NEWS & DEVELOPMENTS

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"Collusion" Defense Fails under Absolute and Unconditional Guaranty

New York's highest court has rejected the argument that a guaranty was unenforceable due to plaintiff's alleged "collusion" in obtaining a default judgment against the principal obligor. In *Cooperatieve Centrale Raiffeisen-Boerenleenbank, B.A. v. Navarro,* 2015 NY Slip Op 04753, 2015 N.Y. LEXIS 2333 (June 9, 2015), the Court of Appeals held that the defense of the plaintiff's collusion was barred by the express language of the defendant's absolute and unconditional guaranty. *Id.* at *1.

The defendant guarantor was an officer and director of Agra USA and its parent, Agra Services of Canada (Agra Canada). Agra Canada's operations were managed by Eduardo Guzman Solis (Solis), and it had a purchase agreement with the plaintiff whereby the plaintiff purchased and financed Agra Canada's receivables. The defendant and Solis each gave the plaintiff their absolute and unconditional personal guaranty of the obligations of both Agra Canada and Agra USA. Two years later, after Solis died, the parties discovered that Solis had caused Agra Canada to submit fraudulent receivables to the plaintiff based on nonexistent transactions, resulting in overpayments by the plaintiff. *Id.* at *4.

Bankruptcy proceedings in Canada were initiated against Agra Canada and an accounting firm chosen by the plaintiff was appointed trustee, who later replaced the management of Agra USA. The plaintiff also brought an action in New York federal court against Agra USA and both guarantors, the defendant and Solis' estate, to recover the overpayments and to enforce the guaranties. The plaintiff eventually entered a default judgment against Agra USA in federal court for over $41 million and voluntarily dismissed the defendant guarantors without prejudice. The plaintiff then commenced an action in New York against the defendant guarantor, claiming that he was liable under the guaranty for the money owed by Agra Canada under the purchase agreement and, alternatively, for the amount of the default judgment against Agra USA.

The defendant argued that his guaranty did not encompass fraudulent transactions of Agra Canada caused by Solis and that those transactions were not "accounts receivable" as defined in the purchase agreement. He also alleged that the plaintiff controlled Agra USA when the default judgment was entered against it and that the plaintiff's "collusion" in obtaining that judgment did not give rise to an obligation enforceable under his guaranty. The court denied the plaintiff summary judgment because questions of fact existed both as to whether actual receivables existed and as to who controlled Agra USA when the default was entered against it. *Id.* at *7.

The Appellate Division, in a 3–2 decision, reversed the lower court and granted the plaintiff summary judgment, finding that the guaranty by its express terms precluded any defense as to the existence of an "enforceable" obligation, including that of collusion. 978 N.Y.S.2d 186 (1st Dep't 2014). As noted by the Court of Appeals, the dissent disagreed, stating that if the default

judgment was obtained by collusion, it would not constitute a "valid obligation" covered by the guaranty. 2015 N.Y. LEXIS 2333, at *8.

On further appeal, the defendant argued that the plaintiff had not met its burden by establishing an obligation was due and owing under his guaranty. The Court of Appeals, however, ruled that the plaintiff had established its prima facie entitlement to enforce the guaranty and that the appeal turned on whether the plaintiff's demand for summary judgment was foreclosed by the guaranty. It affirmed the Appellate Division, holding that the defendant's collusion defense was precluded by his agreement in the guaranty that his liability was "absolute and unconditional" irrespective of any defenses that may exist to its enforcement. *Id.* at *10.

Guaranties that by their express terms are absolute and unconditional "have been consistently upheld by New York courts." *Id.* at *10–11 (citations omitted). In *Citibank, N.A. v. Plapinger*, 66 N.Y.2d 90 (1985), the court held that a guarantor's defense of fraudulent inducement was precluded by the guaranty's language. To find otherwise, the court there reasoned, would condone a guarantor's own misrepresentation that the guaranty was enforceable notwithstanding any defenses that may exist. Here, "by its plain terms, in broad, sweeping and unequivocal language," the defendant's guaranty foreclosed any defense to the defendant's liability as guarantor for the obligations of Agra USA and Agra Canada. 2015 N.Y. LEXIS 2333, at *13–14.

The court also found that the collusion defense as to the Agra USA default judgment "ultimately" amounted to one of fraud and was therefore waived by the defendant's absolute and unconditional guaranty. Moreover, there was no contention that Agra Canada's fraudulent transactions engineered by Solis "were caused, expedited or otherwise facilitated" by the plaintiff as part of a "collusive effort to cash in on" the defendant's guaranty. *Id.* at *17.

Navarro illustrates the extremely high, if not insurmountable, burden faced by a guarantor in New York in defending against the enforcement of an absolute and unconditional guaranty. The court expressly left open the question, however, whether "certain conduct by a creditor and/or debtor may be of such character, and so impacts the guarantor's position that the guarantor may challenge those acts notwithstanding our prior holding in *Plapinger*." *Id.* at *18. Whether or not such circumstances exist in New York awaits further guidance from the Court of Appeals.

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