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UPDATE:
TENNESSEE SUPREME COURT REVERSES LOWER COURT RULING THAT INITIATION OF FORECLOSURE IS "INCREASE IN HAZARD" UNDER INSURANCE CONTRACT

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In a recent decision, the Tennessee Supreme Court reversed a Court of Appeals ruling holding that a mortgagee is required to give notice of the commencement of foreclosure proceedings to an insurer as such proceedings constitute an "increase in hazard" under both the standard mortgage clause in an insurance policy and Tennessee Code § 56-7-804.[2] In reversing this holding, the Supreme Court found that the plain and ordinary meaning of the term "increase in hazard" does not include an increase in a moral hazard, such as the commencement of foreclosure proceedings. Thus, failure to notify the insurer of the initiation of foreclosure proceedings will not invalidate a mortgagee's protection under an insurance policy absent a clear contractual provision to the contrary. *U.S. Bank, N.A. v. Tenn. Farmers Mut. Ins. Co.,* No. W2006-02536-SC-R11-CV, 2009 WL 199856 (Tenn. Jan. 29, 2009).

U.S. Bank, N.A. ("U.S. Bank") held a mortgage on certain residential real estate. The mortgagor obtained a Personal Fire and Extended Coverage Insurance Policy (the "Policy"), listing U.S. Bank as mortgagee, from Tennessee Farmers Mutual Insurance Company ("Tennessee Farmers"). The Policy contained a standard mortgage clause (the "Clause"), under which Tennessee Farmers agreed to protect U.S. Bank's interest in the insured property and that such protection would not be cancelled due to, among other things, an increase in hazard of which U.S. Bank was unaware. In return for this protection, the Clause required U.S. Bank to notify Tennessee Farmers of any increase in hazard of which U.S. Bank did have knowledge. Nothing in the Policy specifically required U.S. Bank to notify Tennessee Farmers of the commencement of foreclosure proceedings against the mortgagor.

After the mortgage went into default, U.S. Bank initiated foreclosure proceedings and notified the mortgagor of such through various letters sent by both U.S. Bank and its attorneys. Tennessee Farmers was not so notified. The foreclosure proceedings were stayed after the mortgagor filed for bankruptcy and were never completed. The house was destroyed by fire approximately six months later.

U.S. Bank subsequently submitted a claim to Tennessee Farmers under the Policy, and Tennessee Farmers refused to pay. Following this refusal, U.S. Bank filed a lawsuit against Tennessee Farmers alleging, among other things, breach of contract and arguing that Tennessee Code § 56-7-804 (the "Statute") prohibited Tennessee Farmers from refusing to pay U.S. Bank's claim based on the occurrence of foreclosure. The Statute contains almost identical language to the Clause. The trial court granted U.S. Bank's motion for partial summary judgment as to the effect of the Statute. The Court of Appeals

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[2] An article on the Tennessee Court of Appeals opinion in this case appeared in December 2008's edition of the ABA Real Property, Trust and Estate Law Section *eReport*.

reversed the trial court, holding that the initiation of foreclosure proceedings constituted an increase in hazard under both the Clause and the Statute such that U.S. Bank's failure to notify Tennessee Farmers of the foreclosure proceedings constituted grounds for invalidation of the Policy. The Tennessee Supreme Court agreed to hear U.S. Bank's appeal of the Court of Appeal's decision.

