



Presented by

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# Guarantee

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# Background

- A guarantee is a common commercial arrangement where a third party, the guarantor, promises to repay the debt owed by the borrower to the lender.
  - It is a secondary liability
  - However, if the primary liability is unenforceable, it follows that there can be no claim against the guarantor as there is no debt to be guaranteed
- Therefore, it is important that **“the lender must preserve the lender’s claim against the guarantor even if the primary claim fails for some reason “**



# THE ROLE OF GUARANTORS

- Frequently contentious issue (especially if asset values fall)
- Often required by lenders so that they can access collateral security
- Difficult to release once given
- Difficult to measure (extent or number of guarantees given)
- No central registry
- Difficult to enforce if not documented & disclosed correctly

# Important Note

- Guarantee is a notoriously fragile instrument
- Unless there is a clear case against the guarantor, the claim against the guarantor is questionable – The court is favourable to the Guarantor as the guarantor receives no direct benefit from the giving of the guarantee

**“Therefore, it is essential that the lender has the correct documents to protect its interests”**



# Unenforceable Guarantee

- A guarantee given under duress or with undue influence may be unenforceable
  - When there is no commercial relationship between the borrower and the guarantor, the lender is obliged to:
    - ensure that the guarantor receives independent legal advice
    - ensure that the guarantor is fully aware of the practical implications of the proposed transaction
  - Therefore, it is essential that in practice, **lenders require that the independent adviser certifies in writing that independent advice has been given and that the guarantor is aware of the implications of giving the guarantee (as part of its mortgagee instruction)**

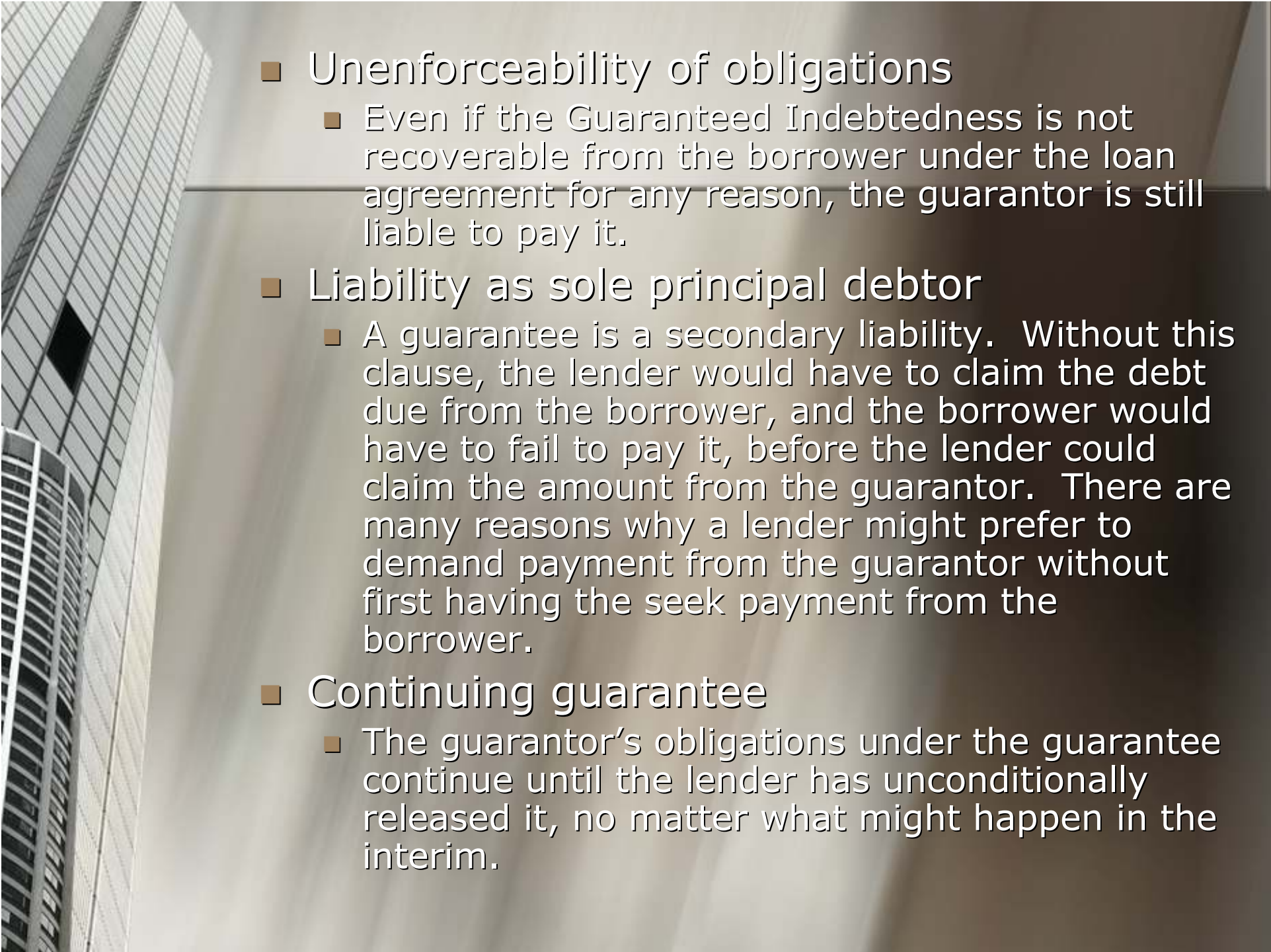
A low-angle photograph of a modern skyscraper with a grid of windows, extending from the bottom left towards the top left of the frame. The rest of the background is a dark, gradient grey.

