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Article

Corporate Law – Guarantees, Guarantor rights and the Benefit of Discussion – July, 2018

A Guarantee is *an accessory contract by which a promisor undertakes to be answerable to the promisee for the debt, default or miscarriage of another person, whose primary liability to the promisee must exist or be contemplated.* (Halsbury's Laws of England, fourth Edition).

In the banking and commercial industry in this and other jurisdictions, often times, lenders of large sums of money seek to secure the repayment of debts owed to them by the execution of additional security in the form of a Guarantee. Ordinarily, when a principal liability is determined the guarantee itself also is determined. Until such time, the guarantor remains liable for the debts of the principal debtor. The relationship between the principal debtor and the guarantor is such that once the debt becomes due, the guarantor may, pursuant to the guarantee, pay the creditor and then make a claim against the principal debtor to indemnify him for satisfying the debt.

Given the onerous nature of a Contract of Guarantee, the law provides several 'safeguards' for individuals who guarantee debts. One such safeguard is that the Civil Code Cap 4.01 of the Revised Laws of Saint Lucia (hereinafter "the Civil Code") makes further provisions for guarantors to be protected. In the Interpretation section it states the "*Right of discussion*" is a right

with respect to property of compelling a creditor to proceed in the first instance against other property liable for the debt" and further "To discuss" is to exercise this right". For the guarantor to take advantage of this right, he must point out to the creditor certain property owned by the Principal Debtor and advance the money necessary to obtain the discussion.

The Civil Code Article 1837 thereafter states that "*The surety is liable only upon the default of the debtor, who must previously be discussed, unless the surety has renounced the benefit of discussion, or has bound himself jointly and severally with the debtor...*". Therefore, an individual that has guaranteed a debt who has not signed a guarantee stating *expressly* that he has renounced the right of discussion, must take advantage of the right of discussion when he is first sued by the Creditor. The Creditor would not otherwise be absolutely bound to discuss the principal debtor if the surety does not take this step (Article 1838).

Putting it another way, unless the guarantee *expressly* states that the Guarantor bound himself to the principal debtor in solidarity i.e. that is to be equally liable and not just in a secondary way, then he may invoke "the benefit of discussion" which compels the Creditor to exhaust recourse against the principal debtor before proceeding against



the Surety. (Commercial Lending Law, A jurisdiction-by-jurisdiction guide to U.S. and Canadian Law, Brian Hulse et al, second edition).

It is important that a Guarantor understands the onerous nature of his obligation and that he is given independent legal advice explaining the terms and conditions of a Guarantee before signing same. Albeit, this advice should enure for all types of legally binding documents.

The relationship between a surety and the principal debtor is to be contrasted from the relationship existing between multiple debtors who share a 'solidary obligation' for the debt.

In the Quebec decision of **Kingsett Canadian Real Estate income fund LP v Chateau Dollard Inc [2012 QCCS 36 (CanLII)]** the creditor in that matter sued the defendants jointly for the repayment of the debt. The debt was secured by a first mortgage and a movable hypothec. None of the evidence of the creditor supported its claim that the guarantors had waived the benefit of discussion. The Court therefore concluded that the solidarity between the debtors was not presumed and therefore there was no waiver of discussion as it was not stated expressly in any documents produced by the creditors. The Guarantors deposited a sum of \$5,000.00 to their trust attorney which was found to be sufficient to cover the costs of the discussion of the debt which totaled more than 15 million dollars.

This decision demonstrates that the Court is guided by the express terms of contracts of guarantee and this protects a surety who has

not sought to be jointly liable with the principal debtor.

This right of discussion, among other safeguards, protects a guarantor and his assets where the principal debtor owns property which has a value which exceeds the debt amount. The right of discussion is contingent on the following:

- (a) No existence of an agreed waiver of the benefit of discussion;
- (b) Indicate property within the jurisdiction that may be advanced at the first instance of being sued by the Creditor;
- (c) The surety cannot indicate property which is litigious i.e. subject to a lawsuit;
- (d) Hypothecated for the same debt but *no longer in the debtor's possession*. (The Law of Real Property, William Marler)

The Court of Quebec in the decision of **Panton v Woods II L.C.J.** (as cited by The Law of Real Property, William Marler) demonstrates how this safeguard has been applied in the Quebec. The principle to be gleaned from this decision is that for a surety to take advantage of this Defence he must advance the money necessary to obtain the discussion. The 'monies necessary to obtain the discussion' is a matter of fact to be determined by the parties. It would be reasonable to infer that the amount would be a safeguard to the creditor to sufficiently entice him to pause any action against the surety.

At the end of the day financial institutions are interested in recouping monies owed to them as a result of bad debts while suffering minimal loss. Any individual considering placing themselves in a position to guarantee



the debt of another must ensure that they have given thought to the liability that is imposed upon them should the Creditor commence action against him.

Join us next time for a discussion on other Surety safeguards!

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