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3HR Legal Weekly

Commercial Property

The Importance of Heads of Terms

Heads of terms should be agreed and written down when buying, selling, granting, or taking a lease of a property.

The process of negotiating heads of terms allows the parties to a transaction to focus on what the deal is and what the obligations on the parties should be. Heads of terms are very important to resolve key issues, identify deal breakers or misunderstandings, or reveal the need for further specialist advice before the transaction gets fully underway.

Heads of terms are not meant to form a legally binding contract; they simply set out the basis on which the parties intend to enter into the deal. To ensure that the parties don't inadvertently enter into a contract, the heads of terms should expressly state that the document is "subject to contract".

Written heads of terms can also assist you and your property lawyers throughout the transaction itself to check that the legal documentation accurately reflects the deal being done and the intentions and requirements of the parties.

Before final heads of terms are agreed you should always seek input from your solicitor. This is to ensure that your legal interests are properly protected, the structure of the proposed transaction works, and that everything that should be has been covered.

Often there are fundamental points that should be agreed at the heads of terms stage, such as break clauses, alterations, alienation and repairing obligations, but these points are sometimes missed or not set out in sufficient detail in poorly drafted heads of terms.

If there are no heads of terms the parties may misinterpret the deal and their obligations at the outset and if the heads of terms are not sufficient then solicitors may end up negotiating commercial terms – wasting time and costs for both parties.

There is a risk that the commercial relations between parties can be jeopardised if issues that could have been addressed at the outset are not picked up until later. The parties will not want a transaction to be held up (with costs escalating) because important points that should have been included at the outset of a transaction have been overlooked.

Even though heads of terms are not legally binding, and as a result neither party can sue on them, they do have some moral force. A party which seeks to change its position once heads of terms have been agreed and whilst the documentation is being prepared will find itself in a weak negotiating position. It is therefore important to make sure that all your requirements are included within the final heads of terms.

To avoid the problems outlined above it is important to give due consideration to the heads of terms at the outset of any transaction, and ask your lawyer to check and advise on the draft heads of terms before they are agreed.

Richard Hull
Commercial Solicitor
E: richard.hull@3hracs.com



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The registered office of both 3HR Corporate Solicitors Ltd and 3HR Benefits Consultancy Ltd is New Broad Street House, 35 New Broad Street, London EC2M 1NH. Mainline Tel: 0207 194 8140 Web: www.3hracs.com