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## REAL ESTATE E-BRIEF

### Co-Borrower v. Guarantor: Who Is On The Hook?

Real estate transactions often involve the use of single purpose entities, which are corporations or limited liability companies, or some other form of business partnership or organization, formed for the sole purpose of acquiring, owning, managing, or developing a particular piece of real property. Single purpose entities are attractive because they enable owners to isolate the potential liability and risks associated with one real estate project from another. When real estate transactions involve financing, lenders may require that a principal or owner of the single purpose entity act as a co-borrower or guarantor of the loan.

The differences between acting as a co-borrower or guarantor of such a loan may be significant. Generally, a co-borrower is a party to the loan whose name appears on the loan documents and who is principally obligated to re-pay the debt regardless of whether there is a default first. On the other hand, a guarantor typically signs a separate agreement and agrees to pay only if a default occurs first.

One of the differences between co-borrower and guarantor structures arises following foreclosure. Under Nebraska law, a lender has 3 months following a trustee's sale to commence a deficiency action to recover the balance owed under the loan not realized by the sale.\* The Nebraska Court of Appeals in *Boxum v. Munce* interpreted the 3-month time

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limit to apply only to the borrower itself, and not to the guarantor of the loan. In *Boxum*, the lender foreclosed on a deed of trust securing a promissory note in November, 2004, but waited until January, 2006, to sue the guarantor to collect on the guaranty of payment.

The Court found that the 3-month statute of limitations applied only when the suit for deficiency is on the obligation secured by the foreclosed trust deed, but did not apply to a deficiency action against the guarantor. The distinction drawn by the Court was that the deficiency statute applied only to efforts to recover the balance owed under the foreclosed obligation; in that case, the deed of trust secured the promissory note. The Court further noted the guaranty of payment was a completely separate and distinct obligation from the promissory note given by the borrower to the lender. Instead of the 3-month time limit, the Court applied Nebraska's 5 year statute of limitations applicable to any written contract. As a result, the 14 month delay between foreclosure and pursuing a claim on the guaranty was considered timely.

In *Boxum*, the fact that the additional party was a guarantor rather than a co-borrower made the guarantor susceptible to a deficiency action for a longer period of time following foreclosure. This is just one distinction between acting as a co-borrower versus a guarantor, and real estate borrowers should be aware of other differences in the obligations and risks associated with signing as borrowers, co-borrowers, and guarantors. When reviewing your loan documentation, be sure to consider whether you are signing (1) individually as a co-borrower, (2) as a representative on behalf of the borrowing entity, or (3) as a guarantor (or some combination of these), and whether the documents accurately reflect your intentions.

\*Neb. Rev. Stat. § 76-1013.

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