Reconsidering Consideration in the Restatement (Third) of Suretyship

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RECONSIDERING CONSIDERATION IN THE
RESTATEMENT (THIRD) OF SURETYSHIP

PETER A. ALCES*

I. INTRODUCTION

The suretyship relation is created by contract and is therefore a creature of contract law. The affinity of common law contract and suretyship belies the fundamental tension between the freedom-of-contract principles that inform the law of consensual two-party relations and the challenges presented by three-party relations. In suretyship, the actions of one party will affect the rights and, concomitantly, the duties of at least two other parties to the transaction.

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1. See Laurence P. Simpson, Handbook on the Law of Suretyship 31 (1950) ("Express contract is by far the most frequent method by which the suretyship relation is created."); Arthur A. Stearns, The Law of Suretyship § 1.1, at 1 (5th ed. 1951) ("Suretyship may be defined as a contractual relation whereby one person engages to be answerable for the debt or default of another."); see also Rhode Island Hosp. Trust Nat'l Bank v. Ohio Casualty Ins. Co., 789 F.2d 74, 77 (1st Cir. 1986) ("A suretyship is a contractual arrangement in which one party . . . agrees to back up the obligation of another."); Jagoe Constr. Co. v. United States Fidelity & Guar. Co., 58 S.W.2d 503, 508 (Tex. Ct. App. 1933) (noting that the "relation of principal and surety is always a matter of agreement between the parties"); Miners' & Merchants' Bank v. Gidley, 144 S.E.2d 711, 714 (W. Va. 1965) ("This [surety] relationship arises only by express contract.").

2. In the course of explaining the drafting difficulties encountered in the preparation of Article 4 of the Uniform Commercial Code, Walter Malcolm described the challenges presented when providing the rules to govern relationships among more than two parties in the commercial law. See Walter D. Malcolm, Article 4—A Battle with Complexity, 1952 Wis. L. Rev. 265, 270-73.

3. Indeed, this interrelation is the source of the so-called suretyship defenses. See generally Peter A. Alces, The Efficacy of Guaranty Contracts in Sophisticated Commercial Transactions, 61 N.C. L. Rev. 655, 660-76 (1983) (noting that many defenses can only be explained by court sympathy for guarantors).
Because the suretyship law is subject to generic contract principles, the *Restatement (Second) of Contracts* is profoundly interrelated with the *Restatement (Third) of Suretyship*. A substantial number of the Reporter’s notes to the *Restatement of Suretyship* provisions acknowledge indebtedness to the second *Restatement of Contracts*. That is true particularly in the portions of the *Restatement of Suretyship* concerning formation of the suretyship contract—the understanding among the three indispensable parties to the suretyship relation. In suretyship, ostensibly formal contract formation issues determine the resolution of basic enforcement issues to an extent perhaps not realized in any other specialized area of the general contract law. If form does not prevail over substance, form certainly qualifies substance.

This Article reviews section 6 of the *Restatement of Suretyship*, denominated “Consideration.” This century has been particularly hard on consideration, what with consideration’s having caused the death of contract and all. It may be that section 71 of the *Restatement (Second) of Contracts*, defining consideration as bargained-for exchange, has indeed been overwhelmed by section 90, describing promissory estoppel, in the general contract law. Suretyship law is subject to generic contract principles, the *Restatement (Second) of Contracts* is profoundly interrelated with the *Restatement (Third) of Suretyship*. A substantial number of the Reporter’s notes to the *Restatement of Suretyship* provisions acknowledge indebtedness to the second *Restatement of Contracts*. That is true particularly in the portions of the *Restatement of Suretyship* concerning formation of the suretyship contract—the understanding among the three indispensable parties to the suretyship relation. In suretyship, ostensibly formal contract formation issues determine the resolution of basic enforcement issues to an extent perhaps not realized in any other specialized area of the general contract law. If form does not prevail over substance, form certainly qualifies substance.

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6. See, e.g., *Restatement (Third) of Suretyship* § 6 reporter’s note (Tent. Draft No. 1) (noting that the consideration section derives, in part, from the *Restatement (Second) of Contracts*).

7. See id. §§ 8-10.

8. Id. § 6; see infra appendix (reproducing § 6 in its entirety).


10. The *Restatement* states:

(1) To constitute consideration, a performance or a return promise must be bargained for.

