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GUARANTY—NOTICE OF ACCEPTANCE OF A GUARANTY—NECESSITY OF

No two terms have caused as much confusion, promoted as many misunderstandings, and have been used as interchangeably as "surety" and "guarantor." The North Dakota Code states that "A guaranty shall mean a promise to answer for the debt, default, or miscarriage of another person." [1] "A surety is one who, at the request of another and for the purpose of securing him a benefit, becomes responsible for the performance by the latter of some act in favor of a third person or hypothecates property as security therefor." [2] A close study of these two definitions will reveal that "guarantor" is the more general term than "surety." [3] Logically, then, every problem should be approached on the assumption that guaranty only is involved unless a basis can be found for inserting the particular obligation in the more limited catagory of suretyships.[4] Most courts never distinguish between guarantor and surety by using the above reasoning but base the distinction on other factors. The California Supreme Court in *Mahana v. Alexander* [5] held the fundamental distinction to be that a surety's obligation is original, while the guarantor's is collateral. The Mississippi Supreme Court points out that "A surety is an insurer of the debt or obligation while a guarantor is an insurer of the ability or solvency of the principle." [6] It is clear that courts have adopted no common standard in differentiating between these two terms.[7]

However, as much confusion arises out of the misuse of

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1 N. D. Rev. Code Sec. 22-0101 (1943)

2 N. D. Rev. Code Sec. 22-0301 (1943)

3 N. D. is a Field Substantive Code State and follows a minority view. Arnold, Outline of Suretyship and Guaranty, Sec. 9-10 (1927) states, "The courts recognize surety to be a more general term than guarantor; and in a statute employing the word 'surety' it will generally include guaranty, where there is nothing in the context to limit its application." *Accord*, Gagen v. Stevens 4 Utah 348, 9 P. 706. Plainly the Field Code does the very reverse of this.

4 10 So. Cal. Law Rev. 371, 375 (1937)

5 88 Cal. App. 111, 263 P. 260 (1927)

6 Biship v. Currie-McGraw Co., 133 Miss. 517, 97 So. 886, 889 (1923)

7 Shore-Mueller Co. v. Palmer, 141 Ark. 64, 216 S. W. 295 (1919). The Arkansas court expressed the view that the contract of a surety starts with the agreement, and that the liability of a guarantor is established for the first time with the default of the principal debtor. Brandt on Suretyship & Guaranty (3rd ed.) Sec. 2, states, "A surety is usually bound with his principal by the same instrument...but the contract of a guarantor is his own separate and a warranty that what is promised by the principal shall be done and not merely an engagement jointly with the principal to do the thing." *Accord*, Coleman v. Fuller, 105 N. C. 328, 11 S. E. 175, 8 L. R. A. 380 (1890).

the terms in the language of the courts as by the standards applied to them. The California Supreme Court, in discussing this problem, points out that "guaranty" and "suretyship" are synonymously or interchangeably used, and frequently, erroneously so. In many of the cases dealing with a suretyship contract the word "guarantee" is obviously used in its colloquial, and not its technical sense, as, for illustration, "the surety, by his contract, guarantees; stating the nature of the obligation or what he has agreed to do." [8] The Michigan court stated that the authorities, in discussing certain principals common to both, often use the terms interchangeably.[9] Pennsylvania solved the problem by passing a statute providing that all written agreements made by one person to answer for the default of another shall subject such person to the liabilities of suretyship unless such agreement shall contain in substance the following words, "This is not intended to be a contract of suretyship." [10] The Pennsylvania court commenting on this statute pointed out that the act was passed to clarify "guaranty" and "suretyship" as they are frequently used interchangeably with little understanding of the technical differences distinguishing the two.[11] It is apparent that the courts do not agree as to what constitutes the technical distinction.[12] As early as 1929 Radin suggested

Arnold, Outlines of Suretyship & Guaranty, Sec. 7, 9-13. (1927)

that the distinction be abolished in California because it has no roots in the past and no sense in the present.[13] Looking about, it can be seen that other jurisdictions find many identical and indistinguishable features between the terms. Thus, in *Siben v. Green* [14] the counsel for the defendant was arguing that a distinction existed between a contract of guaranty and of suretyship when the Court said, "We are not sure that we see the distinction as clearly as the counsel do . . . " Many other courts have failed to recognize a distinction and many have fallen into error by using the words "guaranty" and surety-

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[8] Mahana v. Alexander, *supra.*

[9] In re Kelley's Estate, 173 Mich. 492, 139 N. W. 250, 252 (1913). The New Jersey court stated in *Newark Finance Corp. v. Ascocella,* 115 N. J. Law 388, 180 A. 862, 863 (1935) that, "The words 'guaranty' and 'surety' have frequently been used synonymously. There is, however, a distinction."