On appeal, the Court began its analysis of both the Clause and the Statute by setting out the general rule that, in the absence of ambiguity, the terms of a contract and the language of a statute should be given their plain and ordinary meaning. *U.S. Bank*, 2009 WL 199856 at *3. The Court then addressed the specific issue of whether the commencement of foreclosure proceedings was an "increase in hazard" of which U.S. Bank was required to provide notice to Tennessee Farmers or risk invalidating its coverage under the Policy. *Id.* at *4-*5. In reviewing similar cases from other jurisdictions, the Court found that other courts have generally held that foreclosure proceedings alone do not constitute the type of increase in hazard that requires notice to the insurer by the mortgagee. *Id.* at *5-*6. Courts have typically reached a different result only where the insurance contract specifically requires the mortgagee to provide notice of foreclosure proceedings to the insurer. *Id.* at *6. Based on those cases, the Court concluded that the plain and ordinary meaning of the Clause did not require U.S. Bank to provide notice of the initiation of foreclosure proceedings to Tennessee Farmers. *Id.* The Court observed that requiring such notice, in the absence of a specific foreclosure notice provision, would be the equivalent of the Court's rewriting the Policy, which is not an appropriate judicial function. *Id.* at *7. Therefore, U.S. Bank's failure to provide notice of the initiation of foreclosure proceedings to Tennessee Farmers did not void the Policy for failure to provide notice of an increase in hazard. *Id.*

As the language of the Statute parallels that of the Clause and creates the same protections and obligations, the Court found there to be no substantive difference between the two and found no reason to construe the two differently. *Id.* at *8. As with the Clause, the Court held that the plain and ordinary meaning of the phrase "increase in hazard," as used in the Statute, does not include moral hazards, which are increases in the risk that the mortgagor will destroy the insured property with the intention of collecting the insurance proceeds. *Id.* at *9. The commencement of foreclosure proceedings is one such moral hazard. *Id.* Rather, increases in hazard under the statute include only physical hazards, which are changes in the use or physical condition of the insured property that increase the risk assumed by the insurer. *Id.* Just as the Court declined to judicially rewrite the Policy, it also declined to amend the Statute judicially by expanding the plain and ordinary meaning of the phrase "increase in hazard" to include moral hazards. *Id.* Thus, a mortgagee is not required by either the Statute or a standard mortgage clause to provide notice to an insurance company of the commencement of foreclosure proceedings in the absence of a specific policy provision to the contrary. *Id.*

Although the Tennessee Supreme Court ruled favorably for the mortgagee in this case, the lower court's ruling cites decisions from other jurisdictions supportive of that court's position. Whether this latest Tennessee decision will inspire insurance companies to include language in their polices specifically identifying commencement of foreclosure as an "increase in hazard" remains to be seen. Where a provision in the insurance contract clearly identifies foreclosure as an increase in hazard, a casualty occurring during an unreported foreclosure may not be covered. Mortgagees should recognize that various circumstances may impair their casualty coverage and provide written notice of known circumstances which fall or may fall within the category of an "increase in hazard" to the insurance company.

"SPRINGING RECOURSE" GUARANTIES ENFORCED IN RECENT DISTRICT COURT OPINIONS: WILL THE TREND CONTINUE? SHOULD *IN TERROREM* PROVISIONS BE ENFORCED?

by James H. Wallenstein[1]
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This article updates two excellent papers that have recently been presented by RPTE eReport Real Property Editor Cheryl Kelly.[2] In fact, the impetus for this article is my having requested an update from Editor Kelly and then "volunteering" when she suggested that I perhaps provide for eReport an analysis of the two cases to which she alerted me in her update.

