

FORSTERS REAL ESTATE LITIGATION UPDATE

COMMERCIAL RENT ARREARS RECOVERY

ARE YOU READY FOR CRAR?

From 6 April 2014, the ancient remedy of distress will be abolished. This enabled landlords to instruct bailiffs to enter let premises without notice to seize and sell goods to the value of any rent arrears. The new regime, introduced by the Tribunals Courts and Enforcement Act 2007 ("TCEA 2007"), is known as CRAR (Commercial Rent Arrears Recovery) and, although there are some similarities with distress in that goods can still be seized, there are significant changes which make it a far more restrictive process for landlords. If CRAR does not apply, no distress is possible at all.

THE KEY CHANGES

- CRAR is only available to landlords of written leases of commercial premises. It would not be available, for example, where there is an implied tenancy at will.
- It cannot be used where the premises are let or occupied as a dwelling (unless the residential occupation is in breach of the lease or a superior lease).
- CRAR is not available for mixed use premises (i.e. it cannot be exercised in respect of the commercial element of a mixed use property).
- The procedure can only be used to recover rent, VAT or interest. It cannot be used to recover other sums, even if they are reserved as rent and it is not possible to draft a lease so that such sums will be recoverable.
- In order to exercise CRAR, there must be an amount equal to or in excess of 7 days' rent outstanding less interest, VAT and any permitted set off the tenant could claim ('the net unpaid rent'). This sum has to have fallen due and be outstanding when notice of enforcement is given and at the time the goods are taken control of.
- Tenants must be given 7 clear days' notice in a prescribed form before CRAR can be exercised ('the enforcement notice'). If the enforcement notice is not in the prescribed form, it will be invalid. Note also that it can only be served by the enforcement agent (see below) not by the landlord or its' managing agents or solicitors.
- The Court can authorise a shorter notice period if satisfied that goods are likely to be moved by the tenant to avoid CRAR but, depending on the level of debt, this is an unattractive additional cost and administrative hurdle.
- Only certified enforcement agents (formerly bailiffs) can exercise CRAR.
- The tenant must also be given 7 clear days' notice of the proposed sale of the goods (although a shorter notice period is permissible for perishable goods). Furthermore, in most cases, the sale can only take place by way of public auction.
- It may be possible to exercise CRAR within 6 months of expiry of the lease provided certain conditions are satisfied.

THE IMPACT OF THE CHANGES

Aside from the fact that it will be a slower process, the main concern is that as the element of surprise is lost as, once they receive the obligatory prior notice, tenants have the opportunity to move goods, or goods of significant value, off site to avoid seizure. As CRAR only relates to the principal rent, struggling tenants are likely to prioritise these payments with knowledge that there is no risk of CRAR being used to recover service charge, insurance or similar charges. Also, the requirement that 7 days' rent is outstanding both at the time of enforcement and at the time goods are seized means that tenants may pay the minimum amount necessary to bring the debt just under the required threshold to avoid seizure of goods. Overall, although it may still be an effective remedy for single site tenants who cannot relocate goods to alternative sites, there is no doubt that landlords have lost a highly effective and quick method of debt recovery. Reliance will often have to be placed on Court proceedings which will be more costly and far slower.

ABILITY TO RECOVER ARREARS FROM SUB TENANTS

Pursuant to the TCEA 2007, superior landlords retain the right to serve notice on sub-tenants (being any tenant below the immediate tenant of the premises comprised in the head lease) requiring them to pay the sub-rent directly to them. This is now known as a 'Section 81 notice', replacing the former Section 6 of the Law of Distress Amendment Act 1908 procedure.

Provided the superior landlord would be able to exercise CRAR against its immediate tenant (i.e. the pre-conditions in relation to the amount and type of rent must be satisfied), then notice can be served on a sub-tenant in relation to the net unpaid rent. If the sum is unpaid then the superior landlord can exercise CRAR against the sub-tenant. However, the Section 81 notice only takes effect 14 clear days after service on

the sub-tenant. If the sub-tenant has already paid rent to the intermediate tenant, there will be no obligation to also pay the superior landlord. It will be important, therefore, to consider the timing of service of the Section 81 notice.

If the sub-tenant makes a payment under such notice, save in certain circumstances, he can deduct that amount from the rent that he would otherwise pay to his immediate landlord (and if there is a chain of underleases, this deduction is passed up the chain).

SHOULD I TAKE ACTION BEFORE 6 APRIL 2014?

Where appropriate (e.g. if there is no concern about waiving the right to forfeit), so as to avoid the restrictions of CRAR, landlords should give urgent consideration as to whether to use distress as a remedy to recover rent arrears before 5 April 2014. Do note that goods have to have been distrained against by this deadline. It is not sufficient to have merely instructed the bailiff.

IMPLICATIONS FOR THE FUTURE

- The costs of collecting rent arrears are likely to rise.
- There will be an increase in alternative methods of debt recovery, most probably statutory demands (where the debt must be at least £750 and be of a certain amount which means it is not really suitable for service charge arrears) but, depending on the amount of the arrears, also court proceedings. However, there may also be options to pursue former tenants or guarantors and also, whilst potentially draconian and not without its risks, to forfeit the lease.
- Landlords may opt to use forfeiture to threaten to evict tenants and force them to pay. But see below.
- There is likely to be a greater emphasis on the need for rent deposits (which allow for recovery of sums other than principal rent) or other security on the grant of new leases.
- Mixed use premises may be split by granting separate residential and commercial leases so as to retain the right to exercise CRAR in respect of the commercial element.
- This is likely to be just the first step in limiting landlord's powers. The Law Commission is now looking at abolishing forfeiture by peaceable re-entry so that proceedings will also be needed to terminate leases where the tenant is in default.



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This article offers general guidance only. It reflects the law as at April 2014. The circumstances of each case vary and this article should not be relied upon in place of specific legal advice.