(2) A performance or return promise is bargained for if it is sought by the promisor in exchange for his promise and is given by the promisee in exchange for that promise.

*Restatement (Second) of Contracts* § 71(1)-(2) (1981).

11. Subsection 90(1) of the *Restatement* states:
tyship, however, could be a last bastion of classical contract doctrine, stubbornly reliant on concepts, such as consideration, that are disfavored in the commercial contracts law generally. The law has never quite resolved its ambivalence about the suretyship relation.

Section 6 of the Restatement of Suretyship reformulates the consideration doctrine in the suretyship law, and reformulates it in ways not fully revealed by the case law on which the Restatement’s Reporter has apparently relied. Though it is of course always true that the terms of a restatement should not go beyond the development of the law, it is particularly important that the reformulation of a principle such as consideration not be accomplished in a manner inconsiderate of the case law and, at least arguably, inconsiderate of important commercial concerns as well.

The two parts of this Article focus on two of the exceptions to the consideration requirement provided in the Restatement of Suretyship. Part II considers the proposed exception applicable when the suretyship contract was part of the exchange for which the obligee bargained. The difference between a later created but

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A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

*Id.* § 90(1).

12. Notice of acceptance may fall into this category as well. See *Restatement (Third) of Suretyship* § 5 (Tent. Draft No. 1) (providing that an offeree may become a secondary obligor by advancing credit or contracting with the principal obligor).

13. Provisions of Article 2 of the Uniform Commercial Code have dispensed with the consideration requirement in circumstances in which the common law of contract would have imposed the requirement. See, e.g., U.C.C. §§ 2-205 cmt. 1, -209 cmt. 2, -306 (1990).


15. The terminology used here is drawn from the *Restatement of Suretyship.* See *Restatement (Third) of Suretyship* § 1 reporter’s note, cmt. b (Tent. Draft No. 1). Section 1 states in pertinent part:

A “secondary obligor” has suretyship status whenever:

(a) one person (the “principal obligor”) owes performance of a duty (the “underlying obligation”) to another person (the “obligee”); and

(b) pursuant to contract, a third person (the “secondary obligor”) is subject to a “secondary obligation,” whereby either:

1 the secondary obligor also owes performance, in whole or in part, of the duty of the principal obligor to the obligee; or
bargained-for secondary obligation, on the one hand, and a subsequent guaranty not bargained for initially, on the other hand, is a fine one. The secondary obligation must induce the obligee's promise or performance; it is not enough that the secondary obligation subsequently accommodates the obligee's undertaking. The Restatement of Suretyship formulation of the exception is not considerate of that distinction and does not comport with the case law on which the Reporter relied. The formulation may lead to undesirable results.

Part III treats the exception to the consideration requirement that arises when the terms of the suretyship contract recite a consideration, whether or not that consideration in fact was exchanged. Again, the case law does not support the exception. Too broadly construed, the exception's operation might also yield uncommercial consequences.

Although this Article does not defend the consideration requirement generally, it does argue that before the consideration requirement should be abrogated, the case against it must be made in the particular contexts where the requirement would be avoided. Furthermore, if that case can be made, it must be based on a cogent reading of the existing case law, not by mere reference to decisions without accounting for the courts' analyses. In the event that the suretyship law is codified in a uniform commercial statute, that might provide the setting to ignore or reverse precedent. Even then, however, the drafters would have to demonstrate that their formulations will serve rather than frustrate better commercial practices.

(2) the obligee has recourse against the secondary obligor or its property

... . . .

Id. § 1(1).

16. The American Law Institute is the sponsor of the Restatement of Suretyship. The Institute is also a cosponsor of the Uniform Commercial Code, along with the National Conference of Commissioners on Uniform State Laws. Therefore, subject to funding exigencies, a new Article 3A of the U.C.C., governing commercial guaranty agreements, could follow completion of the Restatement of Suretyship project.
II. Secondary Obligation as "Part of the Exchange"

The requirement of a bargained-for exchange, consideration, is a venerable element of the contract law.\(^7\) A suretyship contract must be supported by consideration in order to be enforceable.\(^7\) Because the suretyship relation is a tripartite contractual arrangement, the consideration issue in the suretyship law is affected by the fact that the suretyship and principal contracts are interrelated.\(^7\) More specifically, the consideration flowing from the obligee to the principal obligor also may support the undertaking of the secondary obligor.\(^7\)

\(^{17}\) See, e.g., Restatement of Contracts § 75 cmt. b (1932) ("Consideration must actually be bargained for as the exchange for the promise. . . . The existence or non-existence of a bargain where something has been parted with by the promisee or received by the promisor depends upon the manifested intention of the parties.").

