Recent case summaries

A corporate insolvency update from **Daniel Lewis**.

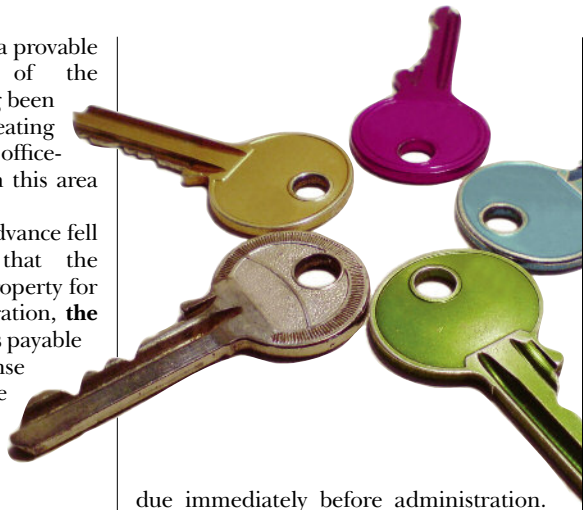
The treatment of rent as a provable debt or expense of the administration has long been a vexed area creating considerable uncertainty for office-holders. Until recently the law in this area was anomalous in that:

(a) If a quarter's rent payable in advance fell due **during the period** that the administrator was using the property for the purposes of the administration, **the whole** of that quarter's rent was payable as an administration expense even if the administrator gave up occupation during the quarter (*Goldacre (Offices) Ltd* v. *Nortel Networks UK Ltd* [2011] Ch. 455);

(b) If a quarter's rent payable in advance fell due **before** administration, **none** of that rent was payable as an expense of the administration even where the administrator retained possession for the purposes of the administration. The rent was instead a provable debt in the administration (*Leisure (Norwich) II Ltd* v. *Luminar Lava Ignite Ltd* [2013] 3 W.L.R. 1132).

> "Rent of £3m remained unpaid in respect of those stores."

The practical effect of this was that it was often in the company's interests to enter administration immediately after the quarter's rent had fallen due. The company could then continue to trade (either in administration or following a sale of the business, through a successor company) without payment of the rent that had fallen due immediately before administration. While such a result might be for the benefit of creditors as a whole (by relegating the landlord's claim for rent to a pari passu entitlement), that result was achieved at the expense of a single creditor (the landlord). The fairest result in the two instances referred to above would be that the rent be treated as an expense of the administration on a pro-rata 'pay for what you use' basis, thereby avoiding saddling the administration with expenses from which the creditors derived no benefit but equally avoiding the situation where the continued trading from the company premises is at the expense of a single creditor.



The issue in *Re Game Station Ltd* [2014] EWCA Civ 180 was whether this was a result open to the Court of Appeal on the basis of the case-law.

Facts: The claims arose from the administration the Game group of companies. One of the group companies was tenant of hundreds of leasehold retail properties from which the group traded. Rent was payable quarterly in advance and fell due the day before the group entered administration. While some stores were shut down immediately, others continued to trade through the administration and following a sale to the purchasers of the business. Rent of £3m remained unpaid in respect of those stores.

At first instance the judge followed the decisions in *Nortel* and *Luminar* but granted the landlords permission to appeal.

The legal principles: Where rent falls due immediately before administration, the rent is provable as a debt in the administration (rule 2.87). Rule 2.67, on the other hand, provides that expenses of the administration will include 'expenses properly incurred by the administrator in performing his functions in the administration of the company'. This rule is subject to the salvage principle, which allows for a debt that would otherwise be provable to be treated as an expense of the administration. The authoritative statement of the principle was given in *Re Lundy Granite Co* (1870-71) LR 6 Ch App 462: *'if the company choose to keep the estates for their own purposes, they ought to pay the full value to the landlord'*.

> "The decision will need to be taken at an early stage at to whether to continue trading from company premises."

Held: In his judgment Lewison LJ provided an authoritative review of the authorities on the salvage principle and the apportionment of rent. He held that the principle was not constrained by the fact that rent payable in advance could not ordinarily be apportioned, since there was no termination of the lease or change of tenant. The salvage principle required that the company pay 'full value' for the use of the property. To limit requirement to provide 'full value' to cases where the rent fell due after administration would be an arbitrary result. Instead, whether or not a quarter's rent in advance was payable before or after administration, the rent should be treated as accruing day-to-day as an expense of the administration.

Practice points

- The administrator must pay for what he uses. This cuts both ways: the administrator is not required to pay for the whole quarter of post-administration rent if he subsequently goes out of possession during that quarter.
- The disadvantage for administrators is that they are now denied the 'breathing space' available where rent in advance has fallen due immediately before administration.
- The effect of this is that the decision will need to be taken at an early stage at to whether to continue trading from company premises. This might be a strategic decision that can be taken in advance in the case of some appointments, but might be far more difficult where there has been little or no involvement of the office-holder before administration.
- It remains unclear whether the administrator is required to pay only for those parts of the premises which he is using on the same basis as he is required to pay for the period of his occupation. The better view appears to be that the rent that is payable is that due under the lease (albeit that it may be apportioned for the period of occupation) and that there is little room for arguing that the extent of occupation can be taken into account.
- It is also uncertain whether or not ancillary charges (in particular service charges) will be treated in the same way as rent. While service charges and insurance reserved as rent might be readily apportionable, in a case where charges fall due for major works for instance, it is not readily apparent how the total charge would be to the benefit of the administration or how this charge might be apportioned.

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