Nothin' goin' on but the rent

Commercial rent arrears recovery: John Sharples asks are you ready?

IN BRIEF

- The long-awaited Commercial Rent Arrears Recovery scheme comes into force on 6 April 2014.
- It abolishes the existing law of distress and regulates when and how a landlord who is owed rent can seize and, if necessary, sell his tenant's goods.
- Landlords, tenants, managing agents and their legal representatives must all familiarise themselves with the new rules.

Commercial rent arrears recovery (CRAR) has had a long gestation. The outline of the scheme is set out in Pt 3 and Sch 12 of the Tribunals, Courts and Enforcement Act 2007 (TCEA 2007). Its implementation however was delayed to allow consultation with interested groups. This has now happened and the result is the Taking Control of Goods Regulations 2013 (SI 2013/1894) (TCGR 2013). They bring CRAR into effect and set out the procedure that landlords must follow.

Modernisation

CRAR is meant to modernise and codify a difficult and ancient body of law. Distress, although quick and cheap, was thought to give landlords an unfair advantage over non-secured creditors and cause potentially unnecessary disruption to tenants' businesses. It was however (and partly for that reason) relatively effective.

CRAR introduces more checks and balances, but as a result will be a slower and more costly process. More seriously the need to serve advance notice, which gives tenants time to remove goods before they are seized, limits its effectiveness and will discourage its use. As a result landlords are likely to look for other ways of securing payment from the outset, for example through the increased use of guarantees, rent deposits and performance bonds.

What follows sets out the broad outline of the new scheme, points out where it differs from the current law and comments on areas of likely difficulty.

Implementation

CRAR abolishes the common law right to distrain as from 6 April 2014, although the old rules will continue to apply where the distress process has already been started before then. The new rules apply to both new and existing tenancies. Since they are less favourable to landlords, those currently owed arrears should consider taking action before 6 April.

> *"The search for fairness has resulted in a scheme that many landlords will be reluctant to use"*

Predictably CRAR contains anti-avoidance provisions: a tenant cannot agree to limit the protection it confers, but a landlord can bargain away his CRAR rights.

Types of tenancies

CRAR only applies to tenancies, including:

- tenancies at will but not tenancies at sufferance; and
- tenancies which are, or are "evidenced", in writing.

The requirement for writing is presumably to limit the scope for dispute about what is due and whether CRAR applies. However the Act and Regulations do not say what amounts to "evidence": eg is it enough to prove some agreement exists or must it also set out the parties/premises/terms/rent? Must it come from the parties/their agents? There is no need for it to be signed, in contrast to other similar provisions (eg the Statute of Frauds 1677, s 4; the Law of Property Act 1925, s 40).

Types of premises

As its name suggests, CRAR only applies to leases of "commercial premises". This includes agricultural holdings, although CRAR cannot be used to recover rent under such tenancies which is more than a year in arrears. Whereas distress can be used against some types of residential tenants, CRAR cannot be used for premises that are let—in whole or part—as a dwelling or used as such unless that it is a breach of the lease or headlease terms. Mixed-use premises (eg the traditional corner shop with flat above) are therefore excluded. Such landlords should consider separate leases of the residential and non-residential parts, so that CRAR can be used to recover the latter rent.

Recoverable sums

CRAR can only be used to recover arrears of "rent" properly so called, ie what is "payable…for possession and use of the [land]" including any interest and VAT. Unlike distress, it cannot be used to recover other sums (eg service charges, insurance premiums) which are merely reserved as rent. Inclusive rents must be apportioned since CRAR can only be used to recover what is "reasonably attributable to possession and use" of the land. As this is likely to be a future source of dispute, landlords should avoid using such rents in future or at least set out in the lease how it was apportioned between its various components.

Excluding other charges from CRAR is a cause for concern. A debt claim by itself is rarely effective in securing payment and forfeiture is unattractive in the current economic climate. For new leases, landlords may well look to secure a higher "basic" rent and then not charge separately for services. As well, tenants are likely to prioritise paying rent above other charges and landlords who are owed different debts should consider appropriating general payments to non-rent sums.