In 1881, Oliver Wendell Holmes stated:

"If it is the essence of a consideration, that, by the terms of the agreement, it is given and accepted as the motive or inducement of the promise. Conversely, the promise must be made and accepted as the conventional motive or inducement for furnishing the consideration. The root of the whole matter is the relation of reciprocal conventional inducement, each for the other, between consideration and promise."

Oliver Wendell Holmes, Jr., The Common Law 293-94 (1881); see also Restatement (Second) of Contracts § 71 (1981) ("To constitute consideration, a performance of a return promise must be bargained for."); Gilmore, supra note 9, at 18-22 (outlining the history of consideration).

\(^{18}\) See Restatement (Third) of Suretyship § 4 (Tent. Draft No. 1) ("The requisites of contract formation apply generally to formation of a contract creating a secondary obligation.").

\(^{19}\) See id. § 1 cmt. c (describing the interrelation between the underlying contract and the suretyship contract).

\(^{20}\) Id. § 6 cmt. a.

The Reporter's note to section 6 of the Restatement cites Superior Wire & Paper Products, Ltd. v. Talcott Tool & Machine, Inc., 441 A.2d 43 (Conn. 1981), a Connecticut Supreme Court case, in support of the rule that consideration supporting the principal obligation also supports the secondary obligation. Restatement (Third) of Suretyship § 6 reporter's note, cmt. a (Tent. Draft No. 1) (citing Superior Wire). Superior Wire involved the obligee's sale of steel to the principal obligor, payment for which was guaranteed by the secondary obligors in their letter written to the obligee; the letter stated that "we [through our company and individually] . . . will guarantee payment of purchases made by [the principal obligor]." Superior Wire, 441 A.2d at 48 n.7. The secondary obligors acknowledged that the language gave rise to a continuing guaranty, but argued that the guaranty could not be enforced by the obligee because it was not supported by consideration. Id. at 48. The court concluded that "[w]hether these shipments were made contemporaneously with the execution of the . . . guaranty or at some time thereafter is legally irrelevant to the issue of inducement." Id. The court found that the obligee's reliance brought the case within the
Subsection 6(a) of the Restatement of Suretyship provides that "[a] secondary obligation does not fail for lack of consideration if: . . . the underlying obligation is supported by consideration and the later creation of the secondary obligation was part of the exchange for which the obligee bargained." Therefore, if O contracts to extend credit to P provided that P obtains a guarantor, S, then as long as there is consideration supporting P's undertaking to O, that consideration—O's promise to make funds available to

scope of § 89C of the Restatement of Contracts, which makes guaranties enforceable on the basis of reliance by the obligee. Id. at 48 & n.8. The court determined that even if § 89C were inapposite, there would be no problem finding sufficient consideration to support the guaranty because the guaranty letter had induced the obligee to make shipments to the principal obligor. Id. at 48.

The Reporter's note also cites Public Loan Co. v. FDIC, 803 F.2d 82 (3rd Cir. 1986), in support of the general suretyship consideration rule. RESTATEMENT (THIRD) OF SURETYSHIP § 6 reporter's note, cmt. a. (Tent. Draft No. 1) (citing Public Loan). In Public Loan, the secondary obligors resisted their secondary liability on the basis of failure of consideration, asserting that "the borrower [principal obligor] never received the loan funds." Public Loan, 803 F.2d at 85 (quoting Appellant's Brief). The court was satisfied with the lower court's finding that the only issue raised concerning the loan funds was the use to which they were put by the borrower, an issue not pertinent to the consideration question so far as secondary liability was concerned. Id. at 85-86.

