

# Briefing Note

## Heads of Terms (HoTs)

The HoTs is a useful document to have at the start of a transaction as it gives the parties the opportunity to discuss and agree the key terms of the transaction. The HoTs are usually not legally binding although they can contain some specifically legally binding provisions such as confidentiality and exclusivity. The types of issues which are usually agreed early on include the purchase price and how it will be paid, the asset being purchased (shares or assets), timetabling, confidentiality, exclusivity, and any matters which are specific to the transaction. This Briefing Note should be read in conjunction with our Guide to the Sale and Purchase of Shares and Assets.

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### 1. To HoT or Not

The HoTs are a useful tool to agree the main points of a transaction with the other party. However, although the main points may have been agreed there may be a considerable amount of detail which will still need to be negotiated in the transaction documents. In general there are four approaches to HoTs:

- (a) Don't have HoTs and negotiate the transaction in the documents. This will save you the cost of preparing the HoTs but can lead to disputes over the terms of the transaction when negotiating the documents.
- (b) Prepare your own HoTs. This will save you on legal fees but it may cause issue later on if a professional adviser has not seen them. Although the HoTs are not legally binding if there is a significant departure from the agreed HoTs this can lead to a breakdown in the relationship.
- (c) We prepare and negotiate the HoTs. This gives you professional advice from the start of the transaction in order to ensure that it is properly structured and the key issues are agreed. This should hopefully mean less negotiating of the documents.
- (d) We prepare and extensively negotiate the HoTs such that very limited negotiation of the documents is required. This can be used for more complex transaction with multiple parties and structured financial arrangements. Equally, if the negotiations are important (ie sale of a family business which leaves your children working under the new owners) then you may want to work through all the details of the transaction in the HoTs).

In some transactions the parties have decided not to use HoTs, while in others a considerable amount of time can be spent negotiating them in order to limit negotiation of the documents and clarify details of the proposed transaction.

### 2. What is in the HoTs?

The HoTs normally include the following provisions:

- (a) an outline of the transaction (eg. whether a purchase/sale, investment, loan terms etc.);
- (b) purchase price and how it is to be paid (eg. bullet payment versus deferred payment or earn out);
- (c) the asset being purchased (shares, assets, contracts, client lists etc.);
- (d) due diligence;
- (e) timeframe for the transaction;
- (f) the role of the seller after completion;
- (g) financial arrangements;
- (h) specific provisions relating to the transaction;
- (i) content and type of documents (eg standard warranties for a transaction of this type, shareholders agreement etc.).

### 3. Legally binding or not?

The HoTs can be completely non-binding, partially binding or fully binding. It is common for the parties to want the HoTs to generally be non-binding except for certain clauses, such as:

- (a) **Exclusivity Clauses** – these prevent either party from entering into competing negotiations for a specified period of time.
- (b) **Confidentiality Clauses** – these prevent the parties from disclosing any confidential information to others except their advisers.
- (c) **Costs Clauses** – normally both parties will want to set out that they will be responsible for their own costs in the event the transaction does not complete. However, there is the option to try and make a party responsible for the costs of the other party in the event that a party unilaterally terminates the transaction without a good reason.
- (d) **Governing Law and Jurisdiction Clauses** – these determine which country's laws apply to the Heads of Terms. This clause is particularly important as some jurisdictions may consider agreements such as HoTs automatically binding, even if this is not the intention of the parties.
- (e) **Circumstances of Termination Clauses** – these make provision for termination of the HoTs by either party should there be a decision not to proceed with negotiations.

### 4. Exclusivity and Confidentiality

#### (a) Exclusivity Agreement

Also known as a “lock-out agreement”, these are typically required from the seller by the buyer. These agreements usually require the seller to agree to not seek out or negotiate with any other potential buyers for a specified period of time. This type of agreement can be either a useful alternative to the HoTs if the transaction is relatively simple, or can be required by the buyer before even agreeing to enter into a HoTs.

#### (b) Confidentiality Agreement (or Non-Disclosure Agreement)

Part of the preliminary process involves the buyer requiring access to a significant amount of information concerning the target business (due diligence). A lot of this information is likely to be confidential in nature and so the seller will typically require the buyer to enter into a confidentiality agreement which restricts the buyer's use and ability to disclose that information to others. This is arguably a key document for the seller and should be required by them, especially if no other preliminary agreement is drawn up.

We strongly recommend that you take legal advice at the earliest opportunity and we are willing to meet and discuss issues with you at a preliminary no cost meeting to make sure that you are on the right track from the start.

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## Contact

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