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MORTGAGES:

How to Ensure Your Guarantee is Enforceable

In the case of *JGB Collateral, LLC v. Rochon 2020 ONCA 464*, a business loan was granted to the JGB Collateral Inc. corporation guaranteed by a mortgage over property exclusively owned by the wife of the chief executive officer and majority shareholder. The corporation defaulted on the loan. At issue was the validity of the mortgage and, more specifically, whether it was unenforceable as a result of the wife being subject to undue influence of her husband.

Undue influence occurs when influence from an external source overpowers the voluntary wishes of an individual, such that legal documents a person has signed are not signed of their own free will. While people are typically influenced by family and friends, undue influence results when the document they are signing does not represent a person's true wishes but the wishes of another party. This scenario can be a significant issue in the case of wills, as elderly people may be unduly influenced to gift all their property to someone they would ordinarily not have selected by choice.

The judge in the case, in overturning the lower court, stated that to determine if the guarantor had been unduly influenced it was necessary to decide whether a presumption of undue influence could be inferred by the nature of the transaction and the relationship between the guarantor and the debtor.

Where there is the presumption of undue influence, the lender can protect themselves by demonstrating they had recommended the guarantor obtain independent legal advice. By definition, independent legal advice for a guarantor is that advice obtained from a lawyer with no interest in the main debt; that is, they were not acting for the debtor. Such a lawyer would explain the nature of the transaction to the guarantor and ensure they are entering into the transaction freely. If the lender does not recommend the option of independent legal advice to the guarantor, they may still defend the validity of the loan by producing evidence of no undue influence, such as the guarantor's statements of signing the guarantee of their own free will.

In this case, the judge believed there wasn't even the presumption of undue influence as the wife had a significant stake in the business and she understood that signing the guarantee would be to its benefit. In addition, her husband had gifted her the mortgaged property in question. However, even if the presumption of undue influence could be inferred, the mortgage would continue to be enforceable, as the lender had suggested to her that she obtain independent legal advice.

DE FRANCESCA LAW

744 Broadview Avenue, Suite 100, Toronto, Ontario M4K 2P1

Phone: (416) 778-4433 • Facsimile: (416) 778-4432 • Email: info@defranlaw.com • www.defranlaw.com



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In conclusion, the safest option for lenders to take in cases where there is a guarantee would be to recommend guarantors seek independent legal advice. In Ontario, this is the advice lenders generally follow by including this recommendation in mortgage instructions.