The general rule applies in the commercial paper suretyship setting. Moses v. Lawrence County Bank, 149 U.S. 298 (1893), which concerned the accommodation of a negotiable instrument, was decided in accordance with "the general commercial law," id. at 300, a pre-Erie, Swift v. Tyson-era concept. Cf. Swift v. Tyson, 41 U.S. (16 Pet.) 1 (1842) (holding that when federal courts exercise jurisdiction based on diversity of citizenship, the courts may develop and apply federal common law of the commercial world), overruled by Erie R.R. v. Tompkins, 304 U.S. 64 (1938) (holding that federal courts sitting in diversity must utilize state law except in matters governed by the Federal Constitution or by acts of Congress). The court in Moses limited the statement of its holding to the terminology of the negotiable instruments law:

A guaranty of the payment of a negotiable promissory note, written by a third person upon the note before its delivery, requires no other consideration to support it, and need express none other . . . than the consideration which the note upon its face implies to have passed between the original parties.

Moses, 149 U.S. at 302-03. The guaranty of payment was affixed to the note before the note's delivery to the obligee and was assumed in order to induce the obligee to extend credit to the principal obligor. Id. at 302. The Court, construing the pre-U.C.C. negotiable instruments law, held that "a guaranty written upon a promissory note, after the note has been delivered and taken effect as a contract, requires a distinct consideration to support it." Id. at 303 (emphasis added). The negotiable instruments law must be concerned with the rights of a holder in due course of a note, payment of which has been guaranteed. The holder could well have no way of knowing when the guaranty was affixed. See infra note 23.

21. RESTATEMENT (THIRD) OF SURETYSHIP § 6(a) (Tent. Draft No. 1).
P, or the actual provision of funds pursuant to that promise—is sufficient to support S’s secondary obligation to O.

Subsection 6(a) expressly contemplates the situation in which the secondary obligation of S arises subsequent to P’s obligation to O, making clear that S will not be able to avoid liability to O by arguing that P already had the promise or even the funds pursuant to that promise and so O could not rely on that promise or those funds to support the subsequently arising secondary obligation. This is consistent with the rule provided in the commercial paper article of the Uniform Commercial Code.

It is not clear why the Restatement formulation in subsection 6(a) refers only to “the later creation of the secondary obligation.” The contemporaneous creation of the secondary obligation is also sufficient. The first illustration to section 6 makes that point:

C agrees to lend D $1,000 if S will guarantee D’s obligation to C. Following S’s execution of a written guaranty, C makes the

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23. The original § 3-415(2) of the U.C.C. explains that “[w]hen the instrument has been taken for value before it is due the accommodation party is liable in the capacity in which he has signed even though the taker knows of the accommodation.” U.C.C. § 3-415(2) (1988). The pertinent comment explains that the subsection “is intended to change occasional decisions holding that there is no sufficient consideration where an accommodation party signs a note after it is in the hands of a holder who has given value.” Id. § 3-415 cmt. 3. The comment further observes that the rule of the subsection is consistent with the general commercial paper rule that “no consideration is necessary for an instrument or obligation thereon given in payment of or as security for an antecedent obligation of any kind.” See id. (citing id. § 3-408). This expression of the rule that consideration supporting the principal obligation also supports a subsequent secondary obligation is not a model of clarity. In the revised Article 3, the new § 3-419(b) resolves the issue similarly but more directly: “The obligation of an accommodation party may be enforced . . . whether or not the accommodation party receives consideration for the accommodation.” U.C.C. § 3-419(b) (1990). Just as in the Restatement of Suretyship, the revision of the Article 3 rule is cast in terms of an exception to the consideration requirement. That statutory language, in sweeping fashion, both resolves the issue of accommodation subsequent to principal obligation and makes clear that gratuitous and compensated sureties will be treated the same way under the revised commercial paper law. The comment to the revised formulation does not explain the intent of the drafters in revising the expression of the rule. See generally Neil B. Cohen, Suretyship Principles in the New Article 3: Clarifications and Substantive Changes, 42 Ala. L. Rev. 595 (1991).
24. Restatement (Third) of Suretyship § 6(a) (Tent. Draft No. 1).
loan. S's guaranty is supported by consideration even though S receives no direct benefit from the loan.25

The illustration correctly describes the result, but it is not within the scope of any subsection of the black letter of section 6. It must be, then, that the consideration requirement is satisfied in the context presented in that first illustration by the general contract law conceptions of consideration, not by anything in section 6 of the Restatement of Suretyship.26

That conclusion is supported by the comment to subsection 6(a), concerning the delayed execution of the secondary obligation rule:

Occasionally, the existence of the secondary obligation is part of the exchange bargained for by the obligee to induce it to [deal with] the principal obligor, but actual creation of the secondary obligation (not supported by separate consideration) is delayed until after the obligee contracts with the principal obligor. Strictly speaking, in such a case the secondary obligation is not supported by consideration because the contract between the obligee and the principal obligor existed at the time the secondary obligor undertook the secondary obligation.27

The rule of subsection 6(a), then, is explained as providing an exception to the general consideration rule to comport with commercial realities.

