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Post Pandemic Commercial Lease Issues

CORONAVIRUS AND RENT ARREARS

As a consequence of S.82 of the **Coronavirus Act 2020**, forfeiture of non-payment of rent in commercial leases has now been suspended until 25 March 2022 in both England and Wales.
It might be suspected that the biggest problem in relation to forfeiture for non-payment of rent when it becomes available, or for other breaches, might be the difficulty in finding the new tenant, especially at the same rent, in the current climate. In addition, there are major issues in relation to business rates liability
Since 1 March 2020, Commercial Rent Arrears Recovery was only available if there were 90 days of rent arrears and not, as previously, 7 days. On 18 June 2020, the level of rent arrears was extended to 187 days. This was subsequently extended to 366 days. This has now been increased to 544 days. It was due to come to an end on 30 June 2021 but this has now been extended to 25 March 2022. Commercial Rent Arrears Recovery is not available for unoccupied premises.

Commerz Real Investmentgesellschaft v TFS Stores [2021] EWHC 863

TFS Stores (The Fragrance Shop) had been closed during the various lockdowns. Since April 2020 it had not paid any rent. The landlord sued for non-payment of rent. In a summary judgment the High Court found for the landlord. Although Commercial Rent Arrears Recovery is suspended it was clear that this did not stop the landlord from suing for the arrears.
The tenant also argued that the landlord had not adhered to the Government Code of Practice for commercial property relationships during the Covid 19 pandemic. The Court held that this is merely voluntary.

Bank of New York Mellon Limited v Cine-UK Limited [2021] EWHC 1013

This involves further summary judgments in relation to Cine-UK, Sports Direct, Mecca Bingo and Deltic, a night club chain. The main question for the Court was whether rent suspension provisions covered pandemic. The Court decided that they did not but merely covered physical damage or destruction. The Court also decided that the contract had not been frustrated as the leases were for between twelve and thirteen years and the maximum closure was likely to be 18 months. For another case where a 25-year lease was not frustrated due to Brexit see ***Canary Wharf v European Medicines Agency [2019] EWHC 335***.

The tenants also argued that the landlord was not out of pocket because they could claim off their business interruption insurance. The Court held that this was irrelevant as it was open to the tenants to have taken out business interruption insurance (see below).

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Note: ***FCA v Arch and others [2021] UKSC 1*** The High Court held that certain business interruption insurance policies would cover closure through lockdown. On 15 January 2021 the Supreme Court confirmed the first instance ruling. The FCA has now issued detailed guidance on various business interruption insurance policies and their effect. In ***TKC London v Allianz (2020)*** this case made clear that there would be no claim if there was no business interruption insurance within the policy.

Note: On 16 June 2021 the Government announced that legislation will be introduced whereby night clubs and other members of the hospitality sector would have their rent ring-fenced whereby the landlord would have to shoulder some of the burden in relation to rent arrears. We do not yet know the detail. More details were provided in August 2021 although the Government's intentions are still rather vague. Any arrears accrued during restrictions on trading and until 25 March 2022 will be ring-fenced in relation to forfeiture of non-payment of rent. Arrears outside this period may give rise to forfeiture. For the ring-fenced rent arrears, the Government will introduce a legally binding Code of Practice to replace the voluntary Code from June 2020 (see above). If the landlord and tenant cannot settle claims there will be binding arbitration. These provisions apply to England only. THE WELSH GOVERNMENT RECENTLY ADOPTED THIS AS WELL.

The Corporate Insolvency and Governance Act 2020

This received Royal Assent on 25 June 2020 and came into force on 26 June 2020. Amongst other things it temporarily bars the making of a statutory demand if the reason for any debt is the Coronavirus pandemic. Likewise, in similar circumstances a winding up petition cannot be made. These provisions are back dated to 27 April 2020.
On the same day it was announced that the inability to make a statutory demand or serve a winding up petition was extended from 30 June 2021 to 30 September 2021 if the reason for arrears was the pandemic.
The Act has also introduced the concept of a Restructuring Plan whereby creditors can apply to restructure a business, for instance in relation to rent by a 75% majority. In some respects, this is similar to a Company Voluntary Arrangement, but will be overseen by the Court and applies to secured, and not merely unsecured, creditors.

Re Virgin Active Holdings [2021] EWHC 1246

The Act introduced the concept of Cross-Class Cram Down whereby dissenting classes of creditors or members may be bound by a restructuring plan if they have not agreed with the plan but would be no worse off. In the present case the creditor landlords had to accept a reduction in rent in relation to various gyms where the tenants have been severely impacted by the pandemic.

Company Voluntary Arrangements

Lazari Properties Limited and others v New Look [2021] EWHC 1209 Company Voluntary Arrangements were introduced by the **Insolvency Act of 1986** as a process whereby a company's liabilities may be restructured if 75% in value of the creditors are in favour. If it is approved, creditors are bound by the scheme whether or not they voted in favour. There is a 28-day window to object on the grounds of unfair prejudice or material irregularities.

