

CLIENT BULLETIN

COVID Rent Arrears Update

With legislation now in place setting out how arrears arising from the period of the pandemic should be treated, and disputes resolved, we are working with all our clients to clear the backlog of debt within this legal framework.

Summarising our experience to date of applying these new rules, this Client Bulletin addresses the following:

- Provides a summary of legislation within the Commercial Rent (Coronavirus) Act 2022
- Considers how best to apply these rules practically to recover tenant debt
- Reviews our experience of how occupiers are reacting to the Act
- Provides a reminder of actions that should be being taken now in light of the time constraints imposed by the new legislation.



THE COMMERCIAL RENT (CORONAVIRUS) ACT 2022

Protected Debt

The Commercial Rent (Coronavirus) Act 2022 came into effect on the 25th March 2022, and enables landlords and tenants to refer any debts due to the landlord under a business tenancy for a protected period, to be resolved by legally binding arbitration (if not resolved by agreement).

The protected period relates to the mandated closure period of the tenant's industry as a result of the COVID pandemic and will be from the 21 March 2020 until the last day of restrictions (including any periods during the protected period where tenants were permitted to open temporarily).

Protected debts can include sums whether or not described as rent within the lease, therefore including service charge, insurance, rent deposit top up payments, interest on unpaid rent and VAT.

The Arbitration Process

Application to the arbitration process is available for 6 months from the 25th March 2022. An application can be made by tenant or landlord and should be made with any supporting documentation and fee to one of the Government approved arbitration bodies, which includes the Royal Institute of Chartered Surveyors (RICS) and the Chartered Institute of Arbitrators (CIArb).

The arbitrator has discretion, however it must take into account two guiding principles:

- any award should preserve the viability of the tenant's business (but not at the expense of the solvency of the landlord) and,
- a tenant that is capable of paying the protected debt in full should do so without delay; any relief should be no greater than what is necessary for the tenant to afford the payment.

The tenant must be "viable" to benefit from the arbitration process. If the tenant is not viable, even with a full reduction in the protected rent, then the referral will be dismissed.

The arbitration process will provide an award which may include; writing off whole or part of the debt, outlining a payment plan (of no longer than 24 months from the date of the award) and reducing and cancelling any interest. The arbitrator is also able to dismiss the referral altogether.

Both parties will bear their own costs under the arbitration process. In addition to the arbitrator's fee, legal advice may be required, and it may take significant time to prepare the submission.



HOW ARE THESE NEW RULES BEING APPLIED PRACTICALLY?

As a result of the new legislation and the creation of a strict timescale for application to the arbitration process, there are some key steps we're taking with our clients:

- Engage with occupiers to resolve protected arrears by agreement - as a referral to arbitration may be costly, time consuming and the result uncertain.
- Have a clear understanding of the tenant's financial position - The Code of Practice for Commercial Property Relationships following the Covid 19 pandemic still applies – if a tenant can pay, even if they were forced to close, they should pay without delay.
- Allocate tenant payments correctly - the Act prevents landlords from applying payments now received to protected debt where there is unprotected debt. Where tenants specify that monies paid relate to a certain period landlords cannot allocate these to anything else and if the tenant is silent, it should be set off against the oldest arrears, provided that it is not a protected debt.
- React promptly if a tenant refers to arbitration – by constructively making a proposal for settlement, otherwise the applicant's proposal may be automatically imposed.

HOW IS THE NEW LEGISLATION AFFECTING NEGOTIATIONS WITH OCCUPIERS?

Given the lack of clarity regarding what happens beyond the six-month application deadline, and the impact thereafter on protected arrears, many clients are holding off making arbitration applications with a view to pursuing the full debt thereafter. Occupiers also appear reluctant to use this new process and are instead more likely increase efforts to seek a negotiated agreement.

A number of occupiers, often those that are represented, have sought to use the protected versus unprotected categorisation of debt within their negotiations, by offering to pay their unprotected arrears in full, but seeking part waivers of their protected arrears.

The ability to use CRAR again for unprotected rent arrears has also had an impact and brought some occupiers back to the negotiation table, including those that did not engage previously and those that were making unrealistic requests, or could afford to pay.

In some cases, rent concession requests have become more realistic, as occupiers are now less likely to request a complete waiver of all arrears, given the classification of protected and unprotected debt in the Act.

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NEXT STEPS - HOW WE CAN HELP.

Within our role as property managers, we are working collaboratively with both clients and occupiers to reach mutually acceptable solutions to avoid the uncertainty and costs of arbitration. Particular areas of focus include;

- Assisting clients to identify asset management opportunities to form part of negotiations – such as removing or deferring break clauses or extending the lease term to enhance asset value.
- Calculating protected and unprotected arrears - to feed into negotiations
- Allocating payments correctly - particularly important where the occupier is silent on allocation and monies should be allocated against any unprotected arrears first
- Assisting clients to understand underlying covenant strength – to inform negotiations
- Implementing CRAR (where applicable) - and recommending other remedies where there are unprotected arrears eg use of deposits
- Agreement of concessions (outside of the arbitration scheme) - assisting clients and solicitors document these with and subsequently monitor compliance.



We are likely discussing the application of this legislation across your portfolio already with you, but if you have any queries please contact your usual Client Partner to discuss in more detail.

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