

No escape for guarantors



In February last year the decision in *Good Harvest Partnership LLP v Centaur Services Limited* indicated that once a tenant had assigned its lease, its landlord could no longer call on the former tenant's guarantor to fulfil its obligations under an authorised guarantee agreement ("AGA"), regardless of the terms of that guarantee or the surrounding commercial circumstances. This decision was followed in *K/S Victoria Street v House of Fraser*, which was subsequently appealed. Today the Court of Appeal provided clear guidance that whilst the guarantor of an assignor cannot normally guarantee the liability of an assignee, it can do so by being party to a valid AGA.

Background

When the Landlord and Tenant (Covenants) Act 1995 ("the Act") first became law on 1 January 1996, abolishing the previous privity of contract regime, there was some uncertainty about the workings of the newly-created AGA. The Act makes it clear that a tenant and its guarantor are released from liability under a lease on a valid assignment of that lease but that a landlord may require a tenant to enter into an AGA to guarantee the assignee's obligations. What was less clear was the extent to which a tenant's guarantor could validly guarantee a tenant's obligations under an AGA. However, as landlords and tenants became more comfortable with the Act they agreed deals on the assumption that this arrangement would work.

In February 2010 the High Court decided in the case of *Good Harvest Partnership LLP v Centaur Services Limited* [2010] EWHC 330 that the authors of the Act intended to release guarantors from any ongoing liabilities under the terms of the lease from the date of an assignment by the tenant, meaning that all parties had been operating under a false assumption. The Court held that any attempt to keep the guarantor on the hook by requiring it to enter into an AGA would fall foul of the Act's anti-avoidance provisions and would be void and unenforceable.

This decision was followed in *K/S Victoria Street v House of Fraser (Stores Management) Ltd and others* [2010] PLSCS 278 where the judge agreed that whilst there were difficulties with the *Good Harvest* judgment it had not been wrongly decided and should be applied to the case in question. He did not address all the issues raised by the *Good Harvest* decision, for example whether a guarantee voluntarily offered by a guarantor would be a valid way for the guarantor of an outgoing tenant to remain bound.

The judgment in *Good Harvest* has vexed both landlords (keen to understand the strength of historic guarantees) and occupiers (troubled that if they wanted weaker group companies to enter into leases, landlords now required some sort of parent company guarantee).

Today's judgment

Today's judgment by the Court of Appeal in *House of Fraser* blesses the historically common practice of an assignor's guarantor entering into an AGA for an assignee and sheds some welcome light on related issues. The Master of the Rolls and Etherton LJ preferred not to accept the purposive and commercial approach that an AGA voluntarily proffered would defeat the anti-avoidance provisions, largely because it would be too difficult to

establish whether that AGA had in fact been freely offered. Instead, they looked to the Act to find a rationale for ratifying this practice.

In brief, s.24(2) of the Act states that where a tenant is released from its covenants, a guarantor is also released "to the same extent as" the tenant. Where the tenant is only released from its obligations under the lease in so far as he is required to re-assume them under an AGA, equally the assignor's guarantor may be released from its obligations only to the same extent and may, accordingly, be required to guarantee the assignor's liability under the AGA.

"...the guarantor is released to precisely the same extent as the assigning tenant."

What this means in practice

This is a relief for landlords of the thousands of pre-*Good Harvest* leases who have looked at the whole package presented by aspirant assignees and taken comfort from the covenant strength of the tenant's guarantor renewing its obligations under an AGA. It is also a relief for landlords going forward who can again require the outgoing tenant's guarantor to sign up to an AGA.

Conclusion

This is a sensible decision. It validates the commercial reality that has evolved over the last 15 years since the Act came into force whilst being based firmly on what the Act actually says.

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