Private Law: Security Devices

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SECURITY DEVICES

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SURETYSHIP

Louisiana Civil Code article 3045 grants the right of discussion to a surety in the following terms:

The obligation of the surety towards the creditor is to pay him in case the debtor should not . . . and the property of such debtor is to be previously discussed . . . unless the surety should have renounced the plea of discussion or should be bound jointly in solido with the debtor in which case the effects of his engagement are to be regulated by the same principles which have been established for debtors in solido (emphasis added).

The unsatisfactory nature of the right of discussion has caused creditors to require its waiver almost universally. This is ordinarily accomplished by having a surety stipulate he is bound "in solido" with the debtor. The last clause of article 3045 seems to indicate such an agreement has a greater effect than a simple waiver of the right of discussion by implying the effects of such a contract are regulated by "the same principles which have been established for debtors in solido." This presents difficulties in that the rules regulating the liability of solidary obligors in some cases conflict with those regulating suretyship.¹ The courts have been inconsistent as

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¹ The most significant of these conflicts can be summarized as follows:
(1) The remission of the debt in favor of the principal obligor releases a surety absolutely, while the remission of the surety's obligation has no effect upon the liability of the principal debtor. LA. CIV. CODE art. 2205. On the other hand, the remission of the obligation as to one solidary obligor completely releases the other obligors unless the debtor reserves his rights against them, in which event, however, he is bound to reduce his claim against the remaining debtors by the part of him who has been released. Id. art. 2203. (2) An extension of the time or prolongation of the term of the indebtedness given to the debtor releases a surety but does not release a co-obligor who is bound in solido. Id. art. 3063. (3) A surety who pays the primary obligation without being sued by the debtor loses his right to contribution from his co-sureties. Id. art. 3058. (4) The filing of a suit against or acknowledgment of the debt by one solidary obligor interrupts prescription as to all solidary obligors. A suit against the surety or an acknowledgment of the debt by him does not serve to interrupt the prescription running against the primary debtor. Id. arts. 2097, 3552.
to which set of rules applies to the surety who stipulates he is bound "in solido" with the debtor, and have never articulated a satisfactory rationale for determining which rules are applicable. In *Louisiana Bank and Trust Co. of Crowley v. Boutte*, four shareholders of a corporation had executed a continuing guaranty agreement in favor of the plaintiff bank by which they agreed to pay certain indebtedness of the corporation "as sureties in solido." The corporation defaulted on its loans and after filing a suit against it and the four sureties, the bank compromised its claim with the corporation and three of the sureties. It expressly reserved "its rights" against the remaining surety, who then pleaded he had been released because of the discharge granted to the principal debtor, the corporation.

The Louisiana Supreme Court held that inasmuch as the sureties had agreed to be bound *in solido* with the corporation, article 3045 rendered the rules of suretyship inapplicable, that the surety's relationship with the creditor should be governed by the rules of solidarity, and that accordingly the bank could recover from the surety, but only after deduction of four-fifths of the debt as the part of those who had been released. It thus treated the three other sureties and the corporation as four of five solidary obligors. The court summarized the reason for its holding as follows: "[T]he effect of the application of these articles [3045 and 2106] is such that as between the creditor and the solidary surety the obligations of the surety are governed by the rules of solidary obligors . . . . Among the co-obligors, however, bound *in solido*, the relationships may be governed by the rules of suretyship."

The differences between the effects of suretyship and those of solidarity arise from the basic nature of the undertakings of the obligors. The rules pertaining to one arrangement cannot consistently be applied to the other without reaching conclusions that are inherently contradictory. This fact has generally been obscured in the cases because the

2. 309 So. 2d 274 (La. 1975). The case also contains an extensive discussion of the jurisprudence on the subject.

3. "The remission or conventional discharge in favor of the co-debtors *in solido*, discharges all the others, unless the creditor has expressly reserved his right against the latter.

   In the latter case, he can not claim the debt without making a deduction of the part of him to whom he has made the remission." LA. CIV. CODE art. 2203.

4. 309 So. 2d at 278.
liability of a surety who has waived the plea of division has sometimes been characterized as being "solidary" in nature. However, such solidarity is not that of a "solidary obligor" as defined by the code.

The term "solidarity" is commonly used in two senses. In its most common usage it refers to a situation in which two or more parties have jointly bound themselves for the performance of a single obligation with the same cause and have agreed with the creditor that he may seek performance from any or all of them indistinguishably. The term also refers to any situation in which a creditor may call upon any one of several parties for performance when that performance will discharge all of the parties who may be bound to him, even though their liability may arise from different obligations with different causes.

