

WHAT TO DO WHEN YOUR CORPORATE TENANT GOES BUST – A FEW PRACTICAL TIPS

This note sets out a brief guide to landlords when they receive notice of tenants' formal insolvency. This does not address the pro-active steps which should be taken when a tenant first shows signs of financial deterioration (on which see our briefings [Property Insolvency: A Practical Introduction](#) and [Insolvency: Key Issues for Business People](#)) or the more creative uses of insolvency procedures for rescues (on which see [Rescue and the Entrepreneurial Business](#)).

WHAT IS THE PROCEDURE?

It is imperative to analyse whether the tenant is subject to administration, compulsory liquidation, voluntary liquidation, receivership, voluntary arrangement or some other procedure. Each have different implications for the landlord. Insolvency procedures for individuals are not addressed in this note.

ADMINISTRATION

This procedure creates a breathing space for implementation of business rescue (perhaps sale of the business as a going concern, orderly realisation of assets or negotiation of a voluntary arrangement).

- **Pre-appointment arrears:** Administration (or even certain steps towards it) creates a broad moratorium preventing commencement or continuation of forfeiture, distress/commercial rent arrears recovery, winding up petitions and litigation without consent of the court or administrator. If, however, a distress/commercial rent arrears recovery walking possession has been started before administration this may create some leverage.
- **Ongoing rent:** The administrator will often agree to pay rent going forward as an expense of the administration (that is in priority to ordinary debts) while he is using the premises for the purpose of the administration (e.g. trading a business with a view to sale) and this should be requested. Landlords may, however, be asked to waive this entitlement to help achieve a sale of the business to an ongoing tenant.

When the administrator ceases to use the premises he will generally treat ongoing rent as an ordinary unsecured liability which would give the landlord a right to a dividend alongside other creditors if sufficient funds are available.

- **Rent deposits:** The administration moratorium will generally prohibit the enforcement of a rent deposit without consent of the court or the administrator but the administrator is likely to agree to this step being taken as he will generally be unable to use the deposit and it will reduce the tenant's liabilities.
- **Sub-tenants/guarantors/original tenants:** Rights to recover rent under sub-leases or to enforce obligations against guarantors are not affected by the tenants administration. Administration will also not prevent available action against an original tenant.
- **Speak to the administrator to find out his plans:** Often the administration strategy would be to sell the business as a going concern. Early dialogue with a prospective tenant may assist with this process and help the landlord agree optimal terms. Commonly the business is sold very quickly without landlord's consent, leaving a new tenant in occupation in breach of the lease. Thought should be given to accepting rent from the new owners as this may create difficulties in enforcing the lease covenants or objecting to assignment later. Administration is also often used to create a breathing space for negotiation of a voluntary arrangement (see below).

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VOLUNTARY ARRANGEMENT

This is essentially a deal struck between the debtor and its creditors which binds everyone if the requisite majority of creditors (75% by value) and members (50%) is obtained. This may, therefore, cause a compromise of debts which has not been approved by all landlords or other creditors.

- **Read the proposal:** It is important to assess at an early stage what the impact of the proposal would be for the landlord. Typically, the proposal would treat outstanding arrears alongside unsecured creditors and offer a compromise while paying ongoing rent. Proposals, however, will sometimes attempt to compromise future rent or limit rights against guarantors. It is important that any objections are voiced early so that an attempt can be made to improve the position in the arrangement itself and, if approved by the requisite majority of creditors and members against the landlord's wishes, that a court challenge can be made in the very tight timescale of 28 days permitted.
- **Pre-appointment arrears:** These are often compromised by the arrangement. If so, once the arrangement is approved, rights to forfeit, exercise distress/commercial rent arrears recovery, litigate or issue a winding up petition for arrears will be waived.
- **Ongoing rent:** As discussed above, this will not generally be compromised by the voluntary arrangement but this may be proposed and the proposal should be checked.
- **Rent deposits:** These are not generally affected for ongoing rent but check the terms of proposal.
- **Sub-tenants/guarantors/original tenants:** Rights against these parties are not generally affected by the voluntary arrangement but attempts have been made to limit rights against guarantors in some proposals.
- **Moratorium:** For voluntary arrangements small companies, a moratorium similar to that given during an administration period may be granted by the court while the voluntary arrangement is negotiated. During this time, as in administration, rights to forfeit, exercise distress/commercial rent arrears recovery, litigate or issue winding up petitions are restricted without leave of the court.

