

Restructuring Bankruptcy & Insolvency Group Legal Alert

Permission to enforce a covenant in a lease prohibiting parting with possession against a tenant in administration and the treatment of post-administration rent as an expense

Areas of Interest

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Summary

The Court of Appeal¹ has refused to give permission to a landlord to commence proceedings against a tenant company in administration. The landlord sought a mandatory order for the immediate termination of a licence which had been granted by the company in breach of the terms of the lease. In doing so, the Court followed the principles set out by the Court of Appeal in *Re Atlantic Computers*².

The Court of Appeal also declined the landlord's request that full rent should be paid for the post-administration period as an expense of the administration.

¹ *Innovate Logistics Limited (in administration) v Sunberry Properties Limited* [2008] EWCA Civ 1261.

² *Re Atlantic Computer Systems plc* [1992] Ch 505

Background

A company (“C”) went into administration pursuant to a Court order. This was a “pre-packaged” administration involving a sale of C’s business as a going concern to a purchaser (“P”). P undertook to perform C’s existing customer contracts and, as agent for C, to collect the book debts due to C (the book debts having been excluded from the sale).

C leased premises from landlord (“L”) (the “Lease”). The Lease contained a prohibition on “*parting with possession of the whole or any part of*” the premises.

In order to perform C’s existing customer contracts and to collect its book debts, P needed access to the premises for a limited period of time. P did not wish to take an assignment of the lease as it required only temporary access. Therefore the sale of the business was on terms pursuant to which C purported to grant an occupational licence of the premises (the “Licence”) to P for a period of six months. P would pay to C a monthly payment equal to the passing rent payable by C under its lease (the “Licence Fee”). The administrators agreed to pass the Licence Fee on to L.

Whilst the Licence was in breach of the terms of the Lease, the administration moratorium prevented any legal process being instituted or continued against C or its property without the consent of the administrators or the permission of the Court. L therefore applied to the High Court for permission to commence legal proceedings against C seeking an order terminating the Licence (the administrators having refused consent). L did not seek an order forfeiting the Lease.

The High Court gave permission to commence proceedings but stayed the order pending an appeal by C acting by its administrators.

The decision of the Court of Appeal

The Court of Appeal affirmed that the principles to be applied when deciding whether to grant permission to commence legal proceedings against a company in administration are those set out in the Court of Appeal’s decision in *Re Atlantic Computers*. The Court must balance the legitimate interests of L and the other creditors. The Court took into account money paid by the administrators to compensate L. The Court attached great importance to the proprietary interests of L, who should not be prejudiced by the way in which the administration is conducted, save to the strictly limited extent that this may be unavoidable. The burden was on L to show that it would be inequitable for it to be prevented from commencing proceedings.

The Court of Appeal allowed the appeal by C, holding that the High Court had been wrong to conclude that the statutory purpose of the administration (to achieve a better result for C's creditors as a whole than would be likely if C were wound up) would not be impeded by the commencement of the proceedings. The High Court had misunderstood the differences between traditional and "pre-packaged" administrations in commenting on the course of action adopted by the administrators. It had not appreciated that one of the main aspects of the administration was the collection of book debts by P as agent for C (and hence for the benefit of C's creditors). In order to pursue this aspect successfully it was essential for P to occupy the premises. The order sought would have prevented P from collecting in the book debts. The High Court had failed to ask itself whether L had shown that it was inequitable for the Court to prevent it from commencing proceedings.

Payment of rent

It was accepted that L had no automatic right to be paid the contractual rent and interest under the Lease during the premises' occupation by C in administration as an expense of the administration. However, if it were not granted permission to bring proceedings, L submitted that it would be wrong in principle for the occupation of the premises to be for the benefit of past creditors at its expense. Therefore the full rent should be paid, not just the Licence Fee, as an expense of the administration.

The Court of Appeal held that L did not have an absolute legal right to be paid contractual sums as an expense. The Court had a wide discretion, which it exercised. P did not wish to take an assignment of the Lease. C (which was unable to perform its obligations under the Lease) did not wish to continue trading and, but for the Licence, would be unable to pay anything in respect of the premises. L would therefore receive the Licence Fee which P was required to pay to C, together with any interest that had been earned by C on the Licence Fee.

Commentary

This decision affirms the broad scope of the administration moratorium. Notwithstanding a breach of the terms of a lease, the Court was not willing to allow the landlord to commence proceedings and would not exercise its discretion to order that post-administration rent be either paid in full or treated as an expense. The outcome may have been different if P had not satisfied the Court that it needed access to the premises to collect C's debts, rather than simply continuing to trade from them. The Court of Appeal made comments in *obita dicta* in support of the "pre-pack", referring to the administrators acting "properly and for the benefit of the creditors". Such temporary licence arrangements are often used in administrations and the decision provides some comfort to those doing so. It may, however, trouble landlords increasingly concerned about tenant solvency.

If you would like any further information about this please speak to your usual contact in the Restructuring Bankruptcy and Insolvency Group or contact:

DAVID ALLEN

Partner

Tel: +44 (0)20 7782 8813

DEVI SHAH

Partner

Tel: +44 (0)20 7782 8669

ASHLEY KATZ

Partner

Tel: +44 (0)20 7782 8818

IAN MCDONALD

Partner

Tel: +44 (0)20 7782 8856

DAVID MORRISON

Partner

Tel: +44 (0)20 7782 8876

SIMON HARTLEY

Senior Associate

Tel: +44 (0)20 7782 8928

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