

Are Guarantors penalised more heavily than the Borrower in case of the Borrower's Default?

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Guarantors are key elements of many loans – they reduce the need for borrowers to provide collaterals while still giving creditors security of repayment, sometimes by offering their own assets as security for the loans granted to the borrowers. While creditors may choose to seek repayment directly from the guarantor in case of the borrower's default by, amongst others, enforcing a mortgage taken out against the guarantor's property, should courts still consider whether there is a reasonable prospect that the guarantor may be able to redeem the mortgage in full before enforcing the mortgage against him?

The High Court and the Court of Appeal considered this question in *Pereira, Dennis John Sunny v United Overseas Bank Ltd* [2017] SGCA 62 (Pereira) and the Court of Appeal ultimately held that it would have jurisdiction to grant a stay of execution of an order for possession under a mortgage against a guarantor if there is a reasonable prospect that the guarantor would be able to redeem the mortgage in full. The effect of this decision is to accord parallel treatment to both the borrower and the guarantor in terms of the enforcement of mortgages against them, thereby upholding fairness to the guarantor and preserving the commercial viability of providing guarantees.

Below, we explain (A) facts of the Pereira case, (B) the difference in the approach taken by the High Court and the Court of Appeal and (C) the commercial implications of these two decisions.

A. Facts of the Pereira Case

The United Overseas Bank Ltd (UOB) granted loan facilities to a company (Borrower) which was majority-owned by Mr Pereira. The loan facilities were secured by personal guarantees provided by Mr Pereira (the Guarantor), whose liability under those guarantees was in turn secured by a mortgage over his properties. Subsequently, the Borrower defaulted on the repayment under the loan facilities.

UOB then applied to the court for an order that the Guarantor deliver possession of the properties, which was granted on 24 August 2016 and stayed until 30 November 2016 with respect to one of the properties (the Property). However, even so, the Guarantor could not deliver possession of the Property on the scheduled date.

Therefore, the Guarantor applied for a stay of execution of the order “until 31st March 2017 or such earlier time that the [company's shares] [are] sold or otherwise dealt with, with liberty to apply for an extension if an impending sale is in the midst of completion”.

The Guarantor argued that the stay should be granted as there was a reasonable prospect that the Borrower would be able to repay its debt to the UOB soon with a fresh injection of funds into the Borrower if the prospective offer for the acquisition of its shares went through. The Guarantor's application was dismissed by the Assistant Registrar, whose decision was upheld on appeal to the High Court. The Guarantor then appealed to the Court of Appeal.

B. Difference in the approach taken by the High Court and Court of Appeal

The High Court dismissed the Guarantor's application for a stay of execution on three grounds:

1. Since UOB did not have to enforce the debt against the Borrower before seeking remedies against the Guarantor, it was irrelevant whether there was a reasonable prospect that the Borrower would be able to repay its debt to UOB.
2. The High Court distinguished an earlier case, *Hong Leong Finance Ltd v Tan Gian Huay and another* [1999] 1 SLR(R) 755, on the basis that it dealt with the direct enforcement of security between a borrower and a creditor, where the borrower was given a short reprieve to satisfy his debt if there was a reasonable prospect of him doing so. However, there was no legal basis for a guarantor to require a creditor to wait for the borrower's repayment before enforcing against him due to a reasonable prospect of such repayment. Otherwise, the commercial value of a guarantee would be defeated.
3. In any case, there was no evidence of a reasonable prospect of the company in satisfying its debt to UOB.

While the Court of Appeal affirmed the High Court's decision not to grant the Guarantor a stay of execution, it did so on a different ground. Specifically, the Court of Appeal rejected both the first and second grounds of the High Court's decision. While a creditor may elect whom to enforce the debt against, once he has so chosen and the enforcement involves the realisation of a mortgage, the court may stay the execution of an order for possession by the creditor for a short period of time if there is a reasonable prospect of the mortgagor redeeming the mortgage in full. The court may grant the stay irrespective of whether the mortgagor is the borrower or the guarantor.

However, the Court of Appeal ultimately held that while a stay of execution could in principle be granted in favour of the Guarantor, the stay was not granted on the basis that the short reprieve had already been spent.

C. Commercial Implications

The Court of Appeal's approach to grant a short reprieve to both the borrower and the guarantor prior to the enforcement of mortgage against them on the ground of reasonable prospect of the mortgagor redeeming the mortgage in full is a fair one since there is no reason why the treatment of the mortgagor should differ depending on the mortgagor's identity, and *a fortiori*, no worse treatment for the guarantor.

This should be the case so that the commercial attractiveness of guarantees as a security mechanism is not over-enhanced to the point where a creditor is incentivised to constantly look to the guarantor first instead of the borrower due to the relative ease of enforcing the mortgage against the guarantor vis-a-vis the borrower.

This will prevent the scales from being tipped too much in favour of the borrower, thus mitigating issues of potential unfairness to the guarantor of having the mortgage enforced against him, possibly to the point of his bankruptcy, while the borrower may be fully solvent and yet possibly the sole beneficiary of the loan. In such case, the commercial viability of providing guarantees as a form of security will also be preserved in the eyes of potential guarantors.

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Your Key Contacts



Doreen Sim

Senior Partner, Singapore

D +65 6885 3697

doreen.sim@dentons.com



Yin Wei Lee

Partner, Singapore

D +65 6885 3649

yinwei.lee@dentons.com