LexAlia
Property + Commercial Law

HEADS OF AGREEMENT

WHAT BUSINESS OWNERS OFTEN MISS

Prepared by

Jackie Atchison, Principal Lawyer. Founder

What Business Owners Miss About Heads of Agreement

Hidden Risks in "Non-Binding" Preliminary Documents

Most business owners understand that Heads of Agreement are meant to record key terms before formal contracts are prepared. What many don't realise is how easily these "preliminary" documents can create binding legal obligations, particularly when the language doesn't match the intention.

I work with business owners navigating commercial transactions where the gap between what they thought they agreed to and what their Heads of Agreement actually says creates significant problems. Often these issues are completely avoidable with better understanding of what courts look at when determining enforceability.

This guide identifies five commonly overlooked considerations that can turn a preliminary outline into an enforceable contract - or create disputes about what you actually committed to.

OVERLOOKED CONSIDERATION 1

Assuming "Subject to Contract" Language Always Protects You

Many business owners believe that including phrases like "subject to contract" or "subject to execution of formal agreement" automatically makes a Heads of Agreement non-binding. While this language helps establish non-binding intent, it's not a complete shield against enforceability.

Courts look at the document as a whole and the parties' conduct. If you've settled all essential terms for that type of transaction, started performing obligations, or behaved as though the arrangement is finalised, "subject to contract" language may not be enough to prevent enforcement.

The problem compounds when documents contain inconsistent language - describing terms as "agreed and binding" in some clauses while including "subject to contract" elsewhere. This inconsistency creates ambiguity that courts must interpret, often leading to expensive disputes.

> The consequence:
> You believe you're still negotiating while the other party treats the arrangement as finalised. When you try to modify terms or walk away, you discover the document may be enforceable despite your intention for it to be preliminary.
>
> The reality:
> If you want non-binding status, the entire document must support this consistently. Include explicit statements like "this document is not legally binding and neither party is committed unless and until both sign formal contracts." Then ensure your conduct matches - don't start performing as though committed.

OVERLOOKED CONSIDERATION 2

Not Recognising When Essential Terms Are Actually Complete

Business owners often underestimate how complete their Heads of Agreement actually are. They think of the document as an outline, but courts ask whether it contains all terms necessary for a workable contract in that type of transaction.

For a business sale, if you've agreed on price, payment terms, what's included, timing, and major conditions, you may have a complete contract even if you intended to negotiate further. For commercial leases, rental amount, lease term, permitted use, and key responsibilities may be sufficient. The fact that you planned to add more detail in formal contracts doesn't necessarily mean essential terms aren't settled.

The gap between "we've agreed in principle" and "we've settled everything material" is smaller than many business owners realise. If the only remaining work is formal documentation rather than negotiation of substance, courts may find you've created a binding contract.

> The consequence:
> You continue negotiating details, only to discover the other side considers major terms locked in. They refuse modifications, pointing to the Heads of Agreement as a binding contract. You're forced to either accept terms you wanted to negotiate or face potential litigation.
>
> The reality:
> If material terms genuinely aren't finalised, your Heads of Agreement must identify what remains to be negotiated explicitly. Use language like "subject to agreement on outgoings calculation methodology" or "final fitout specifications to be agreed" for any points that aren't settled.

OVERLOOKED CONSIDERATION 3

Overlooking How Conduct After Signing Affects Enforceability

Even if your Heads of Agreement clearly states it's non-binding, how you behave afterward matters significantly. Courts consider subsequent conduct as evidence of what parties actually intended and whether they treated the arrangement as finalised.

If you sign a supposedly non-binding Heads of Agreement then start performing obligations, remove your business from the market, invest significant costs in the transaction, or otherwise behave as though committed, this conduct may override the non-binding language. The other party can argue that regardless of what the document said, your actions demonstrated you considered it binding.

This creates particular risk in transactions with long lead times. Months may pass between signing Heads of Agreement and formal contracts. During this period, parties often start preparing for completion - obtaining finance, planning business integration, or making commercial arrangements based on the transaction proceeding. This preparation can transform non-binding understanding into binding commitment.