Minimum amount

A landlord can currently distrain for any amount due, but CRAR can only be used if the equivalent of at least seven days rent, excluding interest or VAT, is due both when notice of enforcement is given (below) and when the goods are seized. A canny tenant who receives notice may try to avoid CRAR by paying down the arrears to just below that level before it expires.

The minimum rent is calculated net of any right of set-off and—in relation to agricultural holdings—any compensation due by custom, agreement or statute. However, well drawn leases already exclude such rights and those terms are not thought to fall foul of the anti-avoidance rules.

Need for notice

Controversially, landlords must in future give tenants at least seven clear days notice of intention to seize goods. At present they can distrain without warning. The regulations specify the form and contents of the notice and how/by whom it must be served.

The need for notice has caused landlords particular concern. Some tenants will have nowhere else to move their goods to and/or will continue to trade from the premises. But others who are close to insolvency, closing down or devious will be tempted to remove goods before they can be seized. The Act tries to provide for that by allowing a landlord to apply to be allowed to give shorter notice where it is "likely" the goods will be removed or disposed of in order to avoid being seized. However that is an imperfect remedy since the risk may often be difficult to prove and the cost of applying high, relative to the value of the debt.

A tenant who is served notice and starts to remove goods can be prevented from doing so by freezing order, but only if there is a risk of dissipation. There is nothing in the regulations that prevent routine stock movements or moving goods to another location merely to avoid CRAR.

To prevent landlords improperly using CRAR, the rules allow courts to set aside a notice or prevent further action under it, but the grounds for doing so are not set out in the regulations, as contemplated. Clearly it will do so if the debt is not due/too low, but what if that is disputed? Must it be proved on a balance of probabilities? Or is the power akin to the one to set aside a statutory demand for a debt that is disputed on substantial grounds? Or an interim injunction, in which case are the *American Cyanamid (American Cyanamid Co v Ethicon Ltd* [1975] AC 396, [1975] 1 All ER 504) principles (and therefore the tenant's solvency) relevant? Are there other grounds for setting aside notices? And can sufficient court time be found before the enforcement process is complete?

Seizure

In yet another change, only the tenant's own goods can be seized whereas now a third party's goods can sometimes be distrained against. Some types of goods are excluded and they broadly correspond to the current exemptions, viz items required for the tenant's business, trade, profession etc, up to an aggregate value of £1350 or for personal domestic. Only goods up to the value of the debt plus enforcement costs may be seized.

In a further change, landlords can no longer act in person. They must now use "enforcement agents" under s 63(2) who must be authorised in writing. The agents' fees, which can be recovered out of the proceeds of sale, are set by the Taking Control of Goods (Fees) Regulations 2014 (SI 2014/1).

Goods are seized by securing them on the premises, removing and securing them elsewhere or entering into a "controlled goods agreement" (akin to taking walking possession). The Taking Control of Goods Regulations 2013 prescribe the form of agreement, how goods may be secured, and when and how entry can be made. They allow the agent to use reasonable force and for warrants to be issued in aid of the seizure process.

Post-seizure duties

On entering the agent must give the tenant written notice of what he is doing. Afterwards he must send the tenant an inventory and have the goods valued. The rules also set out his duties in relation to their care.

Sale

The goods must be sold (i) at public auction unless the court orders otherwise and (ii) for the best price reasonably obtainable. They cannot be sold until seven days have passed and the tenant has had seven clear days' notice of sale. The goods must be returned if at any time during the process the tenant pays the debt plus costs. If they are sold, he is entitled to any surplus.

Notice to subtenants

Although CRAR abolishes the law of distress, a landlord of commercial premises will still be able to serve notice on a subtenant requiring it to pay the sub-rent to him direct until the tenant's rent arrears are paid. The notice takes effect 14 days after service, lessening the risk of the subtenant inadvertently paying the wrong person.

Conclusion

The search for fairness has resulted in a scheme that many landlords will be reluctant to use. The irony is that these changes may well result in them demanding higher rents to cover the risk of non-recovery and/or up-front security, which some tenants will struggle to provide. **NLJ**

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