Note what the subsection provides and how the comment describes what the subsection provides. First, consideration supporting the principal obligation effectively supports the secondary obligation. Second, that conclusion is not compromised by the fact that the secondary obligation arises after the principal obligation arises. But is it true, as the comment argues, that "strictly speaking" there would be no consideration supporting the secondary obligation because of the delay between the time that the principal and secondary obligations arise?

The portion of the Reporter's note concerning subsection 6(a) and comment b cites the portion of the Stearns treatise28 in which Stearns distilled from the case law the general rule that "[t]he

25. Id. § 6 cmt. a, illus. 1.
26. See supra note 17 and accompanying text.
27. Restatement (Third) of Suretyship § 6 cmt. b (Tent. Draft No. 1).
28. Id. § 6 reporter's note, cmts. a-b (citing Stearns, supra note 1, §§ 2.7, 4.9).
same consideration is sufficient for both [principal and secondary] contracts where both are entered into at the same time.” Stearns found consideration and did not posit an exception to the consideration requirement: “[I]t is not necessary that the consideration for the promise of guaranty be distinct from that of the principal debt, if such promise was made as a part of the transaction which created the principal debt.” It is difficult to find in Stearns, the source cited by the Reporter, support for the comment’s suggestion that, “strictly speaking,” in the context contemplated by subsection 6(a), there would be no consideration for the secondary obligation.

Why does or might it matter that the Restatement, at least arguably, misstates the rule, so far as Stearns’s description of the cases is concerned? First, the Restatement is supposed to restate, not make, the law. Second, and perhaps more crucially, the language of subsection 6(a) is so loose as to mislead. The subsection suggests that so long as the later secondary obligation “was part of the exchange for which the obligee bargained,” then the later secondary obligation need not be supported by separate consideration. Does that cover the situation (the “first situation”) in which the obligee and principal obligor agree to the obligee’s provision of a line of credit and then, subsequently, the secondary obligation arises even if the secondary obligation was not in the parties’ (obligee, principal obligor, and secondary obligor) contemplation at the time of the obligee’s agreement to provide the credit line? Or does it only cover the situation (the “second situation”) in which the three parties agree on the terms of both the principal and secondary obligation on Day 1 but the secondary obligation/guaranty is not executed until Day 5?

If the first situation falls within 6(a), then the subsection is inconsistent with Stearns’s formulation of the law: “[A] past transaction or executed consideration will not support a contract of guaranty.” To the contrary, as long as the second situation describes

29. STEARNS, supra note 1, § 4.9, at 71 n.63 (citing Moses v. Lawrence County Bank, 149 U.S. 298 (1893); Mortgage Guarantee Co. v. Chotiner, 64 P.2d 138 (Cal. 1936); Brandon v. Pittman, 158 So. 443 (Fla. 1934)).
30. Id. at 71 (emphasis added).
31. Id., see id. n.65. For cases finding that a past transaction or executed consideration will not support a contract of guaranty, see Lagomarsino v. Gianm, 80 P 698 (Cal. 1905);
the proper 6(a) result, then the Restatement of Suretyship is consistent with the Stearns view: "[T]he contract of guaranty is founded on a valid consideration where the main contract was induced by the promise to give a guaranty, even though such contract of guaranty was not executed until subsequent to the principal contract." 32 That second reading of subsection 6(a) is certainly preferable and is consistent with the case law. The Restatement provision would better accommodate that reading if it used terminology more similar to that emphasized rather than the less certain "part of the exchange for which the obligee bargained."

