Company Directors/Bank and other Guarantees

Preliminary note by Lawrence Rodkin, Partner, Simons Rodkin Litigation Solicitors, Bloomsbury London W1 and Finchley London N12.

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This is a preliminary article and is no substitute for the taking of detailed legal advice. It highlights some of the main considerations which may apply.

I would at first mention that I have been providing advice in relation to Bank and other guarantees for many years. This is both in relation to the initial giving of the guarantees and also the defence of legal claims brought under such guarantees.

It is fairly common for clients to view the required use of a solicitor by a Bank as just for the purpose of witnessing their signature. This cannot be further from the truth.
The signing of a guarantee is a serious obligation and could result in the signatory and their home address being on the receiving end of a large claim, some times in the magnitude of several hundred thousand pounds.

I have had prospective clients who have not proceeded to instruct my firm since I have provided a reasonable cost estimate for the provision of such advice. I have been unable to convince them that they should receive detailed legal advice in relation to the document, and they continue to view the exercise as just for the witnessing of their signature. This is clearly not prudent business practice.

However I would also mention that I have seen clients and based on my recommendations, protections have been built into the guarantees, and indeed some have not entered into the guarantees at all.

Accordingly my first advice is do not consider the instruction of a solicitor as simply your signature being witnessed. You are being asked to give very onerous obligations. You could be bankrupted if called upon to honour a guarantee which you cannot meet. Further, even though the guarantee is not secured it can be mortgaged upon your home address without your consent after a Court Judgement by way of a charging order.

Typically banks also require guarantees to be secured as well upon the home address of the directors with the spouse (if not a director) being asked to take independent legal advice, as the spouse is also asked to sign the charge document.

The second piece of advice is that it is possible to negotiate an upper ceiling or financial limit upon the amount of a guarantee. It is very unwise for any director to sign an open ended guarantee with no financial limit at all. The financial limit is a key part of the advice given.

Bank guarantees are standard documents but usually do contain a small number of important protection for directors. Guarantees prepared by non banking institutions may not contain these protections, and such documents should accordingly be looked at very carefully, and if appropriate amendments sought to the terms of the document.

Accordingly if you are presented with a guarantee by a non bank, it is important to instruct a lawyer to look over the document in detail and to negotiate any protections to be inbuilt into the document. One such protection is the ability for a guarantor to terminate continuing liability under the guarantee for new indebtedness, by the giving of notice to the bank or the guaranteed company. This may sound obvious however it may be overlooked in non bank guarantee documents. This is even more important if it is wished to sell the business of the debtor company by way of a share transfer- since otherwise the guarantor may be underwriting the liabilities of the business after sale.

Notification of default/the provision of information to a guarantor by the Bank/Creditor
Another matter which is obvious which is also frequently overlooked is the question of notification of default to the guarantor. Guarantors frequently are not told when an account becomes in default or

out of control. Large liabilities may be clocking up and the guarantor only finds this out when liabilities have escalated. It is important to insist upon a clause in the guarantee agreement that the bank or other company notifies the guarantor from time to time upon request in relation to the state of the account. The Bank would not normally provide such information due to Data Protection legislation. Accordingly a Data Protection authority may need to be registered with the bank or other creditor company to enable such notification to be provided.

This is a very important provision where the guarantor is not a signatory to the bank account of the debtor company and is also not involved in the day to day running of the company.

Deed of Counter Indemnity

This is also quite important. If you are asked to guarantee the liability of a company or a person and you are doing this to assist, then serious consideration ought to be given to a Deed of Counter Indemnity. If necessary this can be supported by a charge on a property or by other security. Accordingly if there is a call made under the guarantee then there will be a possibility of a personal covenant/ security for reimbursement. Although a guarantor has the right to ask for reimbursement from the debtor company if the company is insolvent then such right is fairly meaningless.

Service of demand under a guarantee

Demand made under a guarantee. The guarantee should be amended so that a very wide service clause should if necessary be changed. It is quite often there is a clause so that sending the demand to the last known home address even though the person has moved is effective service. The guarantor should always nominate or be able to nominate an address for service of a demand notice. The situation can be even worse if proceedings are issued and sent to the last known home address of the guarantor since it may be possible under rules of Court for such proceedings to be effectively served there even though the guarantor has no knowledge of the same. It is even worse if Judgement is entered in default when there is a potential defence to a claim under the guarantee. This is of key importance to ensure that any demands under the guarantee.

are served at an address where the guarantor will receive the notice. This is even of further importance if the guarantor is not resident in the UK or at some point in time ceases to be resident in the UK.

Defence of Claims under Guarantee

There are various defences which may be available. The banks and other companies do their best to avoid these defences by detailed the wording of the guarantee agreement. However if a demand is made under a guarantee then legal advice should be taken as soon as possible to see what defences if any can be raised.

Conclusion

The above are just a number of points. Every transaction is different, and will give rise to different considerations.

If the guarantee is not given to a bank, then proper advice becomes even more crucial. It is not unusual for such guarantees to be very one sided and onerous, and to omit key protections.

One final point again is that signing a guarantee with a solicitor is not just witnessing a signature. The solicitor should provide detailed and constructive advice and it is very good practice for a solicitor to write to the client afterwards summarising the main provisions of the guarantee and key elements of their advice.

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