Options and Conditional Contracts

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Land can be controlled by developers without it being purchased outright. The purchase can be conditional on a particular event-usually a planning consent. Or the purchase can be at the option of the developer. With an option The developer can decide to purchase or walk away from the purchase after a particular event. Again, this is usually a planning consent being obtained.

The difference between these two contract types relates- at first glance- to control. With a conditional contract once the condition is met then, in theory, the contract becomes binding and proceeds. It seems to favour the landowner in giving certainty. However, in practice, the trigger event may be defined so closely that the developer has more control than it first may be assumed. Typically, a planning consent must be satisfactory. What that means can sometimes be what the developer wants only!

The option is more of an honest contract arrangement in that it is quite clear that it is at the option or choice of the developer whether the purchase contract becomes binding or not. Often an option can run for an agreed length of time of up to 21 years. Options can be registered as a land charge at the Land Registry so that the Title of the land will show that another party-the developer-has an interest in the property.

Both conditional contracts and options can have initial deposit monies payable at their commencement. Sometimes these are non-returnable in the event that matters do not proceed. Also, they are sometimes deductible from the eventual purchase price.

Typically, Conditional contracts have a timescale of some 18 months or 2 years as a maximum. This is because most often a conditional contract will have a fixed price attached to it. So, the idea is that a price is agreed between the parties and once an event has been triggered-usually the achievement of a planning permission-this agreed price becomes payable and the land asset is transferred between the parties.

Options are an entirely different and usually more complicated arrangement. As the option often runs for some years it is unlikely the parties will be content to enter into a fixed price. This then gives rise to a valuation formula to determine the price payable. Typically, this refers to an agreed percentage of open market value being payable. Unfortunately, this can become a very complicated area where definitions are required to fix what is being valued and on what specific assumptions. It is akin to rent review provisions in the relation between valuation and legal terms. Deductions that apply also need to be defined. It is not unusual for this valuation process to run to many pages of close "legalese". It is a mine-field for the unwary! Landowners sometimes try to protect their position by inserting a minimum price payable in the documentation. In practice, if values are at or below this level the developer will seek to re-negotiate anyway. The developer can always delay the trigger event in the option for considerable amounts of time- if not indefinitely. The minimum price can then be an illusion of safety for the landowner who may not be prepared to wait!

If the parties to an option are unable to agree what the price payable determined by the formula should be there will be provisions for dispute resolution. This is by reference to independent valuation or arbitration. Sometimes to encourage the parties to agree before this extra stage is reached there can be interesting pendulum formulations where in the event of the dispute being resolved closer to one or other parties' original contention the price payable shifts to that original figure. The idea behind this is to get the parties to be realistic about their figures in the first place.