부산대학교 해운통상법연구
제11권 제1호 (통권 제16호)
2020년 12월, pp. 61~74

Legal aspects of the Memorandum of Understanding(MOU)

- Focusing on M&A transaction -

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Ⅰ. Introduction

1. How will understand the Memorandum Of Understanding(MOU)?

It is explained that the Memorandum Of Understanding(MOU) is a document that creates a framework for the negotiations and agreements between two or more parties until the final conclusion of a contract.[1)] In general, the Memorandum of Understanding is not legally binding, but in Korea, the Memorandum of Understanding for Work-out companies and the M&A for

▌투고일자 : 2020년 11월 13일, 심사일자 : 2020년 12월 9일, 게재확정일자 : 2020년 12월 11일.
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1) Lyou, Byung-woon, “Legal Aspects of Memorandum of Understanding”, The Law Reasearch institute of Hongik Univ., Vol.8. No.1, 2007.

regenerating companies is often legally binding, further complicating discussions on the Memorandum of Understanding.

2. Facts: Memorandum of Understanding at Hyundai Engineering & Construction M&A

On November 16th, 2010, Creditors consisting of nine creditor banks, including Korea Exchange Bank, which has been promoting the sale of Hyundai Construction, selected the form group consortium as the preferred negotiator and signed the Memorandum of Understanding (MOU) with Hyundai Group consortium on November 29th, 2010.

The source of Hyundai Group's stock acquisition funds, which is equivalent to 1.2 trillion won in the name of Hyundai Merchant Marine's French subsidiary, has been questioned, and Korea Exchange Bank has cancelled the memorandum of understanding. Hyundai Group applied to creditors for a ban on lifting the memorandum of understanding, and Hyundai Motor Group consortium selected as a preliminary negotiator has participated in the injunction application as a subsidiary of creditors. The dispute between Hyundai Engineering and Construction creditors, Hyundai Group's consortium, and Hyundai Motor Group's consortium be went to add to the Korea economic daily.

Ⅱ. Contents of Memorandum of Understanding

1. MOUs in general M&A and workout enterprises

A memorandum of understanding for M&A transactions can be divided into a memorandum of understanding usually concluded by a workout or rehabilitation enterprises and a memorandum of understanding concluded by a general M&A.[2] At the stage of signing the Memorandum of Understanding, the transferee does not carry out the due diligence of the company at a

2) Many studies on MOUs are accumulated, but many studies do not seem to clearly categorize MOUs in two part.

satisfactory level, and the transferee tries to reserve the right to suspend negotiations at any time based on the results of the investigation. On the other hand, M&As of workout companies often conclude legally binding MOUs, which are likely to spark legal disputes.

2. Contents of non-binding memorandum of understanding

Non-binding Memorandum of Understanding usually includes M&A objectives and underwriting methods, provisional acquisition price, adjustment reasons and adjustment limits, and binding-related schedules and confidentiality of transferees.[3] If we look at the contents of the Memorandum of Understanding which is not legally binding, we can see as follows;

(1) M&A object and methods

M&A target companies and transactions are described. For example, among various M&A methods such as stock transfer, asset transfer, business transfer, merger, split, new share subscription, joint venture, etc., the transaction method planned by the parties is described.

(2) Provisional acquisition price and adjustment

It is stated that if the provisional underwriting price is stated and a fact contrary to the provisional underwriting price calculation is found (for example, if the investigation finds non-performing assets or contingent liabilities of the target company), the underwriting price may be revised downward. According to the negotiating power of the transferor, the lower limit of the acquisition price can be set and the reason for mediation can be limited.

(3) Some of the important terms and conditions

The main conditions of a transaction that has already been agreed upon between the assignor and the assignee are described, but the statements and guarantees, prior conditions, disclaimers, etc. to be included in this Agreement are generally included.

3) If only a non-legally binding memorandum of understanding is signed, two parties concerned can not obliged to this contract and may terminate the negotiations at any time.

(4) Exclusive rights of assignee

While the Memorandum of Understanding remains in force, It can stipulated that M&A discussions or negotiations with third parties other than the transferee are not permitted.

