The latest on payment of rent in an administration - innovative logistics

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The question of whether an administrator can be required to pay rent as an expense of the administration remains a highly topical one and one to which the answer had been becoming clearer. In short, it was simply a question of whether the premises were being retained for the purposes of the administration. If so, rent should be paid as an expense of the administration during the period of such use.

The underlying reasoning was as follows:

- The categories of administration expenses are prescribed by statute: see r. 2.67(1) Insolvency Rules 1986.
- These categories leave the administrator and the court with no discretion as to what is or is not an administration expense: Exeter CC v Bairstow [2007] EWHC 400, applying the reasoning of the House of Lords in Re Toshoku Finance UK plc [2002] 3 All ER 961 relating to liquidation expenses. It is simply a matter of construction of the relevant categories.
- If therefore an expense falls within one of the categories it must be accorded the status of an administration expense with the priority that flows from that status under para 99 sch B1 Insolvency Act 1986.
- There are two potentially relevant categories which might be said to catch post-administration rent in circumstances where the leasehold premises are being retained for the purposes of the administration:
- "expenses properly incurred by the administrator in performing his functions in the administration of the company" and
- "any necessary disbursements by the administrator in the course of the administration ..."
- At first sight, they both seem wide enough to catch post-administration rent accruing in such circumstances. Such a construction is also supported by the so-called "liquidation expenses" (or Lundy Granite) principle. This principle was developed in relation to liquidation and allows sums falling due post-liquidation under a pre-liquidation contract (eg a lease) to be deemed to be an expense of the liquidation where they related to property being used for the purposes of the liquidation. Although liquidation expenses are now defined by statute, Lord Hoffmann suggested in Toshoku (above) at para 38 that the statutory categories should be construed having regard to the principle. Presumably, the same approach should be taken when construing the categories of administration expenses given what was said by the Court of Appeal in Atlantic Computers [1992] 1 All ER 476 about the principle also finding application in administration.
- It has been held, however, that category (a) is limited to expenses incurred by the administrator personally. David Richards J so held in Exeter CC (above) at para 52 when considering whether rates fell within (a). If this is right (and his reasoning is persuasive), (a) cannot apply to post-administration rent. (It should, however, be noted that Lord Hoffmann seems to have thought in Toshoku (above) at para 38 that the equivalent category in the list of liquidation expenses could extend to post-liquidation rent.)
- Nevertheless, this still leaves category (f). The case for saying that post-administration rent should fall within (f) where the premises are retained for the purposes of the administration seems compelling.
- If this is right, then administrators must pay post-administration rent accruing in such circumstances as an expense of the administration. Neither they nor the court have any discretion to decide otherwise.
- In most cases, it will be relatively easy to determine whether premises are being retained for the purposes of the administration, the most obvious and most common situation being where the business is being continued on the premises pending sale.

Unfortunately, these (relatively) clear waters have been muddied by a Court of Appeal earlier this week - Innovate Logistics v Sunberry Properties [2008] EWCA Civ 1261.

In Innovate Logistics a landlord sought permission to bring proceedings against a tenant in administration to force the tenant to terminate a licence to occupy the premises which had been granted to a purchaser of the tenant's business. The background was a "pre-pack" arrangement under which a purchaser had been found for the business before the administration and the sale had been concluded immediately after the appointment of the administrators. The premises (which were used as a warehouse of storage of chilled foods before distribution to customers) were not included in the sale. However, the administrators had agreed to grant the purchaser a licence to occupy for 6 months to deal with the goods currently stored there and to perform current contracts with customers. This would enable collection of substantial book debts for the benefit of the tenant's creditors. Under the licence the purchaser would pay a monthly fee equal to the rent apportioned on a monthly basis which the administrators would pass directly to the landlords. This would not however put the landlord in quite as good a position as under the lease which provided for the rent to be paid quarterly in advance. Although the licence arrangement was clearly in breach of the alienation provisions of the lease, the landlord did not wish to forfeit the lease because it would not be able to re-let at the same or a better rent. Instead, it wished to force the tenant to terminate the licence in the hope that this would bring pressure to bear on the purchaser to take an assignment of the lease.

The Court of Appeal refused permission for such proceedings and its decision on this point was undoubtedly right. Such proceedings would imperil the collection of book debts for the benefit of creditors and thereby impede the purpose of the administration. Balancing the interests of the landlord who stood to suffer minimal prejudice if permission was refused against those of creditors who would suffer substantial prejudice if permission was granted, it was plainly right that permission should be refused.

However, the Court of Appeal went on to deal with an application by the landlord for an order that (in effect) the administrators should pay the full rent (rather than just the licence fees) as an expense of the administration. Under the principles explained above, one would have thought that the landlord should be entitled to such an order. However, the Court of Appeal refused such an order on the basis (see paras 56-60) that the landlord "had no automatic right to be paid the contractual amounts during the occupation of the Company in administration", that the court had "a wide discretion exercisable according to the circumstances of the case" and that, having regard to those circumstances, it would not be appropriate to require the administrators to pay the rent as an expense of the administration.

This aspect of the Court of Appeal's decision seems wrong as a matter of principle and having regard to the cases mentioned above. It may be that the explanation is simply that the court was not referred to those cases - certainly, there is no mention of Exeter or Toshoku in the judgment. Alternatively, it may be that the court placed too much reliance on the analysis in Atlantic Computers which related to old-style (pre-Enterprise Act 2002) administrations. These allowed a discretion over administration expenses whereas the new-style administrations do not. However, it is of course possible that the court intended to depart from the cases mentioned above or, at least, to add a new dimension to the debate in the form of a discretion over the amount of allowable administration expenses. So, for example, whilst the court may not have a discretion over whether payment for the continued use of the premises should be an administration expense, it does have a discretion over the appropriate level of such payment. On the facts of the case, it felt that the monthly licence fee, not the full rent, was an appropriate payment.

Whatever the explanation, this case has "set a hare running" that administrators will no doubt wish to make considerable use of in negotiations with landlords over coming months.

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