



# Landlords' remedies for tenant/guarantor insolvency (a short case study)

## A case study of what to look out for when a tenant or its guarantor is looking like it is heading for financial difficulties

As a prudent and prepared landlord, it's always sensible to assess what potential remedies you might have should a tenant (or its guarantor) become insolvent or enter into some form of insolvency procedure. In this bulletin, we look at a short hypothetical case study and identify some of the key issues that landlords will need to assess in such circumstances.

### 1. The case study scenario

The case study facts are as follows:

- We have an original tenant that is an English Special Purpose Vehicle (the **Tenant**), established for the purposes of taking a lease dated 1 April 2016 (the **Lease**). The Tenant itself does not have any substantial assets.
- In contrast, the Tenant's obligations under the Lease are guaranteed by its parent company, a US entity (the **Guarantor**). The written guarantee is in a separate agreement to the Lease.
- The Tenant uses the premises for a mixture of:
  - Sublet space to a single third party; and
  - Serviced office space where temporary occupation by customers is under short, written licence agreements.
- It now appears the Guarantor and its group companies are in financial difficulties.

NOVEMBER 2019

London, UK

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## 2. What happens if the Tenant becomes insolvent?

### ... and what is meant by "insolvency" and how might it be spotted?

This means that the Tenant is unable to pay its debts as they fall due. There may be arrears of rent. It may be that the Tenant company gives indications of having difficulties, for example by requesting that it pays rent monthly. There may be press speculation. Alternatively, the first indication may come from the Tenant entering into a formal state of insolvency, for example an administration or possibly a liquidation, or it may propose a CVA, which is a binding arrangement between it and its creditors (if 75% of creditors vote in favour).

#### Steps to take

- Check your rights under the Lease: do you want to take the premises back e.g. exercise rights to forfeit the Lease if the Tenant is in breach? You may need to stop communicating with the Tenant and act quickly, subject to any grace periods in the Lease, to forfeit the Lease so as to prevent risk of waiver of the right to forfeit.
- Do you want to agree to any kind of concession, e.g. monthly rent, or even a rent reduction (N.B. taking care not to discharge the Guarantor by agreeing variations without the Guarantor being a party to the variation). Also, a concession may mean a "double haircut" if there is a subsequent CVA.
- If the Tenant is in a formal state of insolvency, e.g. administration, then a moratorium may already exist which prevents you taking enforcement action (including forfeiting the Lease) without the administrators' or Court's permission. The Tenant's administrators may try to return the keys to you but they are not allowed simply to surrender the Lease unilaterally.
- If the Tenant is already in administration but is continuing to benefit from the use of the premises (either itself or taking an income from the use by others), you may be entitled to insist that the Tenant pays rent (e.g. weekly) for this ongoing period of use and occupation after the administration starts.
- If the Tenant is in liquidation (the final stage before winding up) then the liquidator may seek to "disclaim" the Lease so that it comes to an end, leaving you with only a claim as an unsecured creditor. If disclaimer happens then care must be taken **not to re-enter** the premises physically or otherwise treat the Lease at an end, if you are considering pursuing other contractual parties such as a Guarantor (or on different facts, a former tenant or guarantor).
- If the Guarantor is solvent, you will want immediately to consider claiming against the Guarantor for money owed (see below).

## 3. What if the Tenant is insolvent but the Guarantor is solvent?

### Consider your enforcement options against the Guarantor

Your ability to claim against the Guarantor will be tied directly to the contractual terms of the guarantee.

#### Steps to take

- Check the terms of the guarantee and make sure that the Guarantor is still solvent (credit check).
- Is the Guarantor a "primary obligor"? This means that you do not have to go to the Tenant first before demanding money from the Guarantor, so it is a stronger position.
- Is the guarantee a "money only" guarantee where the Guarantor only agrees to pay for debts etc. that the Tenant has failed to pay? If so, consider making an immediate claim.
- Can you call on the Guarantor to take a lease of the premises, effectively in place of the Tenant's Lease? This kind of provision sometimes exists but would need to be triggered by the landlord, and

sometimes within a limited period of time e.g. within X weeks of a disclaimer or forfeiture. Time limits should be treated as absolute.

