

Kuwait: considerations for guarantees

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Parties often rely on third party guarantees provided by companies and individuals for third part debts as a form of security or credit enhancement. While such corporate and personal guarantees provide some comfort to the creditor, there are various issues a creditor should be aware of to avoid pitfalls.

In Kuwait, the relevant provisions governing guarantees are set out in Law No. 67 of 1980 concerning enactment of the civil code 'Civil Code'. A guarantee, according to Article 745 of the Civil Code, is a contract between the guarantor and the creditor " where a person joins his liability with that of the debtor in the performance of an obligation on him by undertaking to the creditor to discharge it should the debtor fail to do so". Therefore, the guarantor's liability may be considered joint with the debtor. A guarantee may not be presumed and the consent of the surety must be express and accordingly, should be in writing.

Guaranteeing future obligations

Where a future obligation is being guaranteed, the maximum limit of the guarantor's obligations and the duration of the guarantee should be specified so that the guarantor may not back out of its responsibilities under the guarantee. There is no limit set out in the Civil Code regarding the guaranteed amount limit or the duration. However, according to Article 751 of the Civil Code and as confirmed by the Kuwait Court of Cassation in its decision no. 58 of 1985, hearing session dated 22 January 1986, a guarantee shall not be of a sum greater than the debt due from the debtor or have more stringent conditions.

Key issues in guarantees

- The Civil Code sets out, among others: the guarantee is not valid unless the underlying obligation being guaranteed is valid;
- the liability of a guarantor is discharged if the debtor's obligations are discharged;
- if the guarantor has served notice on the creditor to initiate proceedings against the debtor, the creditor has three months to initiate such proceedings failing which the guarantor can walk away from its obligations under the guarantee;
- the creditor must first exhaust its remedies against the primary obligor before taking enforcement measures against the guarantor in accordance with Article 760 of the Civil Code. However, Article 760 would not apply if the primary obligor and the debtor are said to be jointly liable for the debt or if the debt is a commercial debt; and
- if the principal obligor becomes bankrupt, the creditor must prove its debt (which it is owed) in the bankruptcy. Failing this, the creditor will lose its right to claim against the guarantor to the extent of any sums the creditor might have received had it proved the debt in the bankruptcy.

Demand under a guarantee

Unless the parties to a guarantee agree to submit their dispute to an amicable dispute resolution forum such as arbitration, the procedure to demand a guarantee under Kuwait Law includes, but is not limited to, serving a demand notice to both the guarantor and debtor (if applicable) to claim the amount of debt. If such amount is not paid by either the guarantor or the debtor, the creditor may file a lawsuit before the competent Kuwait court asking the court to oblige the guarantor to pay the debt. If the guarantee relates to a commercial debt, Article 99 of Law No. 68 of 1980 concerning the commercial laws sets out that the guarantors are jointly liable and the debtor and the creditor have an option of claiming its debt from whatever party.

Moreover, the lawsuit application shall be submitted by the creditor or a person legally authorised by the creditor, such as its lawyer. The court requests the creditor to pay the applicable court filing fees which are calculated based on the claimed amount. The court schedules a hearing session and notifies the respondents of the hearing.

Corporate benefit and authorisations

The concept of corporate benefit is not specifically included in Kuwait law. However, the provision of third party guarantees needs specific approvals from various types of Kuwait companies and is not considered ordinary course of business. If proper corporate authorisation is not in place, such a guarantee may be invalidated.

If authority cannot be established, a creditor may rely on the ostensible authority argument under the Civil Code. However, establishing the ostensible authority argument and piercing the veil between the company and the act made by an unauthorised person, is subject to the sole discretion of the court or tribunal in light of the circumstances, facts and documents presented by the parties to the dispute.

Due diligence of the guarantor's assets

While it is necessary to consider the legal issues set out above to avoid pitfalls, there is no substitute to conducting due diligence prior to the execution of a guarantee in respect of the nature of the guarantor's assets. Moreover, creditors should undertake periodic monitoring of the guarantor's assets as the provision of a guarantee does not prevent a guarantor from encumbering or disposing of their assets which has a practical effect on the value that may be placed on the guarantee.

It is important to note that Kuwait law does not recognise the concept of 'self-help remedies'. As such, guarantees in Kuwait must be enforced through a process led by the Kuwait courts and a creditor will require a court order to recover amounts due under a guarantee. In this context, conducting due diligence and identifying the guarantor's unencumbered assets assist the court in an expedient issuance of the attachment order and such order will prevent the sale of such assets pending the final judgment.

Conclusion

While there are various factors to consider before relying on a guarantee, guarantees can be helpful in enhancing the credit package of a transaction. Parties should consult with their legal counsel on the

nuances of each situation to confirm the efficacy and suitability of a guarantee.

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