

Proposal to withdraw moratorium on enforcement action for Commercial Property

Created by Landsec and British Land

The proposed model is based on the following principles:

- The Proposal is targeted at retail, food and beverage, hospitality and leisure premises.
- Protecting jobs is our primary aim and we will do everything in our control to avoid any 'cliff-edge' of job losses caused by the moratorium being withdrawn.
- We want to see the market returned to normal operation as quickly as possible without Government being burdened with either long-term support of a sector or a role that opens it up to legal challenge.
- Given the unprecedented nature of the pandemic, it is only right that the landlord, hospitality and retail sectors share the pain but in a way that reflects the relative strengths of their businesses and their ability to trade over the last year.
- Government needs to create the right conditions to bring landlords and occupiers together to negotiate where arrangements have not been concluded. Providing certainty with what will replace the moratorium will contribute to this, as will Government setting out its guideline for what it believes would be a fair way to share costs through lockdown periods.
- It only applies to rent arrears where payment agreements have not yet been reached between landlords and occupiers. Payment agreements that have been formally executed between owners and tenants during the period from March 20 to April 21 will be respected and not be overridden.
- Arbitration should be a last resort but a binding one.

Approach

This proposal seeks to uncouple the treatment of arrears from ongoing rent obligations to encourage prompt payment going forward once businesses can trade again. Given current projections for a consumer-demand led recovery, there are strong signs that the market can start to resume normal operation in line with the Government's roadmap from June.

According to ONS data, published on 22 April, measures of consumer activity have already begun to recover impressively. Retail footfall in the UK in the week to 17 April increased by 31 percentage points from the previous week to 75% of the level seen in the equivalent week in 2019. On Saturday 17 April, seated diner reservations were estimated to be at 60% of the level seen on the equivalent Saturday in 2019, with restrictions on indoor dining still in place. Online job adverts recovered to pre-pandemic levels on 8 April as retailers, pubs and restaurants took on new staff; and retailers have reported strong store sales post re-opening. This data points to a strong rebound in consumer activity in H2 as the economy re-opens.

In this context, and to manage the negotiation and payment of arrears, we propose a phased approach. This is designed to give occupiers breathing space to resume operation before paying arrears or to negotiate payment plans with their landlords by bringing arrears within the enforcement regime only once they have been open and trading for a considerable period.

Under these phases:

- The moratorium ends on 30 June 2021. Normal market operation will resume from this date, particularly given the ring-fencing of rent arrears discussed below. Any rent billed on

or after June quarter day (25 June) will not be ring-fenced alongside historic arrears detailed below.

- Payments owed from before this date (i.e. The period of trading restrictions from March 2020-May 2021) will be ring-fenced with the moratorium remaining in place with respect to those arrears. Landlords and their customers will have until December 2021 to agree concessions where appropriate. Payments can be deferred until after this date as long as an agreement has been reached.
- Current protections around existing debt will continue after December 2021 where both parties have submitted to arbitration having failed to negotiate a deal.

Managing rent arrears

The primary concern for all involved in this process is how to manage the issue of rent arrears without causing significant damage to otherwise viable businesses.

While a blanket write-off of a proportion of debt accrued through lockdown periods is a superficially attractive solution, closer inspection of its potential consequences reveal that it is unviable, creating as many problems as it may solve.

For example, there are several businesses who have paid in full throughout the pandemic – adopting the Government’s principle of ‘those that can pay, should pay’. A blanket write-off would penalise them for their good behaviour and engagement.

Several similar scale well-capitalised businesses have refused to engage throughout. A blanket write-off would benefit them, doubly penalising those who have engaged in good faith throughout – and likely leading to legal challenge.

Setting criteria through which a blanket write-off would apply is problematic and likely to lead to multiple, complex legal challenges. Defining what is a small landlord or a small occupier is not simple, given the number of special purpose vehicles that have been developed on either side of this debate which would allow certain landlords or occupiers to present as smaller businesses than they are.

The best way to reward good behaviour and avoid perverse outcomes in addressing rent arrears remains to bring landlords and occupiers together more quickly in negotiation.

The best way for government to achieve this would be to create a clear guideline for negotiation and to introduce a clear backstop to negotiation that would penalise those who did not engage in good faith.

Creating a guideline for negotiation

The *Code of Practice for commercial property relationships during the COVID-19 pandemic* was endorsed by the key bodies representing landlords and occupiers. It should serve as the basis for creating a new guideline for negotiations.

Although recently updated, the bulk of the Code was created early on in our experience of the pandemic, before the introduction of tiers and various additional lockdowns. We now know more than we did then.

We recommend that the current Code of Practice is enhanced to give more specific guidelines for negotiation between landlords and occupiers to speed up negotiation and resolution. For example, the new code could include that:

- As the Government has set out, those that can pay, should pay. The phased approach set out above is to protect those businesses who need it. Where a business’s cashflow position allows for it – taking into account the overall revenues and resources of its parent group – arrears should be cleared in full although it remains open to the parties to negotiate a schedule for clearing those debts to preserve cash-flow.

- Where a business is unable to pay and has been unable to trade from their premises specifically because of legislation prohibiting operation through specific lockdown periods, landlords and occupiers should aim to share costs on an approximately 50-50 basis by reducing rent for that period by 50%, although the final outcome should also be informed by the relative scale of the two businesses. Genuine through costs such as insurance and service charge should be paid in full.
- Where an occupier is unable to meet its rental obligations in full and has been able to trade but with certain restrictions – for example caused by the tiering system – they should share their books with their landlord to negotiate and agree an equitable solution that reflects the points above. This should be based on the customer providing at least three years of financial information to facilitate a fair assessment of the impact of the pandemic on their business. It should also take into account online/click and collect operations fulfilled from the property.
- Where a business has been able to trade without restrictions to its operation or opening hours during the relevant periods (e.g. supermarkets), they should seek to fulfil their full rent obligations. This should apply regardless of indirect effects of the pandemic on their profitability.
- The negotiation guidelines should provide for a more targeted approach to any future moratorium based on different forms of business operation. Additionally, the guidance on the scope of concessions that are appropriate should be expressed to apply to any such future lockdowns or lesser restrictions.

Stronger guidance along these lines would facilitate speedier negotiation and thus resolution – and provide guidance for arbitration should a settlement not be reached.

Arbitration backstop

- Where an occupier and a landlord cannot reach a settlement within the phases set out above, they will submit to binding arbitration. The arbitration will use the enhanced code of practice as a guideline to what a reasonable compromise should be.
- With the Government setting out clear guidelines for negotiation, arbitration can be provided by an expert in arbitration rather than a real estate specialist service.
- Clear guidelines for negotiation and arbitration would also allow a compromise solution to be reached by the arbitrator rather than a binary outcome as currently envisaged under option six in the Government's call for evidence.

Additional terms

- None of the above means there is a statutory deferment of payment obligations. It simply extends out the current restrictions on the use of statutory demands, winding up petitions, CRAR and forfeiture.
- Debt action through the courts is still available and considered appropriate because it can proceed with judicial oversight.
- In order to prevent aged debt from getting much larger, late payment interest will be capped at 3% for arrears from 25 March 2020 to June 2021. In a low interest environment this will prevent the adverse effect of compounding.
- In return a statutory limit on compromising arrears through insolvency processes (e.g. CVAs and Restructuring Plans) should be applied. If this measure is not applied, then there will still be an incentive for a surge of insolvencies to clear the debts even where landlords have negotiated concessions in good faith.

- While not contingent to this proposal, the role of lenders will be important to support landlords as they work with their customers to manage arrears. There is a clear role for Government to play to ensure this happens.