(5) Obligation of Confidentiality

It can statementd that the conclusion of Memorandum of Understanding and the progress of this Agreement negotiations should be kept confidential. Confidential information about the subject company discovered during the investigation is usually not stipulated in the Memorandum of Understanding as a separate non-disclosure agreement is usually concluded between the transferee, the assignor, and the subject company.

(6) Laws governing the MOU and Dispute Resolution Methods

define applicable laws and dispute resolution methods for interpretation of Memorandum of Understanding.

(7) the legal binding force of the Memorandum of Understanding

clearly states “non-binding force” In the MOU.

(8) Lapse and cancellation

As with the non-legally binding Memorandum of Understanding, if this Agreement is concluded or is not concluded by a certain time, the Memorandum of Understanding shall cease to be effective. On the other hand, if illegal facts or counterfeiting of bidding documents are discovered, and if a party violates the clauses of the memorandum of understanding, such as the statement guarantee clause and commitment clause, it is possible to cancel the memorandum of understanding by expressing its intention.

Ⅲ. Functions of the Memorandum of Understanding

1. Characteristics of M&A negotiations and the need to conclude MOUs

In order for a “contract” to be concluded, the parties concerned must agree on all the terms of the contract. However, M&As that buy and sell enterprises have various internal and external legal relationships as “enterprises” with independent corporate characteristics and operating activities, and the value of the enterprise fluctuates continuously and the sale price is huge. As a result, it is common for a party who has agreed to promote M&A to a target company to start negotiations with a professional lawyer on each clause in the draft contract in order to conclude a contract related to M&A.

There are many clause that require negotiation, but how to meet the preconditions for negotiation is also a problem. No one can negotiate something unknown. As the transferee of M&A transactions cannot offer the acquisition price or accept the terms and conditions of the transferee, the transferee should be able to investigate and assess the risk factors of the transferee before entering into full-scale negotiations. However, as the investigation itself puts a burden on the sales of the target company and risks leaking confidential information of the target company, there is no reason for the transferor to allow the investigation to be carried out if the target company is not seriously willing to buy the target company. Despite these conflicting interests, the potential transferee and the potential transferee are fundamentally placed in a symbiotic relationship where they work together with a common goal of promoting M&As with the target company. Concluding a Memorandum of Understanding is like making it clear to each other before the game start, and setting the rules in advance.

2. Function of Memorandum of Understanding in general M&A

The Memorandum of Understanding may be concluded autonomously to establish rules applicable to the negotiations of this Agreement by (i) giving the assignee exclusive negotiating rights, (iii) documenting the terms and conditions of the agreement and providing procedural matters for negotiations of the assignee's live-action rights. It is looking as follows.

(1) The conclusion of a memorandum of understanding requires the decision of the decision makers of both parties, so whether legally binding or not, an M&A transaction goes beyond the working-level decision-making stage to be exchanged. In other words, the conclusion of the Memorandum of Understanding raises the working-level discussion on M&A transactions to an exchange of views between decision makers, thus clearly recognizing that negotiations on contracts have begun in earnest.

(2) Even in a non-legally binding Memorandum of Understanding concluded in a general M&A, legally binding provisions (e.g., the assignee's exclusive negotiating rights, expense sharing provisions, governing law and jurisdictional provisions) shall bind the parties legally. As a result, the right to demand damages can be established.

However, non-legally binding clauses cannot be regarded as useless. Even if these provisions are not legally binding, the parties have come to recognize that claims contrary to the terms and conditions stated in the Memorandum of Understanding are unlikely to be accepted by the other party, and in the worst case, the negotiations are expected to collapse. Furthermore, making a claim contrary to the Memorandum of Understanding could negatively affect the external reputation and credibility of the parties concerned. Therefore, the parties shall refrain from making claims contrary to the Memorandum of Understanding as long as they make efforts to conclude this Agreement, and the contents of this Agreement shall be the starting point or guidelines for this Agreement negotiation. In other words, by concluding the Memorandum of Understanding, the parties should establish a basic framework and give direction to the negotiations to be carried out in the future. By making the Memorandum of Understanding non-legally binding, they should be able to leave the negotiations open at any time.

