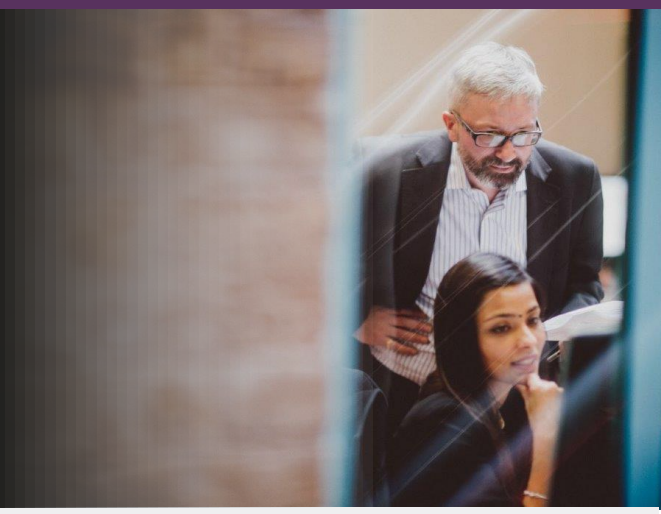
Part 1: Crossing and dotting makes for clear contracts



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Tesla founder Elon Musk is set to become the richest man in the world if he succeeds in growing the company to $650bn, after agreeing to work for no pay for ten years, in return for what's been estimated as a $55.8bn bonus if he hits target.

He must have weighed up the risk, and as he is already a very wealthy man with a fortune of some $21bn he will not go hungry while labouring away for the next decade, but one hopes he has put in place a very clear contract. It may seem surprising, but all too often such agreements are made on a so-called 'gentleman's agreement' which is challenged later, leading to battles fought in court.

In February, art dealer Simon de Pury won his action in the High Court for payment of a $10million commission over the sale of a famous painting by Gaugin - money that he claimed he was owed under a gentleman's agreement with the seller.

But when a former investment banker claimed that Mike Ashley, the chief executive of Sports Direct, had agreed to pay him a £15million bonus if the Sports Direct share price doubled within three years, a High Court judge ruled that the requirements for a binding contract had not been satisfied.

Both cases are interesting, not least because of the high stakes and colourful characters involved, with sensational details and claims of misbehaviour made in court, but also because they take us back to the fundamentals of contract law, something the judge revisited in detail when summing up in Blue v Ashley.

Jeffrey Blue was providing consultancy services to Mr Ashley and had been asked to find a new corporate broker. As a result, he, Mr Ashley and three representatives of a potential corporate broker got together on 24 January 2013, at the Horse and Groom pub.

Blue claimed that Mike Ashley had agreed on that night to pay him a bonus of £15 million if he helped to raise Sports Direct shares from £4 to £8 over a three-year period. He claimed the conversation had formed a legally enforceable contract, but the circumstances that surrounded the conversation were a significant factor in Mr Blue losing his case, as it took place during a heavy-drinking session in a pub.

The judge dismissed the claim, saying the agreement was "not a serious discussion... but was banter in which Mr Ashley was displaying his wealth and scale of ambitions", not a contract, and "that there was no one present in the Horse & Groom pub who thought that it was genuine... they all thought that it was a joke". Justice Leggatt summed up his judgement by saying that "the fact that Mr Blue has since convinced himself that the offer was a serious one, and that a legally binding agreement was made, shows only that the human capacity for wishful thinking knows few bounds".

But the 'wishful thinking' required a High Court judgement to settle the dispute, and nowadays, when we are all involved in communicating in so many ways – email, text, voicemails – and in so many different environments, including the corner coffee shop, it's worth revisiting what does constitute a binding contract.

Under English law it is possible to make a contract without any formality, simply by word of mouth, but if there is no written record the existence and terms of a contract may be harder to prove. In such a case an agreement may be unenforceable on the grounds of uncertainty. And because the value of a written contract is well-recognised, not putting things in writing in a business context may

undermine later claims, as happened in the Blue v Ashley case. Indeed, one of the requirements for a binding contract is an intention to enter into legal relations and not recording an agreement in writing might of itself suggest that there was no such intention.

In looking for evidence of what was intended and understood by the two men, the judge highlighted how unusual it was to have a claim for millions of pounds based entirely on a word of mouth agreement, with no other record existing. As he said: “In the twenty-first century the prevalence of emails, text messages and other forms of electronic communication is such that most agreements or discussions which are of legal significance, even if not embodied in writing, leave some form of electronic footprint.”

This case had no such footprint, with the only source of evidence being what was said in the pub as recalled by the different people present, and with no later conversations recorded or referred to in any written exchange. This led the judge to conclude that Mr Blue did not take the offer to be a serious one at the time, saying: "I cannot believe that if Mr Blue had thought at the time he had made a contract with Mr Ashley under which he stood to potentially receive £15m he would have regarded it as unnecessary for months afterwards to ever check that Mr Ashley recalled what had been said."

By contrast, the legal action over the gentleman’s agreement concerning the sale of the Gaugin painting between former Sotheby’s executive Ruedi Staechelin and the husband and wife team of art dealer and auctioneer Simon and Michaela de Pury, although not written into a formal contract was covered by a series of emails and other communications.

The Tahitian period painting, Nafea faa Ipoipo (When Will You Marry) was owned by Mr Staechelin, who was approached by Mr De Pury to see if he might be interested in selling the work, and Staechelin said he would not accept less than $250 million for it, net of commission. The sale took some time to go through, but was eventually made in 2014, when it was sold to the emir of Qatar, Sheikh Tamim bin Hamad al-Thani for $210 million.

But when the de Purys claimed the $10 million commission they said they were owed for helping negotiate the sale, they were sent away. Mr Staechelin’s lawyer argued that they had known the Qataris would not pay more than $210 million but had encouraged the negotiations by saying they were willing to pay $230 million, so they had breached their fiduciary duty and forfeit any right to commission, if it had ever existed. The judge did not agree, upholding the claim of a legally binding contract for commission to be paid, so there was a happy outcome for the de Pury’s, but only after three years of legal action.

So, is it the case that when it comes to a verbal contract – or gentleman’s agreement - sometimes you win, and sometimes you lose? Well no, it’s not that simple.

Each of these two cases arrived in the High Court because of their individual and complex set of circumstances. The outcomes extended well beyond a simple review of whether something was written down or not, but it is always good practice to record any verbal agreement in writing, whether millions or hundreds of pounds are involved, and ideally have it signed by all parties, if you want to be able to rely on it later.

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