

I know! Let's just put it in a side letter...

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## **Tempting isn't it?**

The terms of a deal have just been agreed having been thrashed out over perhaps a long period of time and right at the end of the process a vital issue or an overlooked point pops up that does not neatly fit into the agreed heads of terms or the envisaged transaction documents.

For example, it might be that:

- one party must have something and it is agreed on the basis that it is personal to that party; or
- on a subletting deal having finally agreed a level of sublease rent that both landlord and sub-tenant can live with, there comes the realisation that the terms of the headlease subletting controls will be breached because the level of rent (or other term of the sublease) does not comply strictly with those controls; or
- simply that the parties think it will be quicker and cheaper to deal with the issue via a side letter rather than a "full blown" legal document.

So the parties agree that the issue is to be documented in a side letter, which is intended to be legally binding.

## **Side letters – some myths:**

- They are quicker to negotiate, less formal than other transaction documents and perhaps the normal rules don't apply to them as they do with other transaction documents.
- They are cheaper (in terms of legal fees) to produce.
- The parties can "hide" terms of the deal in a side letter.
- They are always enforceable.



- They are never lost.
- They are always personal to the parties.
- They are confidential.

### Side letters – the reality:

- **Negotiations** – side letters are of themselves “full blown” legal documents. They require the same time, skill and care as any other transaction document and the same rules (or laws) apply to them as with any other legal document, for example the law relating to formation of binding legal contracts.
- **Cost** – side letters may run to many pages depending on the issue or issues they are drafted to cover. So a cheaper cost is not a given.
- **Hiding terms** – this doesn’t work. Please see the Homebase example below.
- **Enforceable** – yes if the correct procedures are followed, but there are traps for the unwary. Please see the examples below.
- **Never lost** – unfortunately deeds packets do go missing. Or that single page side letter that contained a crucial agreement exempting the addressee from having to comply with the terms of a particular document or clause is just not in the deeds packet. Or the PDF copy appears to be corrupted... The problem is that side letters are not usually registered anywhere so if the original is lost there may be no way to obtain a copy so as to rely on it.
- **Personal** – side letters are only guaranteed to be personal to the parties (or one or other of them) if they expressly state that. If a side letter is silent on the point then it may well bind successors in title. And here’s the rub – following on from the point immediately above, successors in title may be bound by a side letter even if they were blissfully unaware of the existence of the side letter (because for example it was never disclosed on their purchase of the property) and it then turns up. The successor may have a claim against its seller, but that’s a different story.
- **Confidentiality** – this myth is largely true on account of the fact that as said above they do not usually contain terms which would trigger any compulsory registration either at the Land Registry or elsewhere, for example Companies House.

## Case law

A few brief examples of court cases concerning side letters over the years:

*Allied Dunbar v Homebase 2001/2002* – on account of the terms contained in a side letter, the landlord could refuse consent to sublet.

A subletting deal. The tenant wanting to sublet agreed a rent and other terms with the prospective subtenant which did not comply with the subletting controls in the tenant’s headlease. So the parties decided to hide the offending terms in a side letter/agreement so that on the face of it the sublease appeared to be compliant when the application for licence to sublet was made to the landlord.

However, the landlord (and importantly) the Court of Appeal read both the headlease and the side letter/agreement together and decided that as a result the headlease subletting controls were not met. Licence was not granted.

The costs to argue the point all the way to the Court of Appeal would have been significant. And it is worth noting that an application was made by Homebase to take the argument to the House of Lords, but the House of Lords refused Homebase’s application to appeal which would indicate that they saw no merit in allowing the matter to go any further.

*Barbudev v Eurocom Cable Management Bulgaria EOOD and Others 2011* – side letter held to be



unenforceable.

Court of Appeal (again) found a side letter to be unenforceable because its wording lacked certainty and was in general too vague to be performed.

Possibly a symptom of the parties and their lawyers being too informal in their approach to the side letter? It was clear that at least one party's intention was that the letter should be legally binding.

Again the costs to argue the point all the way to the Court of Appeal would have been significant.

*Vivienne Westwood Ltd v Conduit Street Development Ltd 2017* – side letter held to be unenforceable as it amounted to a “penalty”.

On the facts of this case the side letter terms were draconian in their application, which involved payment of money triggered by specific events.

## Conclusion

Side letters do have a place in real estate transactions, are commonly used for personal arrangements and can be useful.

Common uses are, for example, relaxing rent payment provisions in leases from quarterly to monthly payments and such like.

However, they need to be approached and used correctly and they are not necessarily a quick fix solution. If it is possible to cover off the issue in the main transaction documents then that may be a better solution.

## How we can help

If you would like further advice or information on this topic, then we can help. [Get in touch](#) or contact our [real estate team](#)



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