The "solidarity" inherent in the contract of a surety who has waived the plea of discussion is of the latter nature. Suretyship is a separate, nominate agreement between the surety and the creditor regulated by its own terms. No contractual relationship need exist between the surety and the debtor whose obligation is guaranteed. More importantly, suretyship is by its nature accessory to the obligation the surety guarantees; it is given to secure the performance by

5. "The contract of suretyship under these provisions of law is of mixed character. The obligation of each surety is to pay the whole debt. But this solidarity is tempered by the right of division. This right, however, rests in facultate. The surety has the right to demand the division but until the right is exercised the obligation is solidary." McCausland v. Lyons, 4 La. Ann. 273, 274 (1849). "The obligation sued upon is manifestly one of suretyship; and solidarity is of the nature of that contract." Kilgore v. Tippit, 26 La. Ann. 624, 625 (1874) (emphasis added).

6. "Where there are more than one obligor or obligee named in the same contract, the obligation it may produce may be either several or joint or in solido. . . ." LA. CIV. CODE art. 2077. See also id., art. 2091.

7. The two types of solidarity are sometimes referred to as "perfect" and "imperfect." Although the validity of classifying solidarity in such a manner has been debated by civilians, it is clear that the code articles on solidarity assume, at least in matters of contract, a mutuality of interest between the obligors in solido with respect to the engagements of each other, whereas the articles on suretyship assume the surety to be acting independently of the primary debtor. Unless this is recognized in distinguishing the effects of the two concepts confusion will continue to occur in the cases. Perhaps the best and most succinct summary of the distinction in question is found in J. D. Smith, Louisiana and Comparative Materials on Conventional Obligations 350-51 (4th ed. 1973), discussing the case of Gay v. Blanchard, 32 La. Ann. 497 (1880), the leading Louisiana authority on the subject.
another, not to undertake independently direct responsibility for such performance.\textsuperscript{8} It is thus entirely consistent for a surety who, by waiving the right of discussion, has agreed to perform the obligation without requiring the creditor to first resort to an action against the primary obligor to characterize his liability as being "solidary" without intending to negate the essentially secondary and accessory nature of his undertaking.

On the other hand, the particular articles of the Civil Code regulating the rights and duties of solidary obligors clearly assume that there is but one obligation to which all obligors are a party. Since all are bound on the same undertaking, a contractual relationship is also assumed to exist between them so that each is to some extent bound for the performance of the other. At the same time article 2106 recognizes that one of them may in substance merely be lending his credit to the other.\textsuperscript{9}

The court in \textit{Boutte} not only failed to recognize the differences inherent in the nature of solidarity and suretyship but assumed that to characterize a debtor’s liability as being solidary requires the creditor to deal with the debtor in all circumstances as though he were responsible in equal proportions with the other obligor.\textsuperscript{10} It was thus led to the conclu-

\textsuperscript{8} "A principal contract is one entered into by both parties on their own accounts. . . . An accessory contract is made for assuring the performance of a prior contract, either by the same parties or by others; such as suretyship, mortgage and pledge." \textit{L.A. Civ. Code} art. 1771. The idea of the \textit{accessory nature} of security is absolutely fundamental to the civil law and permeates the concepts of suretyship, pledge, mortgage and privilege as they are expressed in the Code.

\textsuperscript{9} "If the affair for which the debt has been contracted \textit{in solido}, concerns only one of the coobligors \textit{in solido}, that one is liable for the whole debt towards the other codebtors, who, with regard to him, are considered only as his securities." \textit{L.A. Civ. Code} art. 2106.

\textsuperscript{10} The court noted that the question of whether the defendant might be liable for more than one-fifth of the debt was not before it because the plaintiff had not asked for an increase in the award of the court of appeal, which had in the first instance determined the defendant to be liable for such amount. However, its comments in this regard clearly indicate it had in mind the problem of whether the terms of the particular agreement might have imposed upon the defendant \textit{a greater} liability. In its affirmance of the decision of the court of appeal it necessarily determined that the defendant was liable for \textit{at least} one-fifth of the debt. The court obviously assumed that before it could hold the defendant to have been completely released it would have to determine that the contract before it was one of suretyship. "Defendant's argument that the release of the principal operated to discharge his,
sion that when article 3045 mentions that a surety who is bound “jointly in solido with the debtor” is to have the effects of his engagement regulated by the rules of solidarity, it was in fact declaring that a surety who says he is bound solidarily has renounced his accessory status.

If the rule of the Boutte case is applied to the situation in which one agrees to be surety in solido for another who is already bound for the debt without the knowledge or consent of the primary debtor, the error in the court’s opinion in this regard will become manifest. Under the Boutte case if the creditor releases the principal debtor but reserves his rights against the “solidary” surety he may still hold the surety for one-half of the debt. Conversely, if one consistently applies the rule, a release of the surety without a reservation of rights against the primary obligor would entirely release him. Even if the creditor reserves his rights he could hold the primary debtor for no more than one-half of the debt.

