



Commercial Lending

Bulletin

Volume 6 Issue 1
January 2007

“Responsive service and practical advice when you need it.”

Creditor Overcomes Challenge of Jurisdiction

The Court of Appeals of Oregon has determined that an Ohio resident who guaranteed debt of an Ohio corporation is liable to suit in Oregon because, by virtue of his contact with a creditor located in Oregon, he “availed himself of the privilege of causing important economic consequences in the State of Oregon.”

Javed Iqbal, President of Pro Sports Wear, Inc., contacted Nike USA, Inc. in an attempt to obtain Nike’s products to sell at his stores. After meeting Nike’s regional sales representative in Cleveland, Iqbal sent an application on behalf of Pro Sports Wear and his personal guaranty form to Oregon for processing. Nike relied on these forms in its decisions to extend credit to Pro Sports Wear and to require Iqbal to guarantee Pro Sports Wear’s debt. On November 20, 2000 Nike sent Iqbal a letter on Nike stationery from its Oregon office notifying Iqbal of its decision to approve a \$15,000 line of credit. During the next 3 years, Iqbal received an invoice for each of his purchases of Nike products, each of which specifically stated that “Customer consents to...jurisdiction...in the State of Oregon.” Iqbal, however, was unable to pay for the merchandise he purchased, and in March, 2004, he faxed a note to Nike’s Oregon office regarding a payment plan. Nike then filed suit in Oregon against Pro Sports Wear and Iqbal to recover over \$100,000 worth of funds advanced under the line of credit. Iqbal filed a motion to dismiss for lack of personal jurisdiction, claiming he had never consented to jurisdiction in Oregon and had never done business with the Oregon office. The trial court agreed with Iqbal, stating that Iqbal did not have sufficient contact with Oregon to provide a basis for jurisdiction.

Nike appealed. While the Court of Appeals disagreed with Nike that Iqbal had consented to jurisdiction in Oregon (because he was a guarantor of the loan and the credit agreement he signed contained no forum selection clause), the Court did find him subject to personal jurisdiction there. Referring to cases decided by the United States Supreme Court, the Court of Appeals cited the rule that, in order to subject someone to foreign jurisdiction, they must have had “minimum contacts” with the forum state in which they “purposefully directed” activities toward causing important economic consequences in the forum state. Here, because Iqbal corresponded with Nike’s offices in Oregon and the decision to extend credit to Pro Sports Wear with Iqbal’s personal guaranty was made in Oregon, the Court found the requisite minimum contacts. Although Iqbal claimed ignorance of the location of Nike’s offices, the Court stated that in a “sophisticated commercial transaction such as this it was [defendants’] obligation to determine with whom they were contracting...[and that]...defendants under these circumstances may [not] rely on their own failure to investigate as a shield...” The Court further stated that Iqbal should have realized that he would be subject to jurisdiction in Oregon if a problem ever arose under the transactions.

What can be learned from this case is that Nike could have avoided the challenge of lack of personal jurisdiction if it had included a forum selection clause in its credit agreement. The Court noted that forum selection clauses are prima facie enforceable and will only be disregarded if the enforcement is unfair and unreasonable. In this case, the forum selection provision was only included in customer invoices, which are not signed by the debtor or guarantor.

This case is cited as *Nike USA v. Pro Sports Wear, Inc.* 145 P.3rd 321 (2006).

Guaranty Does Not Extend To Certain Changes Made By Bank Without The Guarantor's Consent

The Ohio Court of Appeals recently decided that a personal guaranty of a promissory note does not extend to certain changes or alterations made without the consent of the guarantor, despite a general provision allowing the lender to alter or modify the note without the guarantor's consent.

In 1999, Bank One, N.A. extended a \$35,000 line of credit to PIC Photo Finish, Inc. PIC executed a promissory note in 1999 guaranteed by Mark and Georgiann Smith. The Smiths signed the note individually as guarantors. The 1999 Promissory Note contained a provision that each guarantor authorized Bank One "to alter, compromise, renew, extend, accelerate, or otherwise change at one or more times the time for payment or other terms of the Note, including increases and decreases in the rate of interest of the Note, and to grant repeated extensions which may be for longer than the original Note term...without notice or demand and without releasing Guarantor's liability under the guaranty."

In 2003, PIC executed a second promissory note in the amount of \$65,000 that expressly declared that it was a renewal of the 1999 Promissory Note. The 2003 Promissory Note was not signed by the Smiths individually as guarantors. PIC subsequently defaulted on both notes and Bank One filed suit. The trial court held that the Smiths were liable as to the extent of money owed under the 1999 Promissory Note but not the additional obligations evidenced by the 2003 Promissory Note. Bank One appealed the decision that the Smiths did not guaranty the 2003 Promissory Note.