<u>Two Recent District Court Opinions on the Topic of "Springing Recourse"</u>

111 Debt Acquisition LLC v. Six Ventures, Ltd. et al., No. C2-08-768, U.S. District Court, S.D. Ohio, Eastern Division, Opinion and Order dated February 18, 2009, and published at 2009 WL 414181. In November 2006 Six Ventures, Ltd. refinanced six apartment projects with a $20,900,000 mortgage loan. The mortgage loan was non-recourse, meaning that the mortgagee could not pursue the borrower for a deficiency judgment after foreclosure; however, a guaranty executed by three guarantors provided that although their initial status with regard to the loan was also non-recourse, their status would convert to a full-recourse liability for the entire loan balance upon a "Springing Recourse Event," one of which was the borrower's filing for bankruptcy. In September 2008, after having defaulted in its mortgage payments, Six Ventures, Ltd. filed for bankruptcy. In October 2008 the bankruptcy court granted the mortgagee relief from the automatic stay, thus allowing the mortgagee to proceed with foreclosure against the properties. The borrower's bankruptcy filing, though, prompted the mortgagee to sue the guarantors for the full balance of the $20,900,000 loan, claiming that the bankruptcy filing was a "Springing Recourse Event" under the guaranty. In an Opinion and Order dated February 18, 2009, the District Judge in the *Six Ventures, Ltd.* litigation granted the mortgagee's motion for partial summary judgment, holding that the guarantors were liable for the full balance of the $20,900,000 loan. In his opinion the District Judge analyzed (i) whether or not the "Springing Recourse Event" provision in the guaranty and other loan documents was clear (in a quite extensive analysis, he found that it was clear), (ii) whether the mortgagee had followed proper trial procedure (he found that the mortgagee had done so), and (iii) whether the guaranty provision violated public policy by discouraging debtors from filing for bankruptcy protection (he found that it did not violate public policy). However, the District Judge's Opinion and Order contains no discussion of whether the springing recourse provisions, which in this instance would cause the guarantors' liability to increase from zero to an amount approaching $20,900,000, might have prescribed an unenforceable "penalty" since the effect of the borrower's prohibited action appears to have resulted in nothing more than an approximately one-month delay in the mortgagee's foreclosure process.

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[2] Kelly, *Real Estate Work-Outs: Running Dry in the Liquidity Crunch?* June 19, 2008 Telephone Seminar/Audio Webcast sponsored by the American College of Real Estate Lawyers, printed at the following internet web page: http://files.ali-aba.org/thumbs/datastorage/skoobesruoc/pdf/TSNR01_chapter_02_thumb.pdf , which in turn updates Kelly, *Enforcement of Guaranties Including Carve Outs from Recourse Liability and Springing and Exploding Guaranties*, ACREL Fall 2007 Meeting presentation.

Compare *FDIC v. Prince George Corporation*, 58 F.3d 1041 (4th Cir. 1995), which was decided under a different form of limited guaranty provision, i.e., so-called "carve-out" liability for actual losses instead of springing liability on the entire loan amount, and which shows that a court can determine the actual loss that a lender incurs when the borrower violates the no-bankruptcy provisions in loan documents.

CSFB 2001-CP4 Princeton Park Corporate Center, LLC vs. SB Rental I, LLC, et al., No. L-7224-06, Superior Court of New Jersey, Law Division, Middlesex County, unpublished transcript of an oral opinion and order issued March 28, 2007 (supplied to me courtesy of Cheryl Kelly). This still-pending litigation involves a $13,300,000 non-recourse mortgage loan to SB Rental I, LLC, subject to the possibility of springing recourse liability for the full $13,300,000 loan amount being imposed on one or more guarantors (the style of the case includes “et al” and both the style and the District Judge’s opinion refer to the plural “defendants”) in the event that SB Rental I, LLC placed any subordinate financing on the property. SB Rental I, LLC did place subordinate financing on the property, and in his March 28, 2007 opinion the District Judge held that the loan was therefore fully recourse to the guarantor(s). In addition to a discussion in the District Judge’s opinion of whether the springing recourse provision was clear (he held that it was clear), the opinion also included a discussion of whether having the guarantor’s(s’) liability increase from zero to $13,300,000 due to the borrower’s placing a subordinate financing on the property might have prescribed an unenforceable penalty. However, the court did not analyze whether the mortgagee had suffered any actual damages from the subordinate financing (in most states the foreclosure of a superior lien wipes out a subordinate lien), but instead pointed out that the “defendants” -- plural -- “received and retained $13.3 million in loan proceeds” and that the imposition of $13,300,000 liability on the guarantors for the borrower’s subordinate financing was “actual damages” because: “In fact, the damages which the plaintiff seeks are equal to the outstanding loan balance and nothing more.” The District Judge did not attempt to distinguish between damages caused by the borrower’s failure to pay the loan (which was not a springing recourse event) and damages caused by the borrower’s subordinate financing.