[10] Title 8 Sec. 1, 1936 Penn. Statutes.

[11] In re Wever's Estate, 317 Pa. 497, 177 A. 51 (1935).

[12] Mahana v. Alexander, *supra;* Bishop v. Currie-McGraw Co., *supra;* and

[13] 8 Cal. L. Rev. 21, 30 (1929).

[14] 8 So. 2d 706, 708 (La. 1942).

ship" indiscriminately.[15] California in 1939 amended its statute, abondoning the distinction.[16] The Louisiana Court also does not recognize any distinction and in the leading case of *Bank & Trust Co. v. Barhet* [17] the court stated that "a guaranty of a debt which another person owes is essentially an obligation of suretyship, in whatever form the contract may be worded."

The former discussion has been introductory information to present a foundation for the discussion of a problem which is closely related thereto. This problem involves the N. D. Code Sec. 22-0106.[18] The statute states: "A mere offer to guaranty is not binding until notice of its acceptance is communicated by the guarantee to the guarantor. An absolute guaranty is binding upon the guarantor without a notice of acceptance." A cursory examination will reveal that there are two forms of guaranty set forth in this statute, an offer to guaranty and an absolute guaranty. As a general proposition a vast number of cases dispense with notice of acceptance when the guaranty is "absolute." [19] The use of the term "absolute" is a misnomer since all guaranty and suretyship contracts are conditioned on the principal's default. Also, many courts contrast the expression with "offer of guaranty" [20] which is an invalid distinction since all guaranties are revocable offers unless contractual requisites are fulfilled.[21] As pointed out in Williston on Contracts [22] the difference between an absolute and offer of guaranty is wholly formal. Again, an absolute guaranty is indistinguishable from a suretyship, where notice of acceptance also is not necessary, unless specfically stated in the contract.[23] The same principles seem ap-

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15 Chicago Title & Trust Co. v. Tax Theaters Corp., 91 F. 2d 907, reversing D. C., 15 F. Supp. 109 (1937); Riddle v. Thompson, 104 Pa. 330. Here the assignors of a judgment "guaranteed payment thereof in one year from this date." The court held that the words created a suretyship and that the assignors were not guarantors, but sureties.

16 Everts v. Matteson, 132 P. 2d 476, cites Calif. Code abolishing distinction between guarantors and sureties. (Stats. 1939, Ch. 453, P. 1796 Sec. 10, amended by Civil Code Sec. 2787, 1941).

17 177 La. 652, 148 So. 906 (1933). *Accord,* La-Brock v. First State Bank and Trust Co., 187 La. 766, 175 So. 569 (1937).

18 N. D. Rev. Code of 1943

19 Davis v. Wells, 104 U. S. 159, 26 L. Ed. 686 (1881).

20 Standard Sewing Machine Co. v. Church, 11 N. D. 420, 92 N. W. 805 (1902); Rogers Lumber Co. v. Clark, 52 N. D. 607, 204 N. W. 184 (1913); Fisk v. Stone, 6 Dak. 35, 50 N. W. 125 (1888).

21 35 Mich. L. Rev. 529.