## 4. What happens if the Guarantor becomes insolvent?

### Is there anyone else to claim against?

#### Points to consider

- If both Tenant and Guarantor are insolvent, you may want to consider taking the premises back by forfeiting the Lease or accepting a surrender, but take advice on possible liability for business rates first.
- On other facts, there may be a former tenant or guarantor, or a rent deposit, to claim against, in which case advice should be taken before any further steps are taken as forfeiture etc. may prejudice an ability to make a forward-looking claim as future rent falls due.
- In the unusual situation where the Tenant is solvent but the Guarantor is not, it may be possible to require the Tenant to deliver up a new guarantor, failing which you may have a right to forfeit.

## 5. What happens to the Sub-tenant and the Licensees?

### The position will be different depending on whether there is a lease or a licence

- For occupiers under licences, if you forfeit the Tenant's Lease, the licences will come to an end too.
- If you forfeit the Lease with a sublease still existing, then the subtenant has a right to apply for relief from forfeiture (even if the Tenant does not, which here it may well not do), and seek a new lease for the rest of its term. You may be able to insist that the subtenant takes a lease on the terms of the Tenant's Lease (i.e. of the whole property) or you may argue that the subtenant should not have a right to relief at all. The question would be decided by a Court.
- If you have not terminated the Tenant's Lease, and there are existing subleases, you may be able to serve notice on the subtenants requiring that they pay their principal rent (but not other sums reserved as rent, such as service charge) directly to you.
- If licensees are paying fees to the Tenant, while it is in administration, then again you may be able to make a claim against the Tenant because it is benefiting from its use of the property.

## 6. What else should I think about?

- **Dilapidations** – has the Tenant failed to keep in repair and should you serve notice to reinstate so you can make a larger claim for that either against the Tenant or the Guarantor?
- **Rent deposits** – is there a rent deposit which you can draw down if the Tenant is in arrears? The specific terms of the rent deposit should be followed, particularly in relation to how the rent deposit is held (for example, in the name of the landlord or as a stakeholder, charge or on trust for the tenant). Care should also be given as to how and when the landlord can draw down on the deposit as well as any notification requirements to the tenant if this action is taken.
- **Commercial Rent Arrears Recovery (CRAR)** - CRAR can only be used in respect of rent payable under the Lease for the possession and use of the premises. "Rent" does not include any sum in respect of rates, services, repairs, maintenance, insurance or other ancillary matters even if these amounts are reserved as rent in the lease. CRAR is only exercisable by a registered enforcement agent on behalf of a landlord and there is also a mandatory notice period of at least seven clear days before CRAR can be exercised.

- **Business Rates** – taking the premises back will usually mean that you will become liable for these from that point onwards.
- **Safety and security** – is there a risk that third party squatters may move in? You may want to consider steps to ensure that the premises are protected from this, e.g. by ensuring that there is still security at the entrance. **However**, you must be careful **not to do anything** to exclude the Tenant or take back possession, if you want to treat the Lease as ongoing so as to make claims for continuing rent e.g. against the Guarantor.
- **Enforcing for debt** – doing this, either against the Tenant or the Guarantor, is a big subject in itself. With a solvent Guarantor registered abroad, then thought must be given to where the assets are against which a claim could be made, and whether a claim would need to be made here but then registered as a judgment abroad (e.g. in the relevant U.S. state) for enforcement purposes.
- **Monitoring the source of any sums paid on behalf of the Tenant** - a change in the identity of the usual payee may be indicative of a pre-pack administration or some other re-structuring.

## 7. Contacts

### We are here to help.

We are experienced in advising on, and taking steps to pursue, insolvency remedies against tenants in the UK, including enforcement of obligations, claims against guarantors and dealing with formal states of insolvency such as administrations and CVAs. We are a global firm and have successfully pursued foreign registered guarantor entities including in the US to recover arrears of rent or to obtain a substantial capital payment for a release from guarantor liabilities.

**Our Real Estate Dispute Resolution lawyers operate as a combined team practising English and Welsh law from our London and Belfast ALT offices, so as to offer low cost solutions when dealing with contentious matters such as enforcement against insolvent tenants.**



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