

CONTRACT OF GUARANTEE



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Contract of Guarantee

SEC- 126-147

Definition

- Sec. 126- “A Contract of a guarantee is a contract to perform the promise or to discharge the liability of a third person in case of his default.”

PARTIES TO THE CONTRACT OF GUARANTEE

- **PRINCIPAL DEBTOR**
- **SURETY**
- **CREDITOR**

Contd.

- **Principal Debtor-** The person who makes default or the person in respect of whose default the guarantee is given is said to be Principal Debtor.
- **Creditor-** The person who lend money to principal debtor or the person to whom the guarantee is given is called as the Creditor.
- **Surety-** The person who gives guarantee to creditor on the behalf of principal debtor is called as Surety.

ESSENTIALS OF CONTRACT OF GUARANTEE

- There are three parties in a Contract of Guarantee
- There should be a principal debt.
- There should be a consideration as per the sec. 127- anything done or any promise made for the benefit of the principal debtor may be a consideration to the surety for giving the guarantee.
- Consent of surety should not have been obtained by misrepresentation or concealment. (Section- 142 & 143 of Indian Contract Act)

IN CONTRACT OF GUARANTEE -

- There are three parties involved i.e. the person who gives the guarantee known as the surety, the person in respect of whose default the guarantee is given known as the principal debtor and the person to whom the guarantee is given known as the creditor.
- There are three contracts first between the creditor & the principal debtor, second between the surety & the creditor and third between the surety & the principal debtor.

Contd.

- The primary liability is of principal debtor and the surety has a secondary liability which means that the payment is to be made by the surety only if the debtor fails to pay.
- This contract is for the security of the creditor.
- This contract can be oral or written but cannot be implied .
- Till such time as the obligation of the principal debtor does not arise the surety is also free from his obligation.

TYPES OF GUARANTEE

A guarantee may be of the following types:

1. **Retrospective guarantee**- A guarantee given for an existing debt or obligation is called Retrospective guarantee.

2. **Prospective guarantee**: A guarantee given for future debt or obligation is called a Prospective guarantee. This guarantee is of two types –

➤ *Specific Guarantee*

➤ *Continuing Guarantee*

Contd.-

Specific Guarantee : It is given for single debt or obligation and comes to an end when the debt guaranteed has been paid or obligation guaranteed has been discharged. Thus, where A gives a loan to B for which C stands guarantee, it is a case of a specific guarantee. In this case, there is a specific debt and the guarantee shall come to an end the moment the loan is repaid. Specific guarantee once given is irrevocable.

e.g. –A guarantees the repayment of a loan of s. 20 Lakh to B by C . The guarantee in this case is a specific guarantee.

Contd.-

- *Continuing Guarantee* : A continuing guarantee is one where the guarantee given is not for a single or specific debt or obligation, but for a series of transactions. It is generally for an indefinite time or until the end of the guarantee. It is terminated in the following two ways:
 - ❑ By Notice
 - ❑ By Surety's Death

Contd. Continuing Guarantee-

e.g.- A guarantee payment to B, a tea- dealer, to amount of Rs. 10,000 for any tea he may from time to time supply to C. B supplies C with tea of the value above Rs. 10,000 and C pays for it. Afterwards B supplies C with tea to the value of Rs. 15,000 , C fails to pay. The guarantee given by A was a continuing guarantee and he is accordingly liable to B to the extent of Rs. 10,000

LIABILITY OF SURETY

The important points regarding the liability of the surety:

- ☐ The liability of surety is co extensive with that of the principal debtor
- ☐ Liability of surety commences with the default of the principal debtor
- ☐ Liability of co – sureties

DISCHARGE OF SURETY FROM LIABILITY

The surety is discharged from his liability in the following situations:

- ❖ By notice of revocation
- ❖ By surety's death
- ❖ By variation in the terms of the original contract By release of the principal debtor
- ❖ Agreement with the principal debtor
- ❖ By the creditor's act or omission impairing surety's remedy
- ❖ Loss of security by the creditor
- ❖ Guarantee obtained by misrepresentation or concealment
- ❖ Guarantee given under the condition of joining of co-sureties.

RIGHTS OF SURETY

RIGHTS AGAINST DEBTOR

- Right of subrogation.
- Right to be indemnified.

RIGHTS AGAINST CREDITOR-

- Right to securities.
- Right to get information about debtor's conduct.
- Right to set off-if he has to settle his own amt. from creditor.

RIGHTS AGAINST CO-SURITIES-

- **Right to claim contribution—**
 - *IN CASE OF CO-SURITIES OF EQUAL AMT.*
 - *IN CASE OF CO-SURITIES FOR DIFFERENT SUMS.*
 - *IN CASE OF DISCHARGED CO-SURETY*

**THANK
YOU**