

Make the Lease Happen with a "Good Guy" Guaranty

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Every landlord wants a tenant with a "Triple A" credit rating. The landlord's up-front costs and financial exposure are considerable, and many of these, including payment of one or more broker's commissions; fit-out costs; tenant improvement allowance and possibly a free rent period, are expended before the tenant pays a dime of rent. If the tenant's financials are strong enough, the landlord can sleep at night holding little or no security deposit. However, office and retail tenants with little or no net worth pose financial risks that keep landlords awake at night. For tenants like these, the landlord understandably looks for a more substantial security deposit that covers a sizeable portion of the landlord's sunk costs if the tenant defaults before the landlord recoups his expenses via the rent stream. The problem is that the tenants who should post a large security deposit are often the least able or willing to do so. In these cases, the negotiations invariably turn to a personal guaranty from a 'deep-pocket' individual with an ownership stake in the tenant – otherwise the guaranty may not be legally enforceable for 'lack of consideration.'

But the tenant's owner(s) may balk at the notion of an unlimited personal guaranty. After all, that would largely defeat the purpose of doing business as an entity, such as a limited liability company or corporation, which shields the tenant's owners from personal liability for the debts of the tenant. Further, an unlimited personal guaranty is a contingent liability that may hamper the guarantor's ability to get a home or car loan.

If the bank will not finance the lease, or the landlord is not assuaged with some combination of a smaller cash security deposit and a limited or "capped" personal guaranty (either or both of which may "burn-down" over time if the tenant is not in default), consider solving the dilemma with a so-called "Good Guy" Guaranty.

The "Good Guy Guaranty" is a relatively new concept, or at least one which seems to have gained greater favor in recent years. Here the liability of the tenant's guarantor is limited to any rent accrued post-default, and the guarantor is only liable if the tenant remains in possession after the expiration of the default notice and cure period. Since the guarantor must be related to the tenant (and is typically the deep-pocket owner of the tenant), the guarantor controls the tenant and thus the guarantor remains firmly in control of his own financial exposure to the landlord under the Good Guy Guaranty – even if the Guarantor cannot control the finances of the tenant.

In other words, if the tenant defaults under the lease because its business has failed, the Good Guy Guarantor would nonetheless owe nothing to the landlord under the Good Guy Guaranty so long as the guarantor causes the tenant to immediately vacate. The existence of the Good Guy Guaranty should be

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sufficient motivation for the tenant to vacate pronto, thus avoiding the time and expense of eviction and reducing the lost rent period before the landlord can procure a new tenant. If the tenant returns the space to the landlord immediately after the default, the Good Guy Guarantor gets off scot-free.

So long as the cash security deposit and/or limited cash guaranty are sufficient to pay the landlord's unrecouped lease-up costs (if any) at the time of the tenant's default, the Good Guy Guaranty may greatly mitigate any remaining losses of the landlord.

The benefits of the Good Guy Guaranty to landlords are twofold: (1) It eliminates the need for the landlord to evict the tenant and lose income while the eviction is pending and (2) the landlord can immediately relist the property for rent. The benefit to the guarantor is that he gains the ability to control his contingent personal liability for the lease so his credit is not as adversely affected as if he had given an open-ended monetary guaranty.

Needless to say, the facts and circumstances surrounding every lease are different and this article is not intended to constitute "one-size-fits-all" legal advice. Please consult an attorney before deciding what is appropriate security for your lease.

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