<u>A Trend in Enforcing Springing Recourse Provisions and the Presumed Rationale for Such Enforcement</u>

During the past several years, other reported cases in addition to the two cases discussed above have enforced springing recourse loan provisions. See, in reverse chronological order: *Blue Hills Office Park LLC v. JP Morgan*, 477 F. Supp. 2d 366 (D. Mass. 2007); *LaSalle v. Mobile*, 367 F. Supp. 2d 1022 (E.D. La. 2004); *Heller Financial v. Lee*, 2002 U.S. Dist. LEXIS 15183 (N.D. Ill. August 12, 2002); and *First Nationwide Bank v. Brookhaven Realty Association*, 637 N.Y.S. 2d 418 (N.Y. App. 1996). See also three excellent recent articles on the subject, all of which are located on readily accessible internet web pages: Kelly, *Real Estate Work-Outs: Running Dry in the Liquidity Crunch?* http://files.ali-aba.org/thumbs/datastorage/skoobesruoc/pdf/TSNR01_chapter_02_thumb.pdf (June 2008); Kuney, *"Springing Guarantee" Fully Enforced in Non-recourse Mortgage Loan: for Borrower's Loan Breaches Including the Failure to Comply with Separateness Covenants*, www.sidley.com/db30/cgi-bin/pubs/Bankruptcy_Update_08.20.07.pdf (August 2007); and Murray, *Carveouts to Nonrecourse Loans: They Mean What They Say!* http://www.firstam.com/content.cfm?id=2920 (2007).

As was the case in the *Six Ventures, Ltd.* opinion, in most of the above-cited court opinions the judge failed to consider the “penalty” issue at all in his opinion. Generally implied, if not always expressed, in the opinions was a rationale similar to the following: (i) the lender made a loan, and a borrower customarily has liability for repaying a lender’s loan; (ii) in the particular loan in question the lender made a unique exception, granting the borrower and its guarantor(s) exculpation from the repayment obligation if, but only if, the borrower “kept its end of the bargain” by refraining from the specified springing recourse activities; (iii) since the borrower did not so refrain, the borrower and the guarantor(s) were not entitled to the lender’s unique exception, and the customary obligation of repayment returned.

This Author's Analysis and Conclusion[3]

It is the opinion of this author that the business dialogue in most mortgage loan transactions does not follow the rationale that was set out in the immediately preceding paragraph. Instead, the business dialogue generally follows a format such as the following:

> Borrower (before any loan commitment is issued): "The loan is a non-recourse loan, right?"
> Lender: "Yes, that's the deal."
> Borrower (after receiving the lender's loan commitment): "I see the paragraph that says the loan is non-recourse, but it mentions something about your customary carve-out provisions. What are those?"
> Lender: "Don't worry about that; it's just our legal department's standard stuff. Your lawyer can work out the language with our lawyer in the final loan documents."
> Lender's Lawyer to Borrower's Lawyer (during document negotiations): "The commitment says the documents will contain our customary carve-out provisions, and the springing recourse paragraph is standard for us. I don't have the authority to delete it. Just tell your client not to do anything that is prohibited by the paragraph, and there won't be any problem."

While no research has been done other than the author's recollection of his professional experience during the past 38 years to justify the above-quoted scenario, the author believes that a polling of lenders and borrowers about their pre-commitment and contemporaneously-with-commitment verbal dialogue would reveal scenarios very similar to what is quoted above. And, more importantly, the author believes that not a single lender would have answered the borrower's first question in the above scenario with an analysis similar to what was set out in the paragraph of this article that precedes the scenario. Similarly, it is this author's belief that if lenders were polled about why springing recourse provisions are included in their loan documents, not a single one would say that the principal purpose of the springing recourse provisions was to give the lender full-recourse remedies. Instead, they would say that such springing recourse provisions are included to make it prohibitive for the borrower to act improperly -- what some courts and commentators refer to as ***"in terrorem"*** clauses, i.e., clauses whose primary purpose is to place the borrower ***in terror*** against performing the proscribed action. This conclusion is corroborated by occasional references in speech presentations where the speaker uses the term "***in terrorem***" to describe the springing recourse provisions, such as Barton, *Carveouts, Deficiencies, and In Terrorum* [sic] *Clauses*, 2004 Texas Mortgage Lending Institute.

