To Guarantee or not to Guarantee

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A guarantee by nature is a binding agreement made by a person/people (guarantor/s) to ensure that if a borrowing party (principal debtor) defaults on their loan repayments the creditor can recoup any outstanding debt from the guaranteeing party/parties.

In terms of guarantee agreements themselves the recent case of Brougham v Regan [2020] 1 NZLR 315; has interpreted the requirements for an enforceable guarantee to be a lot

more onerous then previously considered. In this case the Supreme Court stated that for a guarantee to be enforceable:

- there must be a written contract of guarantee whereby the terms the Guarantor agrees to answer for the debt, default or liability must be in writing and signed. This can be within the agreement or on a separate deed.
- all documents relating to the agreement must be executed as described (if the document is not executed by all the guaranteeing parties, the guarantee agreement as a whole is unenforceable); and
- the guarantor must sign in their capacity as guarantor (applicable where you may be signing a document in multiple capacities i.e., as director of the company and as guarantor for the loan).

These new developments are aimed to create surety, not only as to whether the party agreed to guarantee the debt, but remove any ambiguity as to the extent they agreed to be liable if a claim is subsequently made against them due to any default by the debtor. Hence why ensuring you understand the extent of any guarantee you are providing is a key prerequisite.

With this in mind it is useful to note that a common guarantee agreement is an *unlimited guarantee*. In this type of agreement the guaranteeing party becomes liable not only for the amount borrowed in the initial loan agreement, but for any further or subsequent borrowing or liabilities that the debtor may enter in the future.

To give this some real-life context, consider this scenario:

Your brother is buying a property, he has asked you to be a guarantor. You agree. Five years down the track he takes out a further loan of $35,000 for home renovations. He encounters some financial difficulty due to covid-19 impacts on his business. He defaults on his loan repayments. The bank comes after you personally to pay your brothers debt, not only for what remains outstanding on the initial home loan but also the additional $35,000 he subsequently borrowed. You are liable for the full amount as you signed an *unlimited guarantee*.

If the guarantee agreement contains an indemnity, then as guarantor you will also be liable for any costs and any losses incurred by the Guaranteed Party because of the breach by the

Debtor.

Accordingly, where possible, a limited guarantee is always recommended as it allows you to limit the amount you are liable for and the length of time you're responsible.

An agreement to guarantee any loan in any capacity should not be taken lightly and all potential risks should be considered before taking any action. Consequently, it is always advised that you should seek independent legal advice before agreeing to guarantee a loan.