

LAWXPERTSMV**CONTRACT OF GUARANTEE AT A GLANCE****CONTRACT OF GUARANTEE**

Definition of Guarantee : Relevant Provision: Section: 126:

Contract of guarantee = A contract to perform the obligation or to discharge the liability of a third party.

When ? In case of its default.

Consideration for contract of guarantee = Anything done, or any promise made, for the benefit of the principal debtor.

Liability in contract of guarantee:

- **Primary liability** – It is on the principal debtor
- **Secondary liability**- This liability goes to surety.

The Essentials of a Contract of Guarantee :**Essential I: The existence of tripartite Agreement:**

- **Contract 1: Debt agreement**- Between principal debtor and creditor.
- **Contract 2: Indemnity agreement**- Between principal debtor and surety
- **Contract 3: Actual guarantee agreement**- Between the creditor and the surety

Essentials II- It requires all essentials of a Valid Contract

Essential III- The principal debt must pre-exist

Form of Contract of guarantee: It can be both oral and written .

Uberrimae fidei contracts:

- ✓ **Uberrimae fidei**= contract 'requiring absolute good faith.' Contract of insurance as contract of uberrimae fidei

- ✓ **Unfortunately !** A contract of guarantee not a contract of uberrimae fidei .
- ✓ **Thus !** Due to this reason the principal debtor or the creditor may not disclose material facts to a surety before making a contract.
- ✓ **Lx Explains:** If a guarantee is given to a bank, the bank may not inform the surety of the matters that pertain to the credit of the principal debtor.
- ✓ **But !** still the suretyship relationship is one of trust and confidence
- ✓ **Therefore !** Even though contract of guarantee does not require utmost good faith – it requires minimum good faith, thus the provision of Section 142 and 143 makes guarantee as invalid on misrepresentation and concealment of material facts.

RIGHTS OF SURETY

Right of the Surety as against Co-Sureties:

1. **Right to claim Contribution:** Surety can ask his co-sureties to contribute the amount when principal debtor comes across default. **Law of England:** contribution = ratio of guarantee amounts. **Indian Law:** Contribution = share of deficit or guarantee amount which ever is less.
2. **Right to claim for share in securities :** When co-sureties make payment to creditor, they get securities from creditors procession.

Right of Surety as against the Creditor:-

1. **Rights of Sub-rogation:** Surety gets creditors rights after payment.
2. **Right to stay informed and consulted-** alteration of contract without approval of surety discharges him# Sec. 133
3. **Right to ask for Set-off:** Surety can give advice to creditor to sell away the security and to utilize the amount thus realized for set off.
4. **Right to get discharged when principal debtor is discharged # Sec. 134**
5. **Right to get Securities from creditor after payment.**

Right of Surety as Against the Principal Debtor

1. Right of Subrogation- After the payment of the debt to the creditor, the surety is subrogated to the rights of the creditor.

2. Right of Indemnity- In every contract of guarantee, there is an implied promise by the principal debtor to indemnify the surety i.e., to compensate the surety.

3. Right to be Relieved Earlier- A surety can, even before making any payment, compel the debtor to relieve him from liability by paying off the debt.

LIABILITY OF SURETY

Basic principle= The liability of the surety is coextensive with that of the principal debtor, unless it is otherwise provided by the contract.

What it implies:

- 1) When the principal debtor gets discharged the surety will also be discharged.
- 2) Creditor can sue surety for money without proceeding against principal debtor # *State Bank of India v. M/s. Indexport Registered.*

CONTINUING GUARANTEE

Definition: Provision: Section 129- a guarantee which extends to a series of transactions is called a continuing guarantee.

Revocation : A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor.

DISCHARGE OF SURETY

The secondary liability of the surety comes to an end by following modes:-

- Discharge by revocation of guarantee.
- Discharge by activities of creditor.
- Discharge by invalidation of guarantee contract.

DISCHARGE BY REVOCATION OF GUARANTEE

By the following modes the guarantee stands revoked.

1. **By Notice:** Surety can revoke his guarantee by giving a notice to creditor only in continuing guarantee for future debts.

2. **By Death:** Whenever surety dies - **Specific guarantee-** legal representative has to take up the secondary liability absolutely. **Continuing guarantee=** legal representative is liable to the debts granted till the date of filing death notice by legal representative.
3. **By Renewal:** Whenever renewal of guarantee contract takes place, old guarantee comes to an end and new one comes into live.

DISCHARGE BY ACTIVITIES OF CREDITOR:

1. **Material Alterations:** Creditor makes material alterations in guarantee contract deed, without consent of surety discharge of Surety occurs # **Witcher Vs Hall**.
2. **Releasing principal debtor:** Principal debtor discharged the surety also gets discharged # **Hewson Vs Ricketts**.
3. **Any fraudulent activities of creditor or principal debtor or both discharges the surety#** Midlon motor show rooms Vs Newman.
4. When the creditor realises his debt through the additional sureties given then both principal debtor and surety stands discharged.

Discharge by invalidation of guarantee contract: When guarantee contract becomes invalid then surety will have no secondary liability.

GUARANTEE VS INDEMNITY

CONTRACT OF INDEMNITY	CONTRACT OF GUARANTEE
Number of parties: 2	3
Names of parties: Indemnifier and Indemnity holder	Creditor, Principal debtor and surety.
Number of Contracts: 1	3
Nature: As indemnity contract includes two parties and one contract, it can be said that indemnity contract is simple in nature.	But guarantee contract includes three parties and three sub-contracts and hence be said that guarantee contract is complex in nature.

Liabilities: In contract of indemnity there is no classification and sharing of liability where the absolute liability rests with indemnifier	In contract of guarantee there will be two types of liabilities namely; primary and secondary liabilities which will be with principal debtor and surety respectively.
Recovery methodology: In case of indemnity contract the indemnifier, after compensating indemnity holder's loss, cannot recover that amount from any person.	In contract of guarantee, if surety makes payment to creditor, he (surety) can recover that amount from principal debtor.
Interest of parties: Indemnity contract gets formed upon indemnifier's interest	Guarantee contract gets formed upon principal debtor's interest.