22 Williston on Contracts, rev. ed. Sec. 69, note 8 (1936).

23 Treweek v. Howard, 105 Cal. 434, 39 P. 20 (1895).

plicable to both. Notice of acceptance given in a reasonable time is held to be necessary by many courts.[24] The reason given for such notices of acceptance are: (1) the guarantor has an opportunity to protect himself against risk;[25] (2) it is not fair to bind the guarantor without notice being given him;[26] (3) the guarantor is entitled to know whether his offer is accepted;[27] and (4) like other contracts the courts reason that notice of intention is essential to mutual consent.[28] These arguments seem feasible until the other side of the picture is presented. The Minnesota Supreme Court declined to follow the rule that notice of acceptance was necessary because they considered the rule contra to the elementary principles of the law of contracts. This court pointed out, "Where the offer contemplates the performance or forebearance from an act as the consideration of the promise of the offeror, then performance or forebearance is an acceptance, unless the offeror expressly or impliedly prescribes that the acceptance must be communicated.[29] "The act of extending credit, standing alone without notice to the guarantor is in itself sufficient acceptance of his undertaking." [30] The writer believes this to be the better rule as it is a direct application of contract law to a *contract* of guaranty. However, an equitable result will not be had if in all cases the rule of no necessity to give notice on the obligee's part is applied. The Illinois Court depicts that the right to notice is not absolute but a relative right, and the failure to give it can only be available as a defense when it is made to

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[24] Davis v. Wells, *supra;* (For early cases in point see note 5 Col. L. Rev. 215, 223); This doctrine that notice of acceptance is required in contracts of guaranty rests upon the dicta of Chief Justice Marshal in Russel v. Clark's Exr's., 7 Cranch 69 (1812) and of Justice Story in Cremer v. Higgenson, 1 Mason 323, Fed. Case 3,383 (1817); Adams v. Jones, 12 Pet. 207, 9 L. Ed. 1058 (1838) (Another early opinion by Justice Story.)

[25] Hudepohl Brewing Co. v. Bonnister, 45 F. Supp. 201 (1942) S. C.; Webb v. Cope, 192 S. W. 934 (Mo. 1917).

[26] Hunsley Paint Mfg. Co. v. Grey, 165 S. W. 2d 486 (Tex. 1942).

[27] Cozzani v. Fioravanti, 51 R. I. 433, 155 A. 409 (1931).

[28] Davis v. Wells, *supra;* M. E. Smith & Co. v. Kimble, 31 S. D. 18, 139 N. W. 348 (1906); Standard Sewing Machine Co. v. Church, 11 N. D. 420, 92 N. W. 805 (1902).

[29] Midland Nat. Bank v. Security Elevator Co., 151 Minn. 30, 200 N. W. 851 (1924); Taylor v. Hoke, 92 Colo. 330, 20 P. 2d 546 (1933) quoting from Clark on Contracts (3rd Ed.) Sec. 27, "But it is held where notice is required, knowledge or information coming to the guarantor, through any source, that the guarantee is acting under the guaranty and extending credit on the strength thereof, is tantamount to direct notice."

[30] Midland Nat. Bank v. Security Elevator Co. *supra; accord,* Royal Tailors v. Newton, 66 Utah 154, 239 P. 949 (1925) citing Frost v. Standard Metal Co., 215 Ill. 240, 74 N. E. 139 (1905).

appear that the guarantor has suffered some loss by such failure.[31] In *Bishop v. Eaton* the Massachusetts Supreme Court stated that ordinarily there is no occasion to notify the guarantor of acceptance as the doing of the act is sufficient, but, if the act is of such a kind that knowledge will not quickly come to the guarantor, the obligee is bound to give notice of acceptance.[32] The courts, holding notice of acceptance not necessary, have in reality disregarded the distinction between contracts of guaranty and suretyship and have applied the suretyship rule, that notice of acceptance is not necessary,[33] to a contract of guaranty. What could be more logical than to bring contracts of guaranty in harmony with suretyship law and contract principles, the solution being the abolition of the technical distinction between guaranty and suretyship and the application of suretyship rules (in reality principles of contracts) to both.

North Dakota, having only two cases relating to the necessity of notice in contracts of guaranty, can be used to illustrate the confusion existing among all jurisdictions in this manner. The first decided case was *Fisk v. Stone.*[34] Here a young lady was starting a millinery business and could not obtain any goods on credit unles payment was guaranteed. Enclosed with an order, the new proprietor sent a letter of defendant guarantor which stated, "... If you will send her goods as she may order; not exceeding $300 due you at any one time, I will guarantee that you are paid in full." This was held to be an absolute guarantee by the North Dakota Supreme Court and no notice of acceptance was necessary. Even if construed as an offer of guaranty the court thought that having communicated through the debtor the defendant waived his right to notice of acceptance. However, in the next decided case, *Parlin v. Hall,*[35] the court failed to recognize an absolute guaranty. The plaintiff sold groceries to Mrs. Hall when informed by Mr.