Here New Look entered into a CVA in September 2020 following a previous one in 2018. The landlords objected to the fact that different classes of creditor were treated differently and there was no give and take. It would not be right that some creditors who would not be affected would impose their will on others who would be. It was held that on the correct interpretation of the legislation such a scheme was possible and was not unfairly prejudicial. This is not an all encompassing test but everything depends on the fairness of the case. The case is now to be heard by the Court of Appeal.

The case of ***Carraway Guildford (and a Nominee) Limited and others v Regis and others [2021] EWHC 1294*** followed on three days after New Look in May 2021. Regis entered into a CVA in October 2018. Certain landlords challenged the CVA on the grounds of material irregularity and unfair prejudice. Regis subsequently went into administration and this terminated the CVA but the landlords pursued the claim arguing that the nominees had breached their duties and should pay their fees back. The CVA was revoked on the basis that the treatment of an inter-company loan and its preferential treatment as critical creditor was not justified. As the CVA had already terminated this had little practical effect. Other arguments as to material irregularity failed as in New Look. There had been a blanket 75% discount of future rent to landlords. This was not a material irregularity but could not be justified. In New Look there had been a 25% discount which had been justified. Despite the finding of a breach of duty, in the absence of bad faith or fraud the court refused to order a payment of the fees of the nominees and the landlords' victory was pyrrhic.

Business Rates & Empty Properties AND *Hurstwood v Rossendale*

Empty commercial properties pay full business rates after 3 months and empty industrial units and warehouses pay full business rates after 6 months. If there has been occupation of at least 6 weeks in these periods then the time period to attract business rates starts again. The Welsh Government intends to increase the length of occupation from 6 weeks to 6 months. Other exemptions include listed buildings, community amateur sports clubs, and premises of companies in liquidation or administration. Premises occupied for charitable purposes pay 20% business rates which the local authority may waive. Such premises will not pay business rates when empty.

In ***Kenya Aid Programme v Sheffield City Council [2013] EWHC 54 (Admin*)** it was accepted that occupation by a charity for storage purposes in two adjoining warehouses could avoid business rates liability even though only 25% and 30% of the floor area was actually occupied. The Charity Commission subsequently warned charities that they should not be involved in avoiding business rates.

Hurstwood Properties (A) Ltd & Others v Rossendale Borough Council [2021] UKSC 16 In this case special purpose vehicle companies were set up with no assets. The companies would then be granted a lease of the otherwise empty premises. They would then be dissolved or go into liquidation. The dissolution or liquidation process would be drawn out for as long as possible and eventually if dissolved the lease went to the Crown under bona vacantia. Premises of companies in liquidation do not pay business rates. The schemes were based on local authority inertia as to what was happening.

The case involved the High Court originally throwing out the claim in a summary judgment against the Council for non-payment of business rates. The Court of Appeal agreed with this. However, on 14 May 2021, the Supreme Court decided unanimously that there was a case to answer.

They stated that the purpose of business rates on empty properties was to ensure that premises were not deliberately empty and the special purpose vehicle companies never intended to occupy. The device was therefore a sham and the business rates liability remained. There was a suggestion that the directors in relation to the dissolution schemes may be committing a criminal offence. There are now 55 further cases in this area due to be heard. How this impacts on other empty property avoidance schemes is yet to be seen.

Landlord & Tenant Act 1954: Renewal Terms and Coronavirus

The new lease will usually be on the same terms as the old tenancy but the court may, occasionally, sanction a change. Nevertheless, the initial assumption is that the terms will not be varied or changed. If a change is permitted then it should be adequately compensated in relation to a change in rent. See e.g. ***O'May v City of London Real Property Co [1983] HC*** and ***Wallis v General Accident [2000] EGCS45***: a change in the law does not mean that the landlord cannot upgrade the new lease to modern standards.

A major talking point of the moment is whether the new lease may include a rent suspension provision in the event of lockdown due to pandemic. The burden would be upon the tenant that this was fair and reasonable and reflected in a change of rent. ***WH Smith v Commerz Real Investmentgesellschaft (2021) April 19, county court***. The tenants had a lease of premises in a large shopping centre. They were able to remain open during the various lockdowns as the premises included a post office. On a lease renewal the landlord accepted that the new lease would include a rent suspension provision in the event of pandemic but only if the tenant's premises had to close. The tenant argued that their profits were much reduced due to lack of footfall in the shopping centre and therefore they wanted a rent suspension provision if any of the premises had to close due to pandemic. The county court judge decided for the tenant. The rent was not increased because of the rent suspension provision. This case may be instructive although a county court decision does not set a precedent.

In spite of this, in ***Poundland v Toplain (2021) July 2***, County Court, the court refused to change a rent suspension provision to include a pandemic clause. It also refused to include a provision whereby the right to forfeit for any breach would be suspended for the duration of any future lockdown. Following on from the House of Lords decision in ***O'May v City of London Real Property Company (1983)***, the starting point is that the new lease should be on the same terms as the current lease and the landlord would be unfairly prejudiced by any change. This distinguished WH Smith on the basis that in that case the landlord was prepared to accept a pandemic clause but was disputing its extent.

In June 2021 a new case settled the market rent for the premises, St James' Gallery in Jermyn Street. Due to the pandemic, the new rent was set at £102,000 pa whereas the original rent was £220,000 pa. It was noted that several properties nearby were now empty.

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