Ⅳ. Meaning of a MOU at the stage of contract signing

1. Is the memorandum of understanding an offer on the contract or not?

(1) In the case of ETRONICS M&A Co., Ltd., the Incheon District Court judged that in

principle, if the bidding entity is a sign, the indication that it is attached to the bidding is only an inducement for subscription. So, if the transferor's bid notice is the cause of the subscription, at what stage is it in the establishment of this contract to select a preferred bidder after the bid and sign a memorandum of understanding?

(2) First of all, is it possible to consider the selection of a party subject to preferential negotiations as an “offer” for this agreement? It would be hard to say so in the case of bidding for M&A. This is because the selection of the preferred bidder is only an expression of intention to give the bidder a position to negotiate this contract with priority, not to conclude this contract with the bidder.

On the other hand, in the case of a Memorandum of Understanding that is not legally binding, the terms and conditions related to this agreement are not legally binding, so it is difficult to accept the declaration of intention which is considered to be an offer or acceptance. On the other hand, when legally binding on the exclusive negotiating rights of the transferee, such contents may have been agreed upon, but this is not directly related to the contents of this Agreement.[4] Therefore, a Memorandum of Understanding, which is not legally binding, cannot be positioned within the conclusion stage of this agreement, and it can be said that it falls under a completely different contract.

In the case of legally binding Memorandum of Understanding, although this type of Memorandum of Understanding limits the content and scope of negotiations, this Agreement may still be concluded in various ways. On the other hand, the legally binding Memorandum of Understanding does not completely exclude the possibility of the suspension of negotiations on this agreement negotiations between the two parties cannot be suspended without permission. Accordingly, the legally binding Memorandum of Understanding may not be identified with this Agreement, nor may the right to request the conclusion of this Agreement be derived from such

4) A unilateral promise to sell or purchase shall become effective as a sale from the time when the other party declares his intention to complete the sale.

Memorandum of Understanding. In other words, the Memorandum of Understanding in such cases cannot be positioned within the conclusion stage of this agreement, and it must be regarded as a completely separate contract that regulates the contents and procedures of this contract.

In the case of M&A or financial contracts, the two parties exchange have revised copies of the draft contract and conclude the contract by obtaining the signature of the authorized signer after the working-level agreement on the final version. In this case, the application and acceptance necessary for the contract must be considered to exist at the last moment, that is, at the moment the signature is signed by the signer. This is because it is difficult to believe that all declarations of intention exchanged between the parties before that are "revocatable",[5] and there is no possibility of consent to this as long as there is no such declaration. Considering this point, it becomes even more obvious that no application or acceptance will be granted until this contract is finalized and concluded by the signatory in an M&A transaction.

(3) In summary, neither the selection of a preferred party for priority nor the conclusion of a memorandum of understanding can be interpreted as a coincidence of intent or a claim for the conclusion of this agreement can be derived from the announcement of the selection or memorandum of understanding.[6] Therefore, despite the selection of the preferred party or the conclusion of a memorandum of understanding, this party will remain in the "contract negotiation stage" and the "legal relationship prior to the conclusion of the contract".

2. Unfair disposal of Contract Negotiations and MOU

(1) The issue of contract negotiations regarding unfair disposal

In relation to the unfair cancellation of contract negotiations, the Supreme Court said, "If one party acted according to the trust of the other party, and refused to conclude the contract for no

5) An offer of a contract may not be withdrawn (Binding Force of Offer of Contract).

6) In other words, there is consensus among doctors on the selection of preferred negotiators and the signing of a memorandum of understanding, but there is no consensus of any doctors on the main contract.

good reason, then the other party constitutes a tort." It states that the cost of contract preparation, such as the cost of contract preparation, would not normally have been paid without such trust, would have been unavoidable even before the firm trust in the conclusion of the contract was established. The Supreme Court said, "It is unusual for one of the parties to prepare or start performing the contract since the contract has not been concluded yet". Even if the contract is implemented, it is considered to be due to the judgment and responsibility of the other party.[7)]

