

GUARANTY AGREEMENTS IN COMMERCIAL
REAL ESTATE FINANCING

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GUARANTY AGREEMENTS (GENERALLY)

- Enhance recoverability rights of lender beyond rights associated with mortgaged property.
- Guarantor is in ownership structure- Consideration for execution is benefit to mortgage borrower which ultimately benefits Guarantor.
- Types of Guaranty Agreements:
 - Full Recourse
 - Completion
 - Nonrecourse Carveout

FULL RECOURSE GUARANTIES

- Credit enhancement for unstabilized properties.
- “Absolute, irrevocable and continuing”
- Utilized primarily for “balance sheet” loans.
- What happens upon death of a warm body guarantor?
- Can you replace the guarantor?

COMPLETION GUARANTIES

- Not a guaranty of payment, but of completion of a construction project.
- Guarantor guarantees project will be completed:
 - On time;
 - In accordance with plans and specifications;
 - Within budget; and
 - Free of any liens.
- Who gets credit for undisbursed proceeds of construction loan?

NONRECOURSE CARVEOUT GUARANTIES

- Lender's recourse is only the property, except for certain "carve-out" exceptions where Guarantor may become liable.
- Recourse limited to certain actions or inactions of Borrower and Principal relating to property ("Bad-Boy/Girl Acts").
- Losses v. Full Recourse (above the line and below the line).
- Recourse limited by ability of Borrower to remain solvent? (*Cherryland Mall*)

NONRECOURSE CARVEOUT GUARANTIES (CONT.)

- Carveouts related to property type (i.e. hotels, leasehold estates and fractured condominium regimes).
- Back-Door into recourse (admission in writing, environmental agreements).
- Incentivize borrower behavior.
- Must Guarantor be related to, or otherwise affiliated with borrower?
- Should the Guarantor control the Borrower?

GUARANTIES- CASE LAW

- ***Wells Fargo Bank, N.A. v. Cherryland Mall Limited Partnership*, No. 304682, 812 N.W.2d 799 (Mich. Ct. App. 2011)**
 - Court held that the Borrower was obligated to remain solvent in order to maintain its SPE status pursuant to the express covenants in the Loan Documents requiring it to do so, and having become insolvent, the Loan became full recourse. Failure to comply with SPE covenants was a full recourse carveout.

GUARANTIES- CASE LAW

- *51382 Gratiot Avenue Holdings, LLC v. Chesterfield Development Company, LLC*, 835 F. Supp. 2d 384 (E.D. Mich. 2011).
 - The Loan Documents provided that the loan would become full recourse in the event the Borrower breached specific covenants set forth in the mortgage. One of the covenants was that Borrower shall not “fail to pay its debts from its assets.” Borrower argued that the requirement to make payments of debts was limited to “its assets” and because Borrower did not have sufficient assets, it was under no obligations to make payments. The Court rejected Borrower’s argument and held that the loan was full recourse.

GUARANTIES- CASE LAW

- ***WELLS FARGO BANK, N.A. as successor by consolidation to Wells Fargo Bank MN, N.A. as Trustee for the registered holders of Bank of America Commercial Mortgage Inc., Commercial Mortgage Pass-Through Certificates, Series 2003-2, by and through its Special Servicer, ORIX Capital v. MITCHELL'S PARK, LLC, et al., 2012 WL 4899888 (N.D.Ga.)***
 - Court denied Borrower's motion for summary judgment and held that Borrower's failure to (i) pay management fees, (ii) maintain sufficient capital, (iii) operate the business under its own name, (iv) maintain a separate office, and (v) file separate tax returns, as set forth in the separateness covenants of the Loan Documents can be cause for recourse to the Borrower (and Guarantor) and such covenants do not need to expressly be set forth in the carveout section of the Loan Documents in order to give rise to liability.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

Borrower shall be personally liable to Lender for the **Losses** Lender incurs arising out of or in connection with the following:

- material physical waste of the Property.

can create liens on any portion of the Property.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

NEGOTIATED PROVISION

Borrower shall be personally liable to Lender for the **Losses** Lender incurs arising out of or in connection with the following:

- material physical waste of the Property **caused by acts or omission of Borrower; provided, however, there shall be no liability for physical waste if such occurs during a time when there was insufficient available cash flow to prevent such waste.**

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

Borrower shall be personally liable to Lender for the **Losses** Lender incurs arising out of or in connection with the following:

- failure to pay charges for labor or materials or other charges or judgments that can create liens on any portion of the Property.