Other than perhaps in the context of will contests, *in terrorem* provisions are not favored by courts. For example, in the case of *Muller v. Light*, 538 S.W.2d 487 (Tex. Civ. App. -- Austin 1976), the court characterized a purported liquidated damages provision in a construction contract to be "an ***in terrorem*** device to insure prompt performance by the builder" and, accordingly, an unenforceable penalty. Similarly, in *Raffel v. Medallion Kitchens of Minnesota, Inc.*, 139 F.3d 1142 (7th Cir. 1998), the court found a purported liquidated damage provision in a lease to be an unenforceable penalty and, in doing so, favorably quoted the following language from a 1915 opinion from the Illinois Supreme Court: ". . . if it [the damage clause in a contract] appears to have been inserted to secure the prompt performance of the agreement, it will be treated as a penalty and no more than actual damages can be recovered." 139 F.3d at 1146. The same court later cited its *Raffel* opinion favorably and described the basis for its decision with essentially the same language in its opinion in *Checkers Eight Limited*

[3] This would be a good time to reemphasize the disclosure and disavowal that is stated in footnote 1 above: (1) the author's clients are predominantly real estate developers and investors, i.e., not mortgage lenders; and (2) the author's comments are solely his personal observations and conclusions, and they in no way represent the views of his law firm or any clients of his law firm.

Partnership v. Hawkins, 241 F.3d 558, 562 (7th Cir. 2001), in holding unenforceable a stipulated fee for failing to make a settlement payment within the prescribed time period. Accord: *In re Dow Corning Corp.*, 419 F.3d 543 (6th Cir. 2005) and *MCA Television Limited v. Public Interest Corporation*, 171 F.3d 1265, 1271 (11th Cir. 1999), which opinions are listed in support of the following statement in 24 WILLISTON ON CONTRACTS, page 249: "Accordingly, a specified sum that is unreasonably large when compared to the damage that could have been anticipated from the breach of the contract, and therefore punishes the breach, is a penalty, as is a sum which is designed to or has the effect of coercing performance of the contract by making the breach so expensive that it forces adherence to the contract."

For a sampling of real estate related court opinions in the author's State of Texas on the issue of penalty versus liquidated damages, see *Flores v. Millennium Interests, Ltd.*, 185 S.W.3d 427 (Texas Supreme Court 2005) (characterizing as an unenforceable penalty a statutory "liquidated damage" provision in connection with a contract for deed); *Stewart v. Basey*, 245 S.W.2d 484 (Texas Supreme Court 1952) (characterizing as an unenforceable penalty a liquidated damage provision in a lease agreement); *Tri-Cities Construction, Inc. v. American National Insurance Company*, 523 S.W.2d 426 (Tex. Civ. App.--Houston [1st Dist.] 1975, no writ), appeal after remand, 551 S.W.2d 106 (Tex. Civ. App.--Houston [1st Dist.] 1977, no writ) (holding a mortgage loan commitment fee to be an unenforceable penalty); *Ashton v. Bennett*, 503 S.W.2d 392 (Tex. Civ. App.--Waco 1973, writ ref'd n.r.e.) (holding an earnest money deposit in a real estate contract of sale to be an unenforceable penalty). See also, among many other sources, the following general analyses on the subject: RESTATEMENT OF THE LAW (SECOND) OF CONTRACTS (1981), pages 157-61, § 356 ("Liquidated Damages and Penalties"); and 24 WILLISTON ON CONTRACTS, pages 248-57, §§ 65:3 and 65:4 ("Distinction between penalties and liquidated damages").

