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FINANCIAL INSTITUTION E-BRIEF

Co-Borrower v. Guarantor: How Are Lenders Affected When Seeking Deficiency Judgments?

When entering into a loan transaction, many times lenders are faced with the decision of whether they want to include an additional party to the loan as a co-borrower, or as a guarantor of the loan. Although these decisions are made during the beginning of the loan transaction, it is important that the lender think through matters which may occur throughout the life of the loan. Specifically, as shown in the below-described case, if the loan transaction is a real estate secured loan, the lender should strongly consider making the additional party a guarantor of the loan, rather than a co-borrower.

The Nebraska Court of Appeals in *Boxum v. Munce* clearly set out the advantage to the lender of including the additional party to the loan as a guarantor rather than a co-borrower. In *Boxum*, the lender foreclosed on a deed of trust securing a promissory note. After foreclosing on the deed of trust in November 2004, the lender waited until January 2006 to sue the guarantor to collect on the guaranty of payment. The guarantor claimed that the lender was out of time to pursue a deficiency judgment, citing Neb. Rev. Stat. § 76-1013, which provides that a deficiency action must be commenced within three (3) months after the trustee's sale to recover the balance owed under the obligation secured by the deed of trust.

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The Court found that the three (3) month statute of limitations applied only when the suit for deficiency is on the obligation for which the foreclosed trust deed was given as security. In *Boxum*, the Court held that the three (3) month statute of limitations did not apply because the note was the obligation the foreclosed trust deed secured and the suit before the Court was not on the note, but rather was on the guaranty of payment. The Court specifically noted the guaranty of payment was a completely separate and distinct obligation from the note given by the borrower to the lender.

Ultimately, the Court found that the action was not barred by the three (3) month statute of limitations, but rather because the suit was brought to collect on a separate and different contract—the guaranty—the five (5) year statute of limitations on an action on any agreement, contract or promise in writing was applicable, and thus the action was brought within the applicable statute of limitations. In *Boxum*, the fact that the additional party was a guarantor rather than a co-borrower provided the lender additional time to pursue an action to collect on the guaranty, and thus the lender was not limited to the three (3) month statute of limitations to bring a deficiency action, as it would have been if the additional party had been included as a co-borrower.

When entering into new loan transactions there are numerous considerations for the lender when choosing between the co-borrower and guarantor structures, and collection matters is certainly one of those key considerations. Although it is impossible to know what the future may hold at the beginning of a loan transaction, various scenarios should be considered, and in some situations discussed with legal counsel, to ensure that the lender is protected and properly situated should the borrower default on the loan in the future.

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