The precedent is that liability for damages resulting from unfair termination of contract negotiations is tort liability, and is established when the other party refuses to conclude a contract without reasonable reason despite the other party acting in accordance with the trust. The scope of such damages shall be limited to those in relation to the trustworthy interest, but such damages shall be after the time of the firm confidence in the conclusion of the contract and, under special circumstances, may include costs incurred to perform the contract. In particular, the costs paid by the bidder for the transaction before being selected as the preferred bidder are out of the scope of damages as "expenses paid before firm confidence in the conclusion of the contract." In addition, if there are costs paid to perform the obligations set forth in the Memorandum of Understanding or to take the measures specifically requested by bidders, those costs may also be included in the scope of damages.[8)]

(2) non-binding memorandum of understanding(MOU)

In the case of a Memorandum of Understanding that is not legally binding, the parties may suspend negotiations on this agreement at any time. Therefore, the size of the Memorandum of Understanding, which is not legally binding, is not considered to be the case of "granting trust in concluding a contract." In general, termination of contract negotiations does not constitute an unjust abandonment of contract negotiations. However, if the transferor violates the legally binding clause in the Memorandum of Understanding, such as proceeding with negotiations with

7) Supreme Court Decision 2001Da53959 Decided April 11, 2003.
8) Supreme Court Decision 2002Da32301 Decided May 28, 2004.

third parties, such as ignoring the exclusive negotiating rights of the transferor, consistently contrary to the principles of fidelity and integrity.

(3) Unfair termination of legally binding MOU

If a legally binding Memorandum of Understanding is concluded, it shall be construed as "granting trust" in the conclusion of this Agreement. However, the contents of such trust will be determined by the interpretation of the Memorandum of Understanding, so if the Memorandum of Understanding itself is cancelled for the prescribed reasons, such as breach of obligation, or if the conclusion of this agreement is broken without breach of the Memorandum of Understanding, liability may arise.

Ⅴ. Conclusion

In M&A transactions, a memorandum of understanding refers to the buyer (bidder) who wants to change and negotiate the terms of the acquisition, such as the acquisition price, and the seller (creditor) who wants to reserve the possibility of voluntary cancellation. The attributes contained in the memorandum of understanding are expected to diversify, depending on whether sellers or buyers dominate the M&A market, and as a result of research and efforts by M&A market participants in the future. Therefore, there will be arguments and disputes over the interpretation of the Memorandum Of Understanding(MOU).

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<Abstract>

In general, the Memorandum of Understanding is left at the disposal of the parties in the preparation stage for this Agreement and the details thereof. However, the memorandum of understanding, which is prepared and concluded in the field of M&A as a practice, has been directed to this Agreement, including certain details. In particular, the Memorandum of Understanding for M&A of workout companies and rehabilitation companies is a legally binding, independent form of contract with special provisions, including performance guarantees, and calls for theoretical review and analysis in terms of legal nature and function. This study attempted to analyze the contents, function, and nature of the general memorandum of understanding at a basic level, and many judgments and studies on the memorandum of understanding are expected to accumulate in the future.

Keywords : Memorandum of Understanding(MOU), binding Memorandum of Understanding, non-binding Memorandum of Understanding, precontract, provisional contract

<국문초록>

양해각서의 법적 성격: M&A 거래를 중심으로

장 원 석

일반적으로 양해각서는 본 계약을 위한 준비단계에서 그 체결여부와 구체적인 내용은 당사자들의 자유에 맡겨져 있다. 하지만, 관행적으로 M&A 분야의 작성·체결되는 양해각서는 일정한 내용들을 포함하면서 본 계약의 방향을 정하여 왔다. 특히 워크아웃 기업 및 회생기업의 M&A에 있어 양해각서는 법적인 구속력을 가지고, 이행보증금을 비롯한 특수한 규정들을 담아 그 자체가 독립적인 계약의 일종으로 법적 성격이나 기능 면에서 이론적인 검토와 분석의 필요를 제기하고 있다. 해당 연구는 일반적인 양해각서의 내용과 기능, 성격에 관하여 기본적인 수준에서 분석하고자 시도했으며, 양해각서에 대한 많은 판결과 연구가 앞으로 누적되기를 기대한다.

주제어 : 양해각서(MOU), 구속력 있는 양해각서, 구속력 없는 양해각서, 사전계약, 잠정계약