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Unilateral termination of a comittment to guarantee granted on a blank promissory note

The Portuguese Supreme Court of Justice Ruling 1/2025, of January 8, standarizes caselaw to allow comittments to guarantee to be unilaterally terminated under certain circumstances

KEY ASPECTS

- Ruling 1/2025 of January 8 ("**Ruling 1/2025**") of the Portuguese Supreme Court of Justice ("**SCJ**") establishes caselaw to the effect that it is admissible to unilaterally terminate (*denunciar*) a commitment to guarantee (*vinculação para aval*) by a guarantor (*avalista*) who ceases to be shareholder or shareholder-director of the company subscribing the promissory note (*livrança*) before it has been completed.
- However, unilateral termination is only allowed if the underlying contract or completion agreement does not provide for a fixed term—either because no term has been agreed upon or because an automatically renewable fixed term has been agreed, with the initial term having already elapsed.
- Unilateral termination will only take effect for amounts that become available after the termination date.
- To avoid having to disburse additional funds, the secured creditor may claim that the underlying legal relationship has been reconfigured due to the loss of the guarantee (*aval*).
- Ruling 1/2025 calls into question SCJ's previously established caselaw.

SCJ Ruling 1/2025 summary

On January 8, 2025, the SCJ issued Ruling 1/2025, which in short establishes the following caselaw:

- A commitment to guarantee granted on a blank promissory note (*livrança em branco*) can be unilaterally terminated by a guarantor who ceases being a shareholder or shareholder-director of the guaranteed company, provided the commitment to guarantee in question (i) has no term; or (ii) has a renewable term, with the initial term having already elapsed, and provided the guarantor does this before the blank promissory note is completed.

- Unilateral termination will only take effect for future amounts—that is, the unilateral termination will only apply to amounts requested after the termination takes effect.

Central legal issue

The central legal issue in this dispute was whether the guarantor of a blank promissory note could unilaterally terminate the guarantee (*aval*) once he ceased being the shareholder or shareholder-director of the company that subscribed the promissory note, provided the promissory note had not yet been completed by the respective holder.

The importance of this matter stems from the widespread practice of Portuguese banks requiring, as a condition for granting bank credit to companies, that their shareholders or shareholders-directors guarantee a security instrument (*título cambiário*) and sign the corresponding completion agreement (*pacto de preenchimento*)—that is, an agreement under which the guarantors and the company itself authorize the bank, in the event of any breach of the guaranteed contract, to fill in the security instrument with the amount due to the creditor bank on the completion date.

By providing this guarantee, the shareholders or shareholders-directors become personally and unlimitedly obliged to pay the amounts the bank may eventually put on the exchange note (*letra*) or promissory note (*livrança*) when it is filled out, as agreed in the completion agreement.

It is generally accepted that a shareholder or shareholder-director would, in principle, have reason to agree to guarantee the debt incurred by the respective company, considering the particular interest in the company's performance and the control that can be exerted over it. However, if the shareholder or shareholder-director no longer holds that status in the company in question, and considering that it was precisely that shareholder status that influenced the decision to be a guarantor, the following question arises:

Is it reasonable to require a former shareholder to remain indefinitely as guarantor of a company's obligations, even if such shareholder no longer controls or is part of that company?

Argument

For the purposes of the ruling, it was important for the panel of judges to consider the caselaw established over a decade ago in the SCJ's Uniform Caselaw Ruling 4/2013, of January 21. To summarize, in that ruling it was decided that, because a guarantee (*aval*) had been provided in an unrestricted and unlimited manner, it would not be admissible for the guarantor, who was a shareholder in the company that subscribed the promissory note, to unilaterally terminate the guarantee, even if he ceased being a shareholder in the meantime.

To distinguish the current understanding from that expressed in the 2013 ruling, the SCJ began its line of argument by identifying the differences between a guarantee (*aval*) provided on a complete promissory note and a guarantee (*aval*) provided on a blank security instrument, also known as "commitment to guarantee" (*vinculação para aval*).

Under the applicable legal regime, for exchange notes and promissory notes to be considered complete instruments, they must contain certain essential elements, such as the amount to be paid or the maturity date. Where any of these essential elements are missing, it is generally concluded that there is no true exchange note or promissory note, meaning there can be no true guarantee (*aval*).

