

Rough guide to arrears of rent

Gillian Craig, a specialist in commercial litigation at MacRoberts in Glasgow says that landlords are in a fortunate position when it comes to forcing payment.

In the current economic climate, landlords need to prepare to take fast action against business tenants who are in arrears of rent. To this end, landlords ought to bear in mind the options open to them and decide what they want to achieve; do you simply want paid - or do you want to get rid of the tenant?

Litigation is the standard form of debt collection. Prior to raising, it's usual practice to serve a pre-litigation demand upon the debtor stating the sum owed, and demanding that payment be made within seven days, otherwise legal proceedings will begin.

Often, the threat of litigation is enough to prompt debtors to make payment, but if the tenant is still not moved to pay up, the next step is to raise a court action.

Whilst court actions are generally perceived to be slow and costly, the advantage they have is the availability of 'diligence on the dependence', which means the landlord can "arrest", which works by freezing sums due to the debtor, and or 'inhibit'. Inhibition is a court order preventing the debtor from selling, or voluntarily disposing of, heritable property.

In order to obtain either, the landlord must convince the court that the case has merits and that the tenant is at risk of insolvency. It is also dearly useful to know the tenant's bank details so you know where to arrest!

But it's possible to arrest or inhibit without the need to resort to litigation- if your lease contains a consent to registration for preservation and execution and is, in furtherance of that, registered. Almost all commercial leases will contain such a clause - or at least they should. The extract copy lease is then equivalent to a court decree and can be enforced in exactly the same way - this is known as 'summary diligence'. However, this can only be used for sums that are either stated or easily ascertainable from the lease.

Finally, the provisions of the Insolvency Act 1986 provide some assistance. In short, the Act provides that a creditor can wind a company up if the debt owed by the company to the creditor is undisputed. Whilst care ought to be taken before actually applying for a court order to wind the debtor" up, the threat of this is an increasingly common debt collection tactic.

Clearly there is little point in winding up a tenant if there is little chance of the landlord receiving a dividend. In this regard, it's worth bearing in mind that the landlord may not be an ordinary, unsecured creditor. One right peculiar to landlords, which other creditors do not enjoy, is a landlord's implied right in security, known as a 'hypothec', over the tenant's moveables within the leased premises. However, it only covers rent arrears, and not other outstanding payments.

What if you just want to get rid of the tenant? Even if the landlord is fortunate enough to have a new tenant waiting in the wings, the landlord cannot bring the lease to an end unilaterally.

Most commercial leases have irritancy clauses, entitling the landlord to terminate the lease prematurely because of the tenant's breach of contract for example, if rent is not paid within 14 days; the tenant is wound up; or an administrator or receiver is appointed.

If there is no irritancy clause, rescission (being the right of a party to bring a contract to an end, if there has been a material breach of the contract by the other party) is still available.

However, non-payment of rent is not considered to be a material breach of a lease entitling the landlord to rescind. As such, in the absence of an irritancy clause the landlord would have to wait until 2 years rent arrears had accrued before he would be able to exercise the implied right of 'legal irritancy'.

Whether you are irritating or rescinding a lease, the provisions of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1985 must be complied with. In short, 14 days notice to pay must be given for monetary breaches. This is often called a pre-irritancy notice and of itself can often prompt payment.

For non-monetary breaches the fair and reasonable landlord test must be satisfied.

Again, care must be taken before actually irritating or rescinding the lease as, depending on the lease terms, certain lease end rights may be lost - such as those relating to the carrying out recovery of terminal dilapidations.

When negotiating a lease, the well-advised landlord will protect his position through the use of terms such as the payment of a deposit; payment of rent in advance; and "no withholding" or "no deduction" clauses stating that the tenant cannot withhold rent from the landlord for any reason.

A guarantee of a tenant's obligations by a third party, typically the individual behind the tenant company or a parent company, can also be invaluable.

In conclusion, landlords are in the fortunate position of having a number of remedies open to them to try to force payment; in these hard times, it is likely that tenants will have a large queue of creditors - there is no reason why the landlord shouldn't be at the front!

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