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## NEW YORK APPELLATE COURT UPHOLDS FINDING OF SPRINGING FULL-RECOURSE LIABILITY OF GUARANTORS BASED UPON FAILURE TO PAY PROPERTY TAXES

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In a recent decision, New York’s Appellate Division, Second Department, held that guarantors under a “springing recourse guaranty” were liable for the full debt amount following the nonpayment of property taxes. Guarantors asserted that such terms constituted an unenforceable liquidated damages provision; however, the Court overruled these objections in a well-reasoned opinion.

The opinion and order in *G3-Purves Street LLC v. Thomson Purves, LLC*, issued on October 17, 2012, analyzed commercial mortgage loan documents of a generally non-recourse loan, but the subject guaranty allowed for full-recourse liability against the guarantors upon the happening of certain “springing recourse events,” including the failure to pay taxes and allowing a lien to be asserted against the property. When the borrower failed to pay real estate taxes on the property, the lender accelerated the maturity date, commenced foreclosure, and ultimately moved for summary judgment.

In opposition to the lender’s motion, the guarantors argued that the springing recourse guaranty intended to impose full-recourse liability upon them only if an affirmative act was committed that would interfere with the lender’s ability to recover the property. The guarantors also argued that the springing recourse provisions of the guaranty constituted an unenforceable liquidated damages provision that would result in a grossly disproportionate penalty upon them as compared to the amount of the liens that had been filed against the property.

Finding that (i) non-recourse loan agreements containing carve-out provisions are generally valid and enforceable, (ii) the terms of the guaranty imposing springing recourse liability were clear and unambiguous, and (iii) the loan agreement and guaranty were entered into by sophisticated business parties negotiating at arm’s length, the Second Department held that the carve-out provisions of the guaranty operated to define the terms and conditions of personal liability rather than affix disproportionate, speculative damages against the guarantors. The Court also noted that the carve-out provisions were bargained for as part of the loan, and that the liability of the guarantors, who had received the full benefit of the loan, was limited to the actual damages incurred to lender—the outstanding debt fixed by the terms of the loan documents.

If you have any questions about the information contained in this Client Alert, please contact the Thompson & Knight attorney with whom you regularly work or one of the attorneys listed below for more information.

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