Of course, the Boutte case only stands for the proposition that rules of solidarity should be applied to the surety’s relationship with the creditor. It is not necessary to extend its holding to require that the same rules govern the liability of the primary debtor to the creditor. In fact, the release of the surety should not affect the primary debtor’s liability. Having unconditionally and primarily incurred the obligation without regard to the existence of the separate agreement of the surety, the debtor would have no complaint that his rights have been impaired or injured. Article 2106 makes it clear that the debtor who pays the debt has no claim for contribution against the surety. The surety’s release thus does him no harm, he is not a party to the surety’s agreement, and it does not violate his contract with the creditor. However, the same factors then suggest a proper application of the rules regulating the effects of solidarity lead to the conclusion, contrary to the result of the Boutte case, that the release of the primary debtor should completely release the “solidary” surety.

The remission of a debt as to one solidary obligor requires the creditor to reduce his claim against the other “for the part of him to whom he has made the remission.” 309 So. 2d at 276. It then determined it could not do this because of its understanding of LA. CIV. CODE art. 3045. 309 So. 2d at 279.

11. LA. CIV. CODE art. 2203.
if one of the debtors pays the whole debt he can claim contribution from the others for "no more than the part and portion of each." Article 2106 then provides that if the affair "concerns" only one of the parties he is deemed to be a primary obligor and the others are his sureties. Therefore, in such a case his "part" of the debt is the whole amount. Accordingly, his co-obligors may, as sureties, recover all of the debt from him if they have to pay it and he can recover nothing from them if he pays.

Now it is true that in many cases the creditor may be unaware of the relationship between his debtors. In the absence of a contrary agreement he may assume them to be equally interested in and proportionately liable for the debt. But this certainly would not be true if the creditor were to expressly recognize the part of the debt each of the debtors is to bear. The reasons for the rules relating to remission are completely in accord with this premise.

Ordinarily, a creditor could not release one solidary obligor from his obligation and still hold the other for the entire amount of the debt without violating the engagements he has made with each. For, if after releasing the first debtor the creditor were to call upon the second for the payment in full, the latter would immediately call upon the released debtor for contribution of his part of the debt and at the same time would demand to be subrogated by the creditor to the claim against the other debtor. This the creditor could no longer do. If the unreleased debtor is denied either contribution or subrogation, his rights have been severely abridged without his consent. On the other hand, if such rights are given to him then the creditor would be forcing the obligor whom he released to pay the debt from which he has been released. One may rationalize the rule embodied in article 2203 on either theory. In any event the result is the same and the principle is directly embodied in the article; a creditor may not recover that part of the obligation owed by the debtor to whom a release has been given.

A stipulation with a creditor that one will be bound "as a surety in solido" with another should ordinarily be equivalent to a stipulation by the creditor that the other debtor's "part" of the debt is the entire amount. Certainly in most cases the denomination of a party as a "surety" in an instrument

12. Id. art. 2104.
13. Id. art. 2103.
should imply that the creditor is not to impair the right of subrogation of the surety to all of the rights against the principal debtor nor to release the debtor without also completely exonerating the surety. Contrariwise the primary debtor, having recognized by his independent undertaking that the matter is exclusively his concern, should be held to have impliedly agreed that a release of the so-called surety will not affect his liability.

Reading article 3045 from this perspective, it is obvious that the redactors did not have in mind the far-reaching consequences that the court ascribed to its last clause. The obvious purpose of the article is to establish the right of discussion for sureties in general. It then recognizes two situations in which one who is in substance a surety may not avail himself of the right. The first is when he has contracted as a surety but waived the right of discussion, thus becoming bound "solidarily" with the principal debtor, but still upon a contract of suretyship. The second is when he has contracted "jointly in solido with the debtor" as a primary obligor in the

