

BERMUDA

SUPREME COURT

***Fifth Street Finance Corporation -v- David Dobbin* [2013] SC (Bda) 55 Com (17 July 2013)**

TRIAL OF PRELIMINARY ISSUE - GUARANTOR'S LIABILITY - LEAVE TO AMEND

The Plaintiff in this action was a Delaware corporation based in New York State which provides business finance. The Defendant was a businessman resident in Bermuda. The Plaintiff sought US\$3,874,441.30 together with, *inter alia*, contractual interest and costs from the Defendant under a Guarantee and Indemnity Agreement dated 28 September 2009 ("the Guarantee"). The principal debtor whose debts were guaranteed by the Defendant is a Canadian company, Repechage Investments Limited ("RIL"). The primary obligations were owed to the Plaintiff by RIL as assignee of pre-existing liabilities under a Credit Agreement owed by two of RIL's subsidiaries. RIL filed a voluntary bankruptcy petition in the United States Bankruptcy Court for the District of Massachusetts (Eastern Division), which the Defendant signed as its President and Chief Executive Officer.

The Defence alleged that the Guarantee formed part of wider financing arrangements involving GE Canada equipment finance, LP ("GE"), a co-creditor of RIL together with the Plaintiff. Under a 16 October 2009 agreement ("the Interpleader Agreement"), GE and the Plaintiff agreed to cooperate and share the liquidation assets of RIL. The Plaintiff participated in the bankruptcy proceedings commenced by RIL and the Group in June 2011. On or about 3 February 2012, an Asset Sale took place by order of the *United States Bankruptcy Court* under which most of the Group's assets were sold. Pursuant to "the Carve Out", which the Plaintiff failed to object to, junior third party claims were paid ahead of GE's senior debt with the result that the RIL assets available to secure the principal debts were significantly reduced.

The crucial averment in the Defence is that the Plaintiff "*failed to take any or any reasonable care in relation to the principal debts and materially changed, or acquiesced in the change, of the risks undertaken by the Defendant in the Guarantee...The Plaintiff has as a matter of Ontario law thereby lost the right to demand under*

the Guarantee ...and/or its rights to claim are reduced by the amounts by which the Plaintiff's conduct has prejudiced the Defendant as surety".

This hearing was listed in order to deal with a preliminary issue of whether the Plaintiff's demand by letter dated 6 January 2012 in the sum of US\$3,941,100.72 was lawful as a matter of Canadian Law. The Court, having reviewed the expert evidence, answered this in the affirmative. As the Defence raised no basis for extinguishing the Guarantor's liability altogether, the Plaintiff's demand for payment could not be unlawful as a matter of Ontario law.

The Defendant's related application for leave to amend the Defence was refused because the draft amendment disclosed no reasonable defence and, alternatively, the Plaintiff validly contracted out of the alleged duty in any event. In short, under the terms of the Guarantee and the related Interpleader Agreement, the Defendant clearly agreed not to resist enforcement of the Guarantee on the grounds that the Plaintiff ought to have pursued alternative remedies against the secured assets or their proceeds of sale.

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