Law of unintended consequences

The regime for commercial rent arrears recovery has been in force for over a year, but are the changes working? Mathew Ditchburn examines how landlords' concerns have played out.

More than a year has passed since sweeping changes to the landlord's right to use bailiffs to collect unpaid rent were introduced through the commercial rent arrears recovery (CRAR) provisions of the Tribunals, Courts and Enforcement Act 2007. At the time of its introduction in April 2014, landlords expressed concern over the potential effect of a number of CRAR's features. The Ministry of Justice committed to a review after 12 months to identify any unintended consequences of the new process. Over one year on, have the landlords' worries proved founded?

A key concern

Probably the most contentious element of the new regulations is the requirement to give tenants seven days' clear notice before an enforcement agent (which the landlord must instruct to exercise CRAR) attends and takes control of any goods at the premises in respect of unpaid rent. Landlords are concerned about the potential for a tenant to abscond with the goods during the notice period, denying the landlord the opportunity to secure the tenant's assets in lieu of the debt. Experience since April 2014 suggests that, in fact, the service of the enforcement notice has not led to a marked increase in tenants "doing a runner". Indeed, the majority of tenants served with a notice have paid within the notice period. However, a different consequence has arisen. Some tenants treat the notice as a week's extra time to pay, with the landlord unable to act until it has expired. The driver behind this would appear to be the fact that the statutory fee payable by the tenant to the enforcement agent at the notice stage is fixed at £75 regardless of the value of the debt. This, arguably, gives larger operators an unfair advantage – a small company or sole trader with a low-value rent suffers the same initial penalty as a national multiple. The fees that apply if an enforcement agent attends the premises to take control of goods (by entering into a controlled goods agreement) once the notice has expired are set at approximately 7.5% of the debt, which is clearly a very strong incentive for tenants to pay within the notice period. Notably, landlords have seen a number of regular, repeated uses of this unofficial "overdraft" by the same tenant companies. Frustratingly, landlords have no easy means of accelerating the process with such repeated cases, and alternative remedies can take even longer.

Other issues

A further unforeseen consequence is that although the goods in the unit are deemed to be "bound" when the enforcement notice is served, without the initial bailiff attendance to take an inventory, there is no way for the landlord to prove what assets were bound. The tenant may remove goods that were present at the time of the notice before the enforcement agent attends to take control of them. The next major concern for landlords was that CRAR could only be used for principal rent and not for other costs, such as service charge and insurance. Landlords were vocal in their objection to this when CRAR was introduced. Although the rationale for excluding variable (and, therefore, less certain) charges was understood, in reality on-account service charge does not usually vary from one payment to the next, and many leases incorporate an all-inclusive rent where the service charge element never varies.

Concerns justified

Landlords' concerns have proved to be justified, with increases seen in property owners using methods such as county court claims and statutory demands to collect service charge and other debts. At the same time, marketing of High Court enforcement services to the landlord community has become more prevalent over the past year. If one of the purposes of CRAR was to establish a remedy for landlords that was less oppressive to tenants, then it would seem unlikely that the use of these alternative remedies was intended, as they are generally more costly and have further-reaching consequences for tenants than CRAR.

BPF initiative

The British Property Federation (BPF) has contributed to the Ministry of Justice review with recommendations to address these experiences and concerns. In particular, the BPF suggests:

- the fees throughout the process to be a percentage of the arrears, with a fee of, say, 2.5% of the unpaid rent at the enforcement notice stage and 5% at the controlled goods agreement stage;
- that CRAR should be available for debts other than rent – in particular, where those other costs are fixed, for example where the lease provides for an "all-inclusive" rent;

- introduction of a 24-hour notice to attend the demised premises to take an inventory. The landlord would still not be able to take control of goods until expiry of the enforcement notice, but evidence of those goods bound by CRAR would be created. The BPF recognises that this may cause some disruption to the tenant, but believes this is proportionate disruption
- introduction of a "three strikes and you are out" system. This would maintain the status quo with existing CRAR legislation, but if an enforcement notice is served three times under a particular lease, the landlord will thereafter be relieved from the requirement to serve an enforcement notice and be entitled immediately to enter into a controlled goods agreement in the event of any further arrears.

The BPF believes these recommendations maintain the transparency for tenants that CRAR sought to introduce, while bringing some much-needed balance to the landlord's position when dealing with non-paying occupiers of its assets.

An earlier version of this article appeared in Estates Gazette on 26 September 2015 and was co-authored with John Cook, revenue manager at Capital & Regional. John and Mathew are, respectively, chairman and vice-chairman of the British Property Federation's Insolvency Committee.

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