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NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

NEGOTIATED PROVISION

Borrower shall be personally liable to Lender for the **Losses** Lender incurs arising out of or in connection with the following:

- failure to pay charges for labor or materials or other charges or judgments that can create liens on any portion of the Property; **provided, however, unless Borrower incurred such charges after the occurrence and during the continuance of an Event of Default, there shall be no liability for such failure to pay if it occurs during a time when there was insufficient available cash flow to prevent such failure to pay.**

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

Borrower shall be personally liable to Lender for the **Losses** Lender incurs arising out of or in connection with the following:

- (i) the misappropriation, misapplication or conversion by Borrower of any Rents following an Event of Default or
- (ii) any Rents paid more than one month in advance.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

NEGOTIATED PROVISION

Borrower shall be personally liable to Lender for the **Losses** it incurs arising out of or in connection with the following:

- (i) the misappropriation, misapplication or conversion by Borrower of any Rents following an Event of Default (provided, however, that the application of Rents to reasonable and customary Operating Expenses or to Extraordinary Expenses approved by Lender in accordance with this Agreement shall not be considered misapplication, misappropriation or conversion) or (ii) any Rents paid more than one month in advance.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

Borrower shall be personally liable to Lender for the **Losses** Lender incurs arising out of or in connection with the following:

- the gross negligence or willful misconduct of Borrower.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

NEGOTIATED PROVISION

Borrower shall be personally liable to Lender for the **Losses** Lender incurs arising out of or in connection with the following:

- the gross negligence or willful misconduct of Borrower; provided, however, Borrower's failure to perform any obligation under the loan documents shall not be construed as gross negligence or willful misconduct if Borrower is required to expend any sum of money in order to perform the obligation in question and there was insufficient available cash flow to allow Borrower to perform the obligation.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

The debt shall be fully recourse to Borrower in the event of:

- Borrower filing an answer consenting to or otherwise acquiescing in or joining in any involuntary petition filed against it, by any other Person under the Bankruptcy Code or any other Federal or state bankruptcy or insolvency law.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

NEGOTIATED PROVISION

The debt shall be **fully** recourse to Borrower in the event of:

- Borrower filing an answer consenting to or otherwise acquiescing in or joining in any involuntary petition filed against it, by any other Person under the Bankruptcy Code or any other Federal or state bankruptcy or insolvency law; provided, however, Borrower may acquiesce or file an answer consenting to any such action if brought by Lender.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

The debt shall be fully recourse to Borrower in the event of:

- Borrower making an assignment for the benefit of creditors, or admitting in writing or in any legal proceeding, its insolvency or inability to pay its debts as they become due.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

NEGOTIATED PROVISION

The debt shall be fully recourse to Borrower in the event of:

- Borrower making an assignment for the benefit of creditors, or admitting ~~in writing~~ in any legal proceeding, its insolvency or inability to pay its debts as they become due.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

The debt shall be fully recourse to Borrower in the event of:

- if Borrower fails to maintain its status as a Special Purpose Entity or comply with any of the Special Purpose Entity representations, warranties or covenants contained in the Loan Documents.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

NEGOTIATED PROVISION

The debt shall be fully recourse to Borrower in the event of:

- if Borrower fails to maintain its status as a Special Purpose Entity or comply with any of the Special Purpose Entity representations, warranties or covenants contained in the Loan Documents and such failure is cited as a factor in connection with a substantive consolidation of the assets or liabilities of Borrower with those of any other Person.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

The debt shall be fully recourse to Borrower:

- if Borrower fails to obtain Lender's prior written consent to any additional indebtedness.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

The debt shall be **fully** recourse to Borrower:

- if Borrower fails to obtain Lender's prior written consent to any additional indebtedness (other than indebtedness expressly permitted by this Agreement);
- How are trade payables addressed?

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

The debt shall be fully recourse to Borrower:

- If Borrower shall fail to obtain Lender's prior written consent to any Transfer as required by the Loan Documents.

NONRECOURSE CARVEOUT GUARANTIES- COMMON CARVEOUTS

STANDARD PROVISION

The debt shall be fully recourse to Borrower:

- If Borrower shall fail to obtain Lender's prior written consent to any ~~transfer as required by the Loan Documents~~ Transfer unless such Transfer is permitted by the Loan Documents.
 - Involuntary "Transfers"
 - Transfers of beneficial ownership interests in Borrower
 - Leases