A blank security instrument corresponds to an instrument that does not contain some of these essential elements. From the outset, it does not include the amount to be paid, which can be filled in by the creditor under the terms agreed upon in the completion agreement. Therefore, in the court's view, the guarantee (*aval*) of a blank security instrument does not represent a true security commitment (*vinculação cambiária*), but merely a pre-security commitment (*vinculação pré-cambiária*), and, as such, the applicable legal regime differs.

True security commitments—typical of complete security instruments—are characterized by (i) the incorporation of the right into the instrument, (ii) literalness, (iii) mutual independence, (iv) autonomy, (v) abstraction, and (vi) the fact that they are temporally delimited. For these reasons, they do not allow for application of the legal institute of the unilateral termination (*denúncia*).

However, pre-security commitments—such as blank security instruments—do not share these characteristics. Therefore, they may be unilaterally terminated under the general terms of the law.

Admissibility of unilateral termination of commitments to guarantee

Following this line of reasoning, the SCJ considers that the commitment to guarantee, as a pre-security obligation (*obrigação pré-cambiária*), is not yet a true guarantee (*aval*). Therefore, provided it constitutes a perpetual commitment, it can be unilaterally terminated at any time under the general terms of the law.

In its argument, the SCJ emphasizes the inadmissibility of perpetual or indefinite commitments, aligning with the widely accepted view among Portuguese legal scholars and in caselaw, which hold that the assumption of indefinite commitments must include the possibility of unilateral termination at any time, without requiring a specific justifying reason.

Therefore, in this particular case, the possibility of unilateral termination of the commitment to guarantee depends on the content of the underlying relationship (i.e., the credit agreement for which the guarantee was provided) or the completion agreement for the blank promissory note.

Accordingly:

- Whenever the underlying contract or the completion agreement provides for a fixed, determined, and non-renewable term, the unilateral termination of the legal relationship by the shareholder or shareholder-director acting as guarantor **is not allowed**.
- If the underlying contract or the completion agreement does not specify a fixed term, either because (i) no term was agreed upon (as in the case discussed here); or (ii) a fixed period was agreed upon but is automatically renewable, with the initial term having already elapsed, then the unilateral termination of the legal relationship by the shareholder or shareholder-director acting as guarantor **is allowed**.

In any case, the unilateral termination by the guarantor, after losing the respective status as a shareholder or shareholder-director of the guaranteed company, when allowed, only takes effect for obligations assumed **after** the date the unilateral termination is communicated to the secured creditor.

If the secured creditor receives a communication of unilateral termination from the guarantor, the creditor may, in accordance with the law, claim that the underlying legal relationship has been reconfigured due to the loss of the guarantee, and refuse to release additional funds, invoking the exception of non-performance, requesting the termination of the contract, or negotiating a modification of the underlying contract. If the secured creditor does not exercise any of these

options, it assumes the risk of the reduction or loss of the guarantee due to the guarantor's unilateral termination.

Lastly, note that the ruling was issued with several dissenting opinions, mainly arguing that the loss of shareholder status—rather than individual freedom—should be the central basis for the termination—rather than unilateral termination—of the pre-security relationship.

Conclusion

To conclude, SCJ Ruling 1/2025 standardizes caselaw to the effect that a commitment to guarantee granted on a blank promissory note may be unilaterally terminated by the guarantor if the guarantor ceased being a shareholder or shareholder-director of the guaranteed company, provided (i) this unilateral termination occurs before the instrument is completed; and (ii) the commitment to guarantee does not have a fixed term or is established with a renewable term, with the initial term having already elapsed. In any such case, the unilateral termination only takes effect for the future.

This possibility is legally grounded in the protection of individual freedom, considering the inadmissibility of perpetual commitments under Portuguese law.

While acknowledging the merit, practical relevance, and innovative nature of this SCJ ruling, it is important to stress that its applicable scope is limited to cases where the guarantee is provided based on a perpetual commitment. Therefore, this caselaw does not apply to cases where the guarantor of a blank security instrument ceased to be a shareholder or shareholder-director of the subscribing company when fixed-term contracts are involved.

In such cases, the solution must necessarily be **contractual**, **ideally through an agreement reached at the time the guarantor's shares are sold**: the withdrawal of the commitment to guarantee and the unilateral termination of other guarantees provided can be required as a condition precedent to the sale of the respective shares to the purchaser. However, if this is not possible because—for example—the creditor bank does not agree to the unilateral termination or cancellation, alternative arrangements may be agreed to allocate responsibility for the payment of any amounts that may be demanded from the seller as a result of the completion of the blank promissory note.