COMPULSORY LIQUIDATION

This is a liquidation following a winding up petition to the court.

- **Choice of liquidator:** The official receiver (a government department) will generally be appointed as liquidator. If a proactive liquidator is required (perhaps to investigate and/or pursue directors for misconduct) and resources are available (in the company or from external sources are sufficient) it may be possible to have a liquidator in private practice appointed by representation to the Official Receiver or, if necessary, by convening a creditors' meeting.
- **Pre-appointment arrears:** Litigation against the company can be restrained at any time after the issue of the winding up petition (even before a court order is made). The continuation of distress/commercial rent arrears recovery is void, and if effected within the three months before the winding up order, proceeds are charged for the benefit of preferential debts of the company (effectively some arrears to employees). While forfeiture through a court application is prohibited without leave of the court, peaceable re-entry is still permitted.
- **Ongoing rent:** While property is used for the purposes of the liquidation, ongoing rent will generally be paid as an expense of the liquidation (that is in priority to ordinary debts). However, after ceasing to use the property, ongoing rent will be treated as an ordinary unsecured liability.
- **Rent deposits:** The landlord's rights to enforce a rent deposit should not be affected.
- **Sub-tenants/guarantors/original tenants:** Rights should not be affected.
- **Disclaimer:** The liquidator may disclaim the tenant's interest in the lease by notice on the landlord and other interested parties. This will bring the tenant's interest in the lease to an end but will not prevent action against any guarantor, sub-tenant or original tenants and will entitle the landlord to claim for damages. Disclaimer can be provoked by notice on the liquidator which requires him to decide whether to disclaim within 28 days. This can be useful where the liquidator refuses to surrender a lease which the landlord wishes to end.

VOLUNTARY LIQUIDATION

This is a liquidation started by resolution of the company's members:

- **Choice of liquidator:** The liquidator will, generally, be chosen by a vote of creditors (by value) in a creditors' meeting. Standards vary and some liquidators may be close to directors. Landlords should, therefore, make use of this vote to secure the appointment of the best alternative.
- **Rent arrears:** The tenant can be sued for arrears, and the landlord can distrain/exercise rights of commercial rent arrears recovery, or forfeit through court application unless restrained by the court. Peaceable re-entry is also permitted.
- **Ongoing rent:** As for compulsory liquidation.
- **Rent deposits:** As for compulsory liquidation.
- **Action against guarantors/sub-tenant/original tenant:** As for compulsory liquidation.
- **Disclaimer:** As for compulsory liquidation.

RECEIVERSHIP

This is a remedy by a bank or other secured creditor. It does not generally affect the rights of a landlord or other creditor. If, however, the tenant is insolvent, ordinary unsecured claims will only entitle the landlord/creditor to share in minimal assets available after secured and preferential creditors are paid.

- **Arrears of rent:** Receivership will not generally restrict the right of the landlord to exercise any remedies which they have to collect arrears (litigation, winding up petitions, forfeiture, distress/commercial rent arrears recovery). Litigation will, however, only be of use to the extent that the company has assets to satisfy unsecured debts.
- **Ongoing rent:** The receiver will often agree to pay rent as an expense of the receivership to the extent that he occupies the property for the purposes of the receivership. Otherwise ongoing rent will be treated as an ordinary unsecured debt to be paid alongside other creditors.
- **Petition for liquidation:** Where the company has insufficient funds to pay an unsecured debt, the creditor may wish to petition for liquidation. This may concern the liquidator by exposing him to greater risk of personal liability for ongoing trading debts (and create some leverage to get a debt paid).
- **Rent deposits:** Rights of the landlord should be unaffected.
- **Rights against guarantors/sub-tenants/original tenants:** Should be unaffected by the receivership.

Jeremy Whiteson heads our Insolvency Team. After qualification at CMS Cameron McKenna, Jeremy worked as a dedicated insolvency specialist and was involved in many of the largest insolvencies of the recession in the early 1990s. Since then he has remained involved with insolvency practice, has published numerous articles on insolvency topics and is author of the Creditors' Meetings chapter of Tolley's Insolvency Law. He now focuses on insolvency for the property sector and entrepreneurial businesses.

This article offers general guidance only. It reflects the law as at October 2008. The circumstances of each case vary and this note should not be relied upon in place of specific legal advice.

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