The Enforceability of Waiver of Defense Provisions in Guaranty Agreements

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It has been said that a guarantor is a fool with a pen. Even the Bible warns, “whoever puts up security for a stranger will surely suffer, but whoever refuses to shake hands in pledge is safe.” Proverbs 11:15, NIV. That notwithstanding, guaranty agreements have been a part of recorded civilization since 2750 BC in Mesopotamian society. Guaranties were even included in the Code of Hammurabi in 1792 BC.

It can be assumed that throughout this long history of guaranty agreements, guarantors have never been excited about paying the debt of another following a default. In fact, over the years dozens of defenses have been raised to avoid paying on a guaranty. These defenses include, but are not limited to the following:

- No Meeting of the Minds
- No Consideration
- Statute of Frauds
- Statute of Limitations
- Conditions Precedent to Liability
- Express Limits on the Scope of the Guaranty
- Revocation of Continuing Guaranty
- Failure to Give Notice of Debt
- Failure to Give Notice of the Borrower’s Default
- Failure to Convey Adverse Information
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- Special Disclosures to Consumer Guarantors
- Material Alteration of the Underlying Debt
- Impairment of Collateral
- Failure to Notify the Guarantor of a Foreclosure Sale
- Failure to Hold a Commercially Reasonable Foreclosure Sale
- Release of Co-Guarantors
- Negligent Administration of the Loan
- Duty to Pursue the Borrower First
- Absence of Default by the Borrower
- Borrower Defenses on the Underlying Debt

In response to this panoply of defenses that delayed and potentially frustrated a lender’s ability of collect on a guaranty, provisions waiving the ability of a guarantor to assert these defenses were included in guaranty agreements. Not to be dissuaded, guarantors have forged ahead with their defenses and have attacked the enforceability of the provision waiving those defenses. Recently, the Colorado Court of Appeals was faced with just such an attack in *Community Banks of Colorado v. Landy*, 16CA1806, July 27, 2017. In this decision the Colorado Court of Appeals analyzed the waiver of defense provision in the guaranty and upheld its enforceability.

Specifically, the guaranty at issue in the Landy case included the following waiver of defenses provision:

GUARANTOR’S WAIVERS. Guarantor also waives any and all rights or defenses based on suretyship or impairment of collateral including, but not limited to, any rights or defenses arising by reasons of (A) any “one-action” or “anti-deficiency” law or any other law which may prevent Lender from bringing any action, including a claim for deficiency against Guarantor, before or after Lender’s commencement or completion of any foreclosure action, either judicially or by exercising of a power of sale;...[C] any disability or other defense of Borrower, of any other guarantor, or of any other person, or by reason of cessation of Borrower’s liability from any cause whatsoever, other than payment in full legal tender, of the indebtedness;...[F] any defenses given to guarantors at law or in equity other than actual payment and performance of the Indebtedness...

Guarantor warrants and agrees that each of the waivers set forth above is made with Guarantor’s full knowledge of its significance and consequences, and that, under the circumstances, the waivers are reasonable and not contrary to public policy or law.
The guarantor in the Landy case argued that the waiver clause was unenforceable because (1) it was drafted and presented as an adhesion instrument; (2) it was "inconspicuous," and "buried in tiny text"; (3) it lacked meaningful notice of the protections being waived; and (4) it stripped the guarantors of their critical legislative rights. The Colorado Court of Appeals rejected each of these arguments. Initially, the Court recognized that commercial parties are free to negotiate and bargain away rights as part of a financing transaction. Further, the Court emphasized that the guarantor in this particular matter was a commercial real estate developer and was not an unsophisticated party. Accordingly, the Court found no public policy reason to prevent the enforcement of the waiver of defenses.

The Court then considered the argument that the waiver was "inconspicuous," and "buried in tiny text." It found that, "the clause is capitalized and is title “GUARANTOR’S WAIVERS,” it is in the same type face and font as the remainder of the commercial guaranty, it is part of a two-and-one-half page document, and it is separated by additional spaces from the preceding paragraph, thereby creating visual separateness from the remainder of the document." Landy at p. 15. Finally, the Court observed that the guarantor had initialed each of the waiver clauses in the multiple guaranty agreements that had been signed thereby indicating he had signed and understood the waivers.

The Court concluded that guaranty contracts containing waiver of defense clauses are widely used in the banking industry and that "absent language expressly prohibiting the waiver" public policy favors the right to enter into contracts that limit or extinguish rights that confer a right or benefit to one or both parties. Based upon its analysis of the enforceability of the waiver of defense provision, the Court of Appeals upheld the trial court’s entry of summary judgment in favor of the Bank. Therefore, in the context of a commercial guaranty, the terms of a waiver of defense provision should be enforceable if drafted within the guidelines discussed by the Court in this particular case.

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