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31 Mamerow v. National Lead Co., 206 Ill. 626, 633, 69 N. E. 504, 507 (1903).

32 Bishop v. Eaton, 161 Mass. 496, 500, 37 N. E. 665 (1894). Restatement of the law of Securities Sec. 86 (1941) states the identical rule but applies it to sureties.

33 N. D. Rev. Code Sec. 22-0304 (1943) "In interpretating the terms of a contract of suretyship, the same rules are to be observed as in the case of other contracts." Williston on Contracts, Sec. 68 (1920) "As to ordinary unilateral contracts, the rule is that mere performance of the act required is enough without communication."

34 6 Dak. 35, 50 N. W. 125 (1888).

35 2 N. D. 473, 52 N. W. 405 (1892).

Hall that the defendant guaranteed payment up to $200 on any groceries ordered. The instrument contained these words, "... that whereas, the said party of the first part has agreed to guaranty the grocery bill of said second party, contracted for use on the premises hereinafter described, at any place said second party may select to trade, not exceeding the sum of two hundred ($200) dollars in any one season..." The trial court held this to be a guaranty, but, the Supreme Court construed the rest of the instrument, in conjunction with the part set forth above, not to be a letter of credit. The majority opinion did nothing but interpret the words of the contract to arrive at the conclusion that this was no guaranty, nor was it specifically intended for the benefit of the plaintiff. Justice Bartholomew dissenting, with whom the writer agrees, criticizes the majority view in that they did not consider the intent of the parties. In his dissenting opinion the judge pointed out that Mr. and Mrs. Hall believed this to be a guaranty when they received the instrument from the guarantor. Also the statement of Mr. Hall to the plaintiff that the defendant had guaranteed the grocery bill indicates the intention of the Halls that the instrument was a guaranty. Bartholomew stated, "It is, as I think, simply a question between a guarantor and guarantee, and I fear that the court by its too literal adherence to the strict letter of the wording has relieved appellant of a liability that he fully intended to incur when he signed the contract." *Standard Sewing Machine Company v. Church* [36] dealt with the distinction betwen an absolute and a mere offer of guaranty. The Guaranty stated, "In consideration of your supplying J. N. Edmunds . . . with sewing machines and articles connected therewith on credit, do hereby guarantee the payment of the price and value of said goods at maturity to an amount not to exceed ($1,000) dollars,... this agreement to be held as continuing security in your favor, and to cover any and all renewals of the debts, notes, or acceptances which may from time to time be made..." The guarantor delivered this instrument to Edmunds, no agents of the plaintiffs being present. The court determined this instrument to be an offer of guaranty as there was no meeting of the minds necessary to the existence of a completed contract, hence notice

[36] 11 N. D. 420, 92 N. W. 805 (1902).

of acceptance by the plaintiff must be given.[37] No reasonable man reading this instrument could possibly see a need for notice of acceptance. By its terms the contract is for one thousand dollars, a definite amount. Also, the phrase "this agreement to be held as continuing security in your favor and to cover any and all renewals of debts, . . . " imports the interpretation of an absolute guaranty. Certainly notice of acceptance would not have to be given for each new debt renewed thereunder, then why is not the supplying of sewing machines by the plaintiff acceptance of the offer and a meeting of the minds of the parties. In *Singer Manufacturing Company v. Freeks and Propper* [38] a bond was issued by guarantors in consideration of employment of one Clement by the plaintiff company. The bond was issued upon the request of Clement and given by the guarantors to Clement who in turn transmitted it to the plaintiffs. The trial court, applying the reasoning of the *Standard Sewing Machine Co. Case,*[39] determined this to be an offer with notice of acceptance by the plaintiffs necessary. The Supreme Court reversed the decision holding that when the guarantors signed the bond and left it with Clements to deliver to the Machine Company as the bond Clement had agreed to furnish, the mutual assent was present and no further act or notice was necessary. In reality the the court is classifying this as an absolute guaranty or suretyship where notice is not necessary. The writer believes the beter view to be set down in this case. The facts of the *Standard Sewing Machine* and the *Singer Manufacturing Cases* are almost identical and it is difficult to reconcil the contrasting decisions. The trial court in *Emerson Manufacturing Co. v. Tvedt and Rustad* [40] also applied the doctrine of the *Standard Sewing Machine Co. Case,* however, the Supreme Court stated that the doctrine as there set forth was inapplicable and reversed the decision of the trial court, holding now for the plaintiff. Upon the back of an order made by Tvedt for certain machinery Rustad signed the following guaranty, "In consideration of one dollar to me in hand paid by Emerson Manufacturing Co. (Plaintiff), the receipt which I hereby acknowledge, I hereby guarantee the fulfillment of the within