The Court of Appeals noted that while the 2003 Promissory Note was a renewal of the 1999 Promissory Note, the declaration contained in the 2003 Promissory Note was not binding upon the Smiths because they did not sign it as guarantors. Accordingly, the issue on appeal was whether an increase in the principal obligation of the 1999 Promissory Note was included in the scope of the alterations that the Bank could unilaterally make without the Smith's consent. The Court held that an increase in the principal obligation was not something the Bank could do without the express consent of the Smiths as guarantors, even with the guarantor's consent to modifications set forth in the 1999 Promissory Note. Thus, the Smith's guaranty was limited to the original principal amount of \$35,000.

This case highlights the importance of ensuring that all guarantors expressly reaffirm their obligations arising under their guaranty and that they consent to any modification of a promissory note, even where there is a general provision in the loan documents to allow for modification without the guarantor's consent.

This case is cited as *Bank One, N.A. v. PIC Photo Finish, Inc.*, 2006-Ohio-5308.

Vague Contract Terms Cannot Create Personal Liability

The U.S. District Court for the Northern District of California recently held that an ambiguous provision in a credit agreement was not enough to create personal liability for the individual who signed the credit agreement on behalf of a business.

In January 2002, Ronald Poulin, on behalf of Virginia Hematology Oncology, signed a credit application and agreement with Oncology Therapeutics Network in order to purchase products and set up a line of credit with the Network. Virginia Hematology began purchasing products from Oncology Therapeutics and at some point fell behind in its payments. In June 2005, Oncology Therapeutics filed a complaint against Virginia Hematology and Poulin alleging that by signing the credit application and agreement, Poulin personally guaranteed the debt. The Court disagreed stating that the credit application and agreement did not clearly impose liability on Poulin solely as a signatory.

The language which Oncology Therapeutics based its claim on appeared directly above the signature line and stated “the person signing below personally guarantees that Applicant will pay all amounts due under this agreement and shall be responsible for such amounts being paid.” The Court found that this language states that Poulin will ensure that Virginia Hematology pays its debts, but does not state that Poulin expressly assumes the debts of Virginia Hematology and does not personally guaranty the debt. Further, the Court found that evidence outside of the credit application and agreement could have been presented to show that the intention of both parties was to bind Poulin as a personal guarantor, but Oncology Therapeutics failed to provide any such evidence. Poulin also noted that he signed the document by including the title “managing member” after his name, and that he was referred to as “authorized representative” and not “guarantor” throughout the application. Finding no evidence to support the claim that Poulin assumed personal liability of Virginia Hematology’s debt, the claim against him was dismissed.

It is important to remember that if a lender intends an individual to be a personal guarantor to a loan, such an intention must be in clear language on the face of the documentation and must be agreed to by all parties.

The case above is cited as *Oncology Therapeutics Network Connection v. Virginia Hematology Oncology PLLC and Ronald Poulin*, No. C 05-3033 WDB (N.D. Cal. Feb. 10, 2006)

Practice Tip:

Loan Guaranties

A guaranty is a contract by which a lender has recourse against a person, the guarantor, or that person’s property, with respect to obligations of another. As a matter of contract law, there must be consideration for the contractual obligations of the guarantor. Generally, a lender’s undertaking to make a loan to a borrower in reliance upon a guaranty should constitute consideration.

Please see “Practice Tip” continued on page 4

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Prudent lenders, however, will always assume that the guarantor will assert a defense in any collection action that there was no independent consideration for the guarantor’s undertaking to guaranty the loan. Although the issue of consideration is too broad to be discussed at great length here, two issues bear mention: First, the guaranty should always be dated concurrently with underlying loan documents such that the lender can assert that the loan would not have been made but for the guaranty. Second, lenders should require that, in those instances where secondary collateral not owned by the borrower is pledged, the owner of the secondary collateral should execute a “limited” guaranty or another document memorializing the rationale behind and basis of the collateral pledge.

The potential liability of a guarantor is interpreted in accordance with different state statutes; additionally, the courts have interpreted the liability of a guarantor depending upon the specific language used in the guaranty document. To that end, after a loan has been closed, lenders should always consult with counsel before entering into any transactions with a borrower or a guarantor, or otherwise involving collateral pledged in connection with a loan or a guaranty, to be sure that any such transactions do not unintentionally release or limit the guaranty or additional collateral.

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