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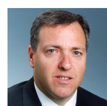
Current Trends and Issues Arising in U.S. Real Estate Transactions: Several Versus Joint and Several Liability of Guarantors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In this issue of *REF News and Views*, we will discuss the use of several versus joint and several liability of guarantors in real estate finance transactions. Of late, some borrowers have been successful negotiating several liability for sponsors under guarantees in their transactions.

Historically, if there were multiple guarantors on a matter, their liability was joint and several. The thinking for a lender was that any contribution among the parties was the sponsor's "problem" in that if there was liability caused by one or the other parties, they would work it out among themselves in their organizational documents through cross indemnities. Since it is not uncommon that various parties which constitute the sponsorship of a borrower have differing economic profiles, some parties have questioned their ability to recover against their "partner" and try to shift this risk to the lender.

When liability is joint, a lender can sue either party or both and can recover the obligation it is owed from either. The lender is receiving the joint credit of both parties. If the parties have a different percentage of liability among themselves, then if one paid more than its fair share, it would have a claim for contribution from the other and could seek recovery. The lender would not be taking on the *individual* credit risk, but would be obtaining the *joint* credit of the parties.

If the liability is several, then simply put, a lender is usually limited in its recovery against each party to the respective percentage of liability it has in the deal. So if the "joint venture" is between a "money" partner who has 90% of the deal and a "developer" or "operating" partner who has 10% of the deal, then the lender would be limited in its recovery against each such party to that respective percentage. Leaving aside the shifting of credit risk, the lender is also taking on additional litigation cost and exposure.

While there are a multitude of reasons why a lender should not or would not agree to such a shift, in reality there are instances where the identity of the parties,

leverage of the deal, overall economics of the deal and other factors persuade a lender to accept this departure from the norm.

The jury is still out as to whether this development will become the new normal. We are skeptical that it will evolve as such.

There are many ways to satisfy the concerns that one partner may have as to the financial wherewithal of its partner and, consequently, there are many reasons that a lender should not be asked to take on this additional liability. In addition, each guaranty in a transaction is different, and a payment guaranty will be approached differently than a completion guaranty, a carve-out guaranty, a carry guaranty or an environmental indemnity.

As we all know, each transaction is different and what works in one may not work in all. This development is just another “deal” term to be worked out among sophisticated parties.