The commentary to subsection 6(a) suggests that no consideration is given by the obligee for the later guaranty: "[T]his paragraph [6(a)] provides an exception to the requirement of consideration in [the case within its scope]." 33 This passage is at the least misleading. The obligee did in fact give consideration for the secondary obligation. She simply gave it at the time that the principal obligation arose, not at the time the secondary obligation was later executed. The later secondary obligation, therefore, in fact is supported by consideration. There is, as yet, no reason to carve the type of exception to the consideration requirement that could accommodate a reviewing court's conclusion that a later arising secondary obligation needs no independent consideration supporting it so long as it "was part" of the exchange between the obligee and principal obligor. If it in fact was a part of the bargained-for exchange, then there was consideration; if it was not, then there was

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32. Stearns, supra note 1, § 4.9, at 71 (emphasis added).

no consideration and it should not be enforceable without the provision of some independent consideration.

There is, however, a situation in which discerning consideration flowing to the secondary obligor might be more difficult, and, therefore, indulging the subsection 6(a) "exception to consideration requirement" idea might be helpful. Consider the case in which O and P agree on Day 1 that P will construct a building for O and that, pursuant to the same agreement, P will within 120 days provide a secondary obligor to guarantee P's performance. P perhaps does not yet know who the secondary obligor, S, will be; it is part of P's undertaking to secure an S. Subsection 6(a) contemplates the situation posited in this hypothetical—the bargain between O and P incorporated "later creation of the secondary obligation." Thus, it would be antithetical to sound commercial principles to permit S later to avoid the knowingly assumed secondary obligation by interposing an insubstantial consideration fiction.

The Restatement of Suretyship's illustrations of subsection 6(a)'s operation do not include a hypothetical such as that offered above, the later identified secondary obligor. That would seem to be the precise situation to which 6(a) should apply. If the secondary obligor is discerned at the time that the principal obligation arises, and not later identified, then there may be no good reason to provide an exception to the general consideration requirement rather than conclude that the subsequently executed—and therefore later arising—secondary obligation is supported by the consideration supporting the principal obligation, a relatively straightforward application of the general rule.

34. Illustration 4 to comment b states:

C agrees with P Corp. to lend P Corp. $100,000 if the indebtedness is guaranteed by S1 and S2. S1 and S2, who are married to each other, are the sole shareholders of P Corp. On March 28, at a meeting in C's offices, P Corp. executes the loan agreement, S1 executes a guarantee, and C advances P Corp. $100,000. S2, who was unable to attend the March 28 meeting due to illness, executes a guaranty on April 6. The guaranty of S2 need not be supported by consideration because it was part of the exchange for which C bargained.

Id. § 6 cmt. b, illus. 4; see also id. illus. 5, reproduced infra text accompanying note 68 (discussing a transaction in which one secondary obligor is anticipated and identified at the time the underlying obligation arises, and another secondary obligor is neither anticipated nor identified at such time).
In fact, however, the portion of the Stearns treatise cited in support of subsection 6(a) does not find an exception to the consideration requirement but instead finds consideration:

[A] suretyship agreement entered into subsequent to the principal agreement must either be supported by a new and independent consideration or the principal agreement must have been made on the strength of a promise to the creditor that a surety would be procured. Where there is such a promise, no new consideration is necessary as the surety’s agreement is considered to “relate back” to the original transaction and to be supported by the same consideration. Such antecedent promise may be made either by the principal debtor or by the surety.\textsuperscript{35}

If the later identified context does not rely on the exception to the consideration requirement but instead is premised on relation back of consideration, as Stearns explains, then the subsection 6(a) “exception” may be read to pick up other contexts. When the broad language of 6(a) is not explained or illustrated as concerning the later identified secondary obligor situation, then the reason for a separate subsection 6(d) is less clear. The two subsections would seem to collide.

Subsection 6(d) provides that consideration is not necessary to support the secondary obligation if “the secondary obligor should reasonably expect its promise to induce action or forbearance of a substantial character on the part of the obligee, . . . and the promise does induce such action or forbearance.”\textsuperscript{36} This subsection does not cover the hypothetical above, the later identified secondary obligor. The secondary obligor’s subsequent agreement to answer for the debt of the principal obligor could not have induced the obligee’s action or forbearance. The assurance, made by the principal obligor, that there would be a secondary obligor might have been such an inducement. But it would contort the language of subsection 6(d) to find that a subsequently identified secondary obligor induced action that might have been taken some time before the secondary