

Beware guarantees

by JOHN MARCHANT*

The practitioner commonly is asked to certify that the person who is signing a document understands the true purport and effect of the transaction. The duties of a solicitor giving such a certificate were outlined by the majority in the Full Court of South Australia in *McNamara v Commonwealth Trading Bank* (1984) 37 SASR 232 at 241.

The comments appear to be general in their application, even though *McNamara's Case* itself concerned the provision of a certificate pursuant to Section 43(2) of the *Consumer Transactions Act* (SA) (which dealt with independent obligations undertaken in addition to the guarantee of obligations under the *Consumer Credit Act*). Increasingly banks and other financial institutions demand similar certificates in the context of a variety of guarantees and security documents, irrespective of whether or not they are required by s 43 of the *Consumer Transactions Act*.

Practitioners should consider carefully the desirability of providing such certificates, particularly where they are not required under s 43 of the Act. The practitioner may be personally liable to the lender if the certificate is found to be incorrect.

The majority of the Full Court in *McNamara's Case* considered that it was not only necessary for the practitioner to review the document clause by clause and give a detailed explanation of its legal effect, but for the solicitor to raise with the person intending to sign the document the prudence of becoming a surety, and the wisdom of entering into the guarantee from a practical point of view.

Regard should be had to:

- * the guarantor's affairs and assets;
- * the possibility of any undue influence or unconscionable dealing;
- * any likely encumbrance of the guarantor's assets which may work to the guarantor's disadvantage;
- * any special features of the relationship between the debtor and

the guarantor; and

- * the nature of the arrangement or the contract between the debtor and the creditor.

The advice should *not* be given in the presence of the debtor. Conflict of interest issues affecting the practitioner must also be considered.

Finance Document Guidelines

The following matters are outlined for the assistance of practitioners when advising potential guarantors or other persons who seek a solicitor's certificate in relation to finance documents.

1. The general nature of the document should be explained. It is stressed that the advice cannot be given adequately in 5-10 minutes if the *McNamara's Case* guidelines are followed. In most cases, three to four hours work by the solicitor would be required after taking into account time spent with the client and ensuring other enquiries are undertaken. Obviously practitioners should charge an appropriate fee for this work.

2. The legal effect of each clause of the document should be explained to the person to ensure that the nature of the provisions in it are properly understood.

3. Careful consideration should be given as to whether the client should be advised to seek accounting or other financial advice concerning the transaction.

4. Where the document is in the nature of a guarantee, the practitioner should enquire into the extent of knowledge in the person of the arrangements between the debtor and the creditor of which the following matters may be relevant: is a sum certain being borrowed?; is it a revolving credit arrangement of some kind?; what are the terms of repayment and interest payment?; for what purpose is the debtor intending to use the funds?; how long has the debtor been in business and his business his-

tory?; is the debtor already indebted to the creditor and for how much?; what has the person been told or requested by either the debtor or the creditor about the document?; has the creditor informed the person of any facts of circumstances which appear either to the person or the practitioner to warrant further enquiry?

5. Persons should be asked their understanding of the terms of the arrangement. In this regard persons should be asked about conversations with the bank manager and the debtor and whether any representation has been made as to limitation of liability or the extent of the guarantee in time.

6. Where limitations of liability appear at first glance, the practitioner should search for qualifications contained in the document which are not obvious.

Practitioners should keep some written evidence that the document was fully explained to the borrower/guarantor for the practitioner's protection. It is recommended that a practitioner make a photocopy of the document or documents and made a note on the copies that the particular clauses were explained.

Practitioners may also want to obtain from the person at the end of the interview an acknowledgement in writing endorsed upon the photocopies of the documents that the document has been fully explained to them clause by clause on the stipulated date and that the client fully understands the legal effect of the document. Practitioners may, as a further step, confirm the important points arising from the interview with the client by letter as soon as practicable after the conclusion of the interview.

Practitioners are reminded that in giving such a certificate the solicitor incurs a duty to the bank or financial institution and represents that the proper advice has been given. If the certificate is proved to have been incorrectly given, the bank or lending institution may look to the solicitor for indemnity with potentially serious consequences.

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