# Independent advice

- It requires:
  - explaining the nature of the transaction
  - satisfying yourself (as the advisor) that the decision by the guarantor is their own free choice
  - ensuring that a real choice is made and that the course of action chosen is not a mere formality
- It is not clear whether this course of action will be sufficient to ensure a guarantee is enforceable if there is duress or undue influence, and is therefore not recommended.
  - Recommendation would be to get the borrower to sign:
    - (1) the waiver of the guarantee independence; and
    - (2) independent legal advice.

# Practical Terms

- Guaranteed Indebtedness
  - This is all indebtedness, present and future, of the borrower to the lender.
  - The lender should resist any limit on the amount guaranteed. This may complicate the making of further advances to the borrower and may expose the lender to loss if accruing interest and costs are not covered by the limited guarantee.
- Obligations joint and several
  - Where there is more than one guarantor, their obligations are:
    - Joint (for example, if there are two guarantors, they are obliged to pay half each); and
    - Several (notwithstanding there is more than one guarantor, each guarantor is obliged to pay the entire amount if the other guarantors do not pay their share).

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- Unenforceability of obligations
    - Even if the Guaranteed Indebtedness is not recoverable from the borrower under the loan agreement for any reason, the guarantor is still liable to pay it.
  - Liability as sole principal debtor
    - A guarantee is a secondary liability. Without this clause, the lender would have to claim the debt due from the borrower, and the borrower would have to fail to pay it, before the lender could claim the amount from the guarantor. There are many reasons why a lender might prefer to demand payment from the guarantor without first having to seek payment from the borrower.
  - Continuing guarantee
    - The guarantor's obligations under the guarantee continue until the lender has unconditionally released it, no matter what might happen in the interim.



A low-angle photograph of a modern skyscraper with a grid of windows, viewed from the side and slightly below, against a clear sky. The building's facade is composed of many small, rectangular windows, creating a repetitive pattern. The perspective is looking up and to the right, emphasizing the height and scale of the structure.

# Related issues...

- **Corporate powers and benefit**

- Corporate powers and benefit must be considered in all cases where a company is entering into a transaction. E.g. where a subsidiary company is guaranteeing its holding company's indebtedness, special consideration must be given.

- **Company**

- Where the guarantor is a company, the amount guaranteed must be assessed to determine if giving the guarantee constitutes a major transaction.

- **Financial assistance**

- Consider whether the guarantee might constitute financial assistance. This commonly arises in acquisition financing.



- **Cross-border transactions**

- Any transaction involving a jurisdiction other than New Zealand will need to be considered from the perspective of the other jurisdiction(s).

- **Insolvency issues**

- **Guarantor primary credit**

- **Generally, representations, undertakings and events of default should refer to both the borrower and the guarantor, so that an event of default will be triggered by the guarantor as well as the borrower.**



# Checklist

- Is a guarantor required?
- If yes, the guarantor must be independently advised
- The lender must give clear and unequivocal instruction to the legal adviser acting for the guarantor
- Check the authority and execution - ensure that all relevant and required steps are taken
- Is there any possibility that there may be duress or undue influence on the guarantor? Review the circumstances

A low-angle, upward-looking photograph of a modern skyscraper with a grid-like facade of windows. The building is on the left side of the frame, and the sky is a pale, overcast grey. The overall tone is professional and architectural.

# Question?

- Go over the checklist