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[37] This is the majority view but is not in accord with contract principles.
[38] 12 N. D. 595, 98 N. W. 705 (1904).
[39] *supra.*
[40] 19 N. D. 9, 120 N. W. 1094 (1909).

contract . . . " This instrument showing consideration moving directly from the plaintiff, the guarantee, to Rustad, the guarantor, was absolute and no notice was held necessary. Even if the consideration was nominal or in fact never paid, the result would not be changed,[41] mutual assent was proved, and the delivery of the guaranty would complete the contract.[42] *Rawleigh Medical Co. v. Laursen*,[43] contained an express waiver of notice and acceptance in the instrument, hence the Supreme Court held notice not necessary. Even if no waiver was present the court indicated notice would not be necessary. The appellant, arguing notice of acceptance was necessary, expressed the view that in order to waive notice of acceptance, there must be consideration expressed in the guaranty. It was pointed out that when the plaintiff accepted the guaranty and began to ship goods, thereunder, "a consideration sprang into existence." The application of the principle, that consideration arises when the guarantee acts, to the *Standard Sewing Machine Case* [44] would change the result therein.[45] *Rogers Lumber Co. v. Clark* [46] again illustrates the uncertainty of the courts in this field. Here Kunkel went to the plaintiff lumber company to purchase some needed repairs. The plaintiff drew up an estimate but indicated no lumber would be sold unless Kunkel got a guaranty. Kunkel then went to the bank and procurred the following guarantee attached to the estimate, "Please let S. S. Kunkel have this bill of lumber, and I will guarantee payment. Better take his note." The defendant had the case dismissed by a directed verdict on the grounds that the offer to guarantee was conditional and the plaintiff did not inform the defendant of the acceptance of the offer. The writer can see no justification for this decision as Kunkel went to the defendant bank upon the request of the plaintiff and when the bonds were furnished there was a meeting of the

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41 Davis v. Wells, 104 U. S. 159, 26 L. Ed. 686 (1881).

42 Pruden v. Liebick, 22 N. D. 591, 135 N. W. 186 (1912) *in accord.*

43 25 N. D. 63, 141 N. W. 64 (1908).

44 *supra.*

45 Note: *Aluminum Cooking Utensil Co. v. Rome*, 43 N. D. 433, 175 N. W. 620 (1919) was decided on the pleadings. However, the court in dicta indicates the following guaranty is only an offer and notice is necessary. "In consideration of your taking into or continuing in, your employ Irvin E. Harris . . . I hereby agree to pay you forwith for all goods ordered . . . my liability not to exceed two hundred dollars ($200.00)." This case is not in accord with the Fisk Case, *supra;* Rawleigh Medical Co. v. Laursen, *supra;* and Singer Mfg. Co. Case, *supra.*

46 52 N. D. 607, 204 N. W. 184 (1913).

minds and adequate consideration to form a contract. The result obtained in the *Standard Sewing Machine Company Case* was followed herein and again led the court astray from sound principles of contracts.[47] All jurisdictions could hand down more equitable decisions if (1) guaranty and suretyship obligations were identical and (2) the rules of contracts were applicable in all cases.

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[47] See Fist Case, *supra;* Emerson Mfg. Co., *supra;* Rawleigh Medical Co., *supra;* and Singer Mfg. Co., *supra;* for contra views in North Dakota. Note: Only other N. D. case on this matter, *State of N. D. ex rel Fay Harding,* 60 N. D. 703, 236 N. W. 353 (1931), distinguishes between a surety and a guarantor, holding there was a suretyship obligation, thus notice of acceptance was not necessary.