14. Any rationale of the Code which ascribes to article 3045 the far-reaching effects assumed by Boutte is incomplete without an explanation of why the redactors chose to place it as an almost parenthetical note to an article whose obvious purpose is to regulate when the plea of discussion is available to sureties. To conclude that its authors intended to establish a rule which in substance would declare that, at least between the creditor and surety, the rules of suretyship are not applicable if the latter waives the plea of discussion or says he is bound solidarily with the debtor, would be to give the clause a greater and more far-reaching effect than the rule it modifies. This is certainly contrary to the principles of arrangement that normally were followed in the preparation of the Code. If, however, one assumes the latter part of article 3045 in substance means: "the plea of discussion is not available to a surety who has waived it, nor to one who has bound himself, not as a surety but as primary obligor in solido jointly with the debtor (for in such a case there is no contract of suretyship and his liability is that of a solidary obligor bound with the debtor)," it would then appear that the clause in question would not be establishing a rule but merely describing the effect of what would otherwise follow by virtue of the nature of the parties' agreements. That is, it is declarative, not dispositive. This is entirely consistent with the parenthetical nature of the clause. Were article 2106 to contain a clause stating, "nor shall such parties [who are bound solidarily on the debt with another but who have no interest in the matter] be entitled to plead discussion," precisely the same assumption would be present: that the parties, while actually sureties, are not bound as such to the creditor—but it is doubtful the courts would have found it necessary to conclude the purpose of such a clause to be as they have apparently conceived the purpose of article 3045 to be: to decide in the first instance whether the rules of suretyship or of solidarity are applicable.
manner contemplated by article 2106. In the latter instance there is no contract of suretyship but only the one on which he and the debtor are both bound as primary obligors.

In the first instance, the articles on suretyship should regulate the relationship of the parties. In the second, the articles on solidarity would be applicable since as to the creditor there is no agreement of suretyship, but only the one agreement with his debtors who are both principals. If the agreement with the creditor is silent as to the underlying relationship between the parties he of course may assume that they are equally interested in the matter, enabling him to treat them as equally bound. If, however, one of the parties is characterized as a “surety” it would ordinarily be a recognition by the creditor that the matter concerns only the other debtor and that the surety who renders performance is to be completely subrogated to the claim of the creditor against such debtor. In this case no substantial difference in the liability of the parties would result from application of the articles on suretyship as distinguished from those on ordinary solidarity except to the extent the latter rules assume each of the obligors has held the other out to the creditor as being able to act for both. For example, the filing of a suit

15. The difference between being bound primarily on the obligation as a principal and secondarily bound for it as a surety, which is at the heart of the problem, is sometimes obscured when the primary obligation is for the simple payment of a debt. However, when the contractual relationships are more complex the distinction is much more easily seen and has been recognized by the courts in situations which are intrinsically in conflict with the rule announced by the Boutte case. The Private Works Act, LA. R.S. 9:4803 (Supp. 1962), affirmatively declares the surety of a contractor is solidarily liable on his bond with the contractor. The courts have never considered this provision to do more than waive the pleas of division and discussion. Nor could they do so without negating the basic provisions of the Act which clearly contemplate that the “solidary” surety in such a case is still a surety. To apply the articles on solidarity would also dictate that one might thereafter properly refer to the surety as a “joint contractor” with the builder. Obviously he is not. Persons who for valid business or pecuniary reasons have verbally contracted with a creditor to undertake responsibility for debts of others have sometimes attempted to escape liability on the grounds that such a contract is required to be in writing by article 2278. The courts have rejected their pleas holding that such an undertaking is not accessory but primary and direct. See Collier v. Brown, 11 La. App. 567, 569, 141 So. 405, 406 (1932), where the court held “Brown [the third person] did not become surety for Willard [the original debtor] . . . but became bound as principal with him for the payment of the account. Two persons may be bound as principals for the same debt, where as between them only one in reality should pay it.”
against or acknowledgment of the debt by either should interrupt prescription as to both, the extension of time to perform given one party, unless it constitutes a novation, should not affect the liability of the other, and so forth.

At the heart of the problem is the overriding consideration, sometimes overlooked, that the matter is one of contract, not imperative law. The task of the court is always to arrive at the intention of the parties as to the effects to be given to their engagements, remembering that they are free to make such modifications to the normal consequences of their agreement as are not contrary to public policy. Any rule establishing that, as a matter of law, the presence in an agreement of words that actually may be consistent with two or more premises imposes upon the parties one set of consequences rather than the other will undoubtedly lead to unjust and erroneous conclusions. The apparent conclusion by the court that the words "in solido" in a contract negate the existence of a relationship of suretyship when the parties may have at the same time characterized themselves as being "sureties" is just such a rule.

Furthermore, the author submits that for over a century the almost universal commercial practice in this state has been to require a surety to waive the pleas of division and discussion by agreeing to be bound "in solido" as a surety, but without any intention of negating the essentially accessory nature of his contract. Any rule of law so obviously contrary to such an established practice cannot but create confusion and impose upon parties consequences totally contrary to their understanding. It is neither necessary, proper nor realistic to do so.

The first inquiry should always be whether the party claiming to be a surety has contracted as a principal or as an accessory; is he undertaking joint responsibility for performance in fact or only guaranteeing performance by another with whom the primary contract is made? The second should be: given the basic nature of the agreement, either as a principal undertaking or suretyship, to what extent have the parties modified the normal consequences of such an engagement by the particular stipulations or conditions of their agreement?