> The consequence:
> Your non-binding Heads of Agreement becomes evidence of a binding contract based on how you behaved. The other party points to your actions as proof you considered yourself committed, regardless of what the document stated.
>
> The reality:
> If you want to preserve non-binding status, your conduct must match. Don't start performing obligations, maintain the right to continue negotiating or withdraw, and avoid actions that signal you consider the arrangement finalised. Document any significant steps in writing as "subject to execution of formal contract."

OVERLOOKED CONSIDERATION 4

Missing the Binding Effect of Selectively Enforceable Clauses

Many Heads of Agreement make certain clauses immediately binding while keeping commercial terms non-binding. This is common and appropriate - protecting confidential information, preventing parallel negotiations with competitors, or allocating transaction costs. However, business owners often don't fully appreciate that these selectively binding provisions create real legal obligations with real consequences.

A confidentiality clause that's binding means you can be sued for damages if you disclose commercially sensitive information shared during negotiations. An exclusivity clause that's binding prevents you from talking to other potential buyers or partners during the exclusivity period - breach this and you may face claims for damages or loss of transaction rights.

The problem arises when business owners think "the Heads of Agreement isn't binding" without recognising that parts of it very much are. They treat the entire document as preliminary and inadvertently breach binding obligations they didn't realise they'd under taken.

> The consequence:
> You breach a binding confidentiality or exclusivity obligation because you treated the entire Heads of Agreement as non-binding. The other party claims damages or terminates the transaction. You're surprised because you thought nothing was enforceable yet.
>
> The reality:
> Read carefully which clauses are binding. If the document says "Clauses 7, 8 and 9 are immediately legally binding," treat those clauses like a signed contract - because they are. Manage confidential information appropriately, respect exclusivity periods, and honour binding cost-sharing arrangements even while commercial terms remain under negotiation.

OVERLOOKED CONSIDERATION 5

Not Understanding Special Requirements for Retail Leases in NSW

Business owners negotiating retail leases often don't realise that NSW has specific legislative protections affecting when lease agreements become enforceable. Under the Retail Leases Act 1994 (NSW), a retail lease isn't binding on a tenant until the tenant has received a Lessor's Disclosure Statement in the proper form.

This means even if you sign a Heads of Agreement that appears to create a binding retail lease, it won't be enforceable against the tenant without proper disclosure. This gives retail tenants additional protection against being locked in prematurely.

However, many business owners don't understand the boundaries of this protection. It only applies to retail leases as defined in the Act - commercial office leases, industrial leases, and other commercial tenancies don't have the same safeguard. Additionally, while the lease itself may not be enforceable, other binding obligations in the Heads of Agreement (like confidentiality or exclusivity) remain enforceable.

> The consequence:
> Retail landlords assume they've locked in tenants through Heads of Agreement without providing proper disclosure. When tenants try to withdraw, landlords discover the agreement isn't enforceable. Conversely, retail tenants assume all their obligations are unenforceable without disclosure, missing that confidentiality or other selectively binding clauses may still apply.
>
> The reality:
> If you're negotiating a retail lease in NSW, understand that the Retail Leases Act creates specific disclosure requirements before lease terms become binding on tenants. Don't assume a signed Heads of Agreement locks in a retail tenant without proper disclosure. However, also don't assume that no obligations apply - selectively binding clauses may still be enforceable even if the lease terms aren't.

IMPORTANT NOTE

These overlooked considerations highlight common gaps in understanding about Heads of Agreement. Every commercial transaction involves unique circumstances and objectives. This guide helps you identify potential issues, but professional legal advice tailored to your specific situation remains essential for protecting your interests effectively.

READY TO GET YOUR HEADS OF AGREEMENT RIGHT?

You now understand the common gaps that turn preliminary documents into binding obligations or create disputes about what was actually agreed. Let's make sure your Heads of Agreement accurately reflects your intentions and avoids these overlooked issues.

I work with business owners to prepare Heads of Agreement that provide the protection they need while maintaining the flexibility they want. We'll ensure your language matches your objectives, identify which provisions should be binding, and help you avoid the common mistakes that create problems later.

Ready to discuss your commercial agreement with expert guidance? Contact Jackie Atchison at LexAlia Property & Commercial Law to explore how we can structure your Heads of Agreement to avoid these commonly missed issues.

LexAlia Property & Commercial Law | Northern Beaches, Sydney
Email: hello@lexalia.com.au | Web: lexalia.com.au
Serving NSW for property matters | Australia-wide for business law