It is the opinion of this author that court opinions referring to the springing full liability as being "actual damages" [Excerpt from the *SB Rental I, LLC* opinion: "In fact, the damages which the plaintiff seeks are equal to the outstanding loan balance and nothing more."] mistakenly confuse the damages caused to the lender by the borrower's failure to repay the loan (which is not a recourse event and, in fact, is generally the basis for the non-recourse exculpatory language) with the damages caused to the lender by the borrower's taking an action that is proscribed in the springing recourse provision. It is also the author's opinion that the judges' opinions in cases such as the two that precipitated this report often reflect an impatience on the part of the judges with the certain specific prior actions or court arguments of the respective defendants. This author predicts a different line of reasoning, i.e., with a thorough analysis of the "penalty" aspect of *in terrorem* clauses, in a future appellate court decision. And this author would especially predict a court's rejection of the springing recourse remedy in the event of litigation involving a guarantor whom the judge does not suspect of having drained the property of cash but instead has merely succumbed to an economic downturn, who has not attempted to delay the lender's foreclosure, and who is now being sued by the lender for the entire loan balance on account of a specified springing recourse action that caused little or no expense to the lender, such as, for example, a prohibited transfer of an insignificantly small, non-controlling limited partner's interest (and for this example, not the interest of the guarantor) or a violation of one of the "single purpose entity" provisions by the borrower's having occasionally used the wrong forms for obtaining materials for the property.

International Guaranties

By Sidney G. Saltz[*]

In this age of globalization, many companies domiciled in other countries have created subsidiaries to do business in the United States. Often, those subsidiaries do not have their own financial statements, and sometimes, even if they have separate financial statements, their net worth is insufficient to assure the other party to a transaction that they have the financial where-with-all to pay and perform in accordance with their undertakings in their agreement. Under those circumstances, the other party may request a guaranty from the foreign parent company.

Guaranties by a foreign company, which I refer to in this Article as "foreign guaranties", present special issues of which the drafter would be well advised to be aware. In the typical domestic guaranty, an action under the guaranty may be brought in the domicile of the guarantor, and sometimes in the place of residence of the party benefiting from the guaranty. It is a matter of reviewing the jurisdictional and venue provisions in the applicable state, and determining the rules for service of process. In any case, the action is brought in the United States and any judgment is entitled to full faith and credit in other states in which assets of the guarantor may be located. That may not be the case with international guaranties.

There are four basic problems with international guaranties which should be dealt with in the body of the guaranty itself. The first relates to consent to jurisdiction, the second to service of process, the third to choice of law. The final major issue, and perhaps the most important, is the issue of enforcing any judgment obtained in a United States court in the home country of the guarantor.

Let us assume, for the sake of this article, that the guaranty relates to a lease for premises in Chicago, Illinois, the landlord being an Illinois limited liability company having its principal place of business in Cook County, Illinois, the county where Chicago is located, and the guarantor being a German company. In a diversity action in the Federal District Court for the Northern District of Illinois, the action may be brought where all the plaintiffs or all of the defendants reside. Although the Federal statutes provides for that jurisdiction, and although it is established law that parties cannot, by agreement, confer jurisdiction (as opposed to venue) where it does not otherwise exist, it is helpful to have language in the guaranty agreeing to jurisdiction (as well as venue) if the international company can be properly served with process. Hence the guaranty may contain the following language regarding jurisdiction:

> With respect to any dispute or legal action of any kind arising from the terms of this Guaranty that any party may have, either during the term of this Guaranty or thereafter, it is expressly agreed that such action shall be brought either in the Circuit Court of the State of Illinois in the County of Cook (or in the Federal District Court for the Northern District of Illinois, to the extent such court has jurisdiction thereof), and that such court shall be deemed to be the court of sole and exclusive jurisdiction and venue for the bringing of such action. The foregoing consent to jurisdiction and venue shall not constitute general consent by Guarantor to jurisdiction and venue in the State of Illinois for any purpose except as provided herein and shall not be deemed to confer rights on any other person or entity.

