



GUARANTEES – A GUARANTOR’S PERSPECTIVE

1. Personal guarantees are commonly requested from owners of businesses. Typically, banks or other financiers of a business require a director or shareholder to personally guarantee loans or other facilities made available to the business. Landlords also generally require a guarantee of lease obligations, and many common forms of leases (such as the Auckland District Law Society standard Deed of Lease) require personal guarantees to be provided by the directors and/or shareholders of a new tenant if a lease is assigned. It is also not uncommon for trade suppliers to require a personal guarantee to be granted in connection with the supply of product or services provided to the business.
2. There are a number of key questions which a guarantor should ask himself or herself prior to entering into any guarantee, being:
 - (a) what am I guaranteeing? Which obligations of which debtor are guaranteed?
 - (b) what is the maximum amount I am guaranteeing? Is the guarantee for a specific sum or an unlimited amount?
 - (c) what is the financial position of the debtor? Do I control the debtor, or am I only a minority shareholder and therefore others control the amount and nature of the debts which I will guarantee?
 - (d) what other security is given for the loan or other guaranteed obligation?
3. Turning to the first issue, namely the scope of the guarantee, a guarantor should consider whether the guarantee is “all moneys” or relates to a specific debt. A guarantee which relates to a specific debt is a guarantee of a particular loan or obligation. When that loan is repaid, the obligations under the guarantee will (in general terms, subject to some technical exceptions) be satisfied. In contrast, an “all moneys” guarantee is a guarantee granted by a guarantor in relation to the obligations of a debtor from time to time to a particular lender or other creditor. This means that the guarantee will relate to not just the current loan being considered, but all future loans or other obligations which may be provided by or owed to the creditor. Typically, a guarantee given by an individual to a bank in relation to a residential or business loan will be “all moneys”. Note that an “all moneys” guarantee can sometimes extend to obligations which would not usually be expected to be within the ambit of the guarantee. For example, if you granted a guarantee in relation to company X, and then company X granted a guarantee in relation to company Z, effectively you have guaranteed company Z through the chain of guarantees.
4. When granting a guarantee, consider whether the creditor will accept a dollar limit or cap on the maximum liability under the guarantee. By this mechanism, if you have granted an all moneys guarantee, you still may be able to limit your maximum liability under the guarantee. Note however that generally banks are reluctant to agree to limitations of this kind, and the availability of limitations may be influenced by how eager or otherwise the bank is to win your business.
5. Typically guarantees are joint and several. This means that the creditor can take action against any one or more guarantors for the full amount of the debt, without taking action against the other guarantors.



6. It is of course critically important for any guarantor, prior to giving any guarantee, to have a thorough understanding of the financial position of the debtor in respect of which or whom the guarantee is to be granted. By granting the guarantee, the obligations of the debtor which are guaranteed effectively become those of the guarantor. It is not uncommon for private business people to arrange their affairs so that their key assets are held in trusts, one effect of which is that if their personal guarantee is called upon, those assets in the trusts (generally speaking) are not available to satisfy the obligations under the guarantee. Note that trusts, or transfers or other dispositions to trusts, can in certain circumstances be challenged if they are established with the intention of defeating creditors.
7. If a guarantor makes payments under his or her guarantee, and satisfies the obligations under the guarantee, that guarantor will have rights of “subrogation”. That is, the guarantor then has the right to step into the shoes of the lender. In particular, the guarantor in those circumstances is entitled to sue the debtor for the amount paid under the guarantee, and also assume the security that the lender may have held (such as a mortgage).
8. Be careful to study in detail the provisions of any document that you sign. Often terms of trade from trade suppliers include guarantee provisions. For example, there may be a clause that any director that signs a particular set of terms of trade personally guarantees the obligations of the debtor. In short, personal guarantees are sometimes hidden away in the fine print of documents you may be requested to sign.
9. Also be particularly wary if you are signing a personal guarantee in relation to a lease. Typically that guarantee will also apply to any renewals of the lease. The obligations of the original tenant company will generally survive if the lease is subsequently assigned to a new tenant, so if the new tenant fails to pay the rent or outgoings, and the lease is terminated, the landlord can seek recovery from the prior tenants which assigned the lease (being the original tenant you may have guaranteed).
10. In conclusion, signing a guarantee is an action surrounded by risk, and should be considered very carefully. In particular, you should fully understand the legal and commercial risks before taking on as a personal obligation to pay the debts of a business or another person. Many business people, particularly in the current economic environment, have signed guarantees in haste and lived to regret that decision at length.

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