The final sentence affords the guarantor protection against other actions in the chosen jurisdiction by providing, in effect, that the consent to jurisdiction and venue (and service of process) is limited to this guaranty.

The second issue relates to the service of process. Since the process of the Circuit Court of Cook County or the Federal District Court for the Northern District of Illinois does not extend to Germany, provision has to be made for the appointment of someone in the State of Illinois to accept service of process so that the case may be commenced. That can also be dealt with in the guaranty, designating each of the tenant and the Secretary of State of the state where the contract is to be performed as the agent for the guarantor to accept service of process. In our example, the following language may be suitable for that purpose:

> Guarantor agrees that (a) Tenant and (b) the Secretary of the State of Illinois, shall each hereafter have full authority and be duly empowered to accept service of process on behalf of Guarantor in connection with the enforcement of this Guaranty, and Guarantor hereby appoints Tenant and such Secretary of State as its agents for purposes of acceptance of service of process in connection with the enforcement of this Guaranty, so long as a copy of any such legal proceeding served upon Guarantor through Tenant or the Illinois Secretary of State is promptly furnished to Guarantor by an international courier service at the following address: ____.

Note that the language provides for a copy of the complaint to be sent to the defendant in its home jurisdiction.

The choice of law language is fairly typical:

> It is expressly understood and agreed by Guarantor and Landlord that all matters arising out of this Guaranty, including the validity or any provisions hereof, are to be governed by, interpreted and construed in accordance with the laws of the State of Illinois (without giving regard or effect to any conflicts of law rules or other choice of law rules).

Of course, in each instance, references in the quoted language to Illinois and Cook County are merely illustrative and the appropriate state and county (if appropriate) should be inserted if the reader is using the examples.

The final issue, enforceability of the judgment in the home country of the guarantor, is more problematic. It is unlikely that the drafter of the guaranty knows the law of that country sufficiently to advise the client that if it obtains a judgment against the guarantor in the courts of the United States, it will be able to enforce that judgment in the foreign country without having to bring a totally new action and prove its case again—an expensive and time consuming outcome. Some countries may have laws providing for the enforceability of foreign judgments, provided that they are not obtained in a manner contrary to the public policy of that country.

A way to have some level of comfort with that issue is to require that the guarantor provide an opinion from its attorney in the country where the judgment is proposed to be enforced, stating that it will be enforceable without a new trial on the law and facts. The results disclosed by those opinions can be quite surprising. Some years ago, I represented a landlord who requested a guaranty from a German company. Fortunately we did request such an opinion and were shocked to learn that the taking of pre-trial discovery was against public policy in Germany. Accordingly, if our client had done discovery in connection with its action against the guarantor—a very typical trial preparation tool, it could not have enforced the judgment. I do not know whether the opinion was accurate and I do not know if that continues to be the law in Germany today, but if an action under that guaranty had been required, my client would certainly have not done pre-trial discovery without further investigation of German law.

If the foreign guarantor is unwilling or unable to provide such an opinion, it may be incumbent on the party seeking the guaranty to hire its own attorney in the guarantor's home country, or to seek advice from an American firm with attorneys licensed to practice in that country. Retrying the issues in a foreign country may be very difficult and expensive, and may require the trial to be conducted in a hostile, or at least unfriendly, forum.

Conclusion

If a party to a transaction involving the United States subsidiary of a company domiciled in a foreign country deems it necessary to obtain the guaranty of the parent company to conclude the deal, it is incumbent on that party to seek to assure that the guaranty has real value. That assurance can be accomplished by inserting provisions in the guaranty not usually required in guaranties from United States companies, and also assurances that, under the law of the foreign country, a judgment obtained in the United States court will have the anticipated value when collection on the judgment is sought in that country. After all, a guaranty, even from a very strong company, is no good if the guarantor cannot easily be sued, and a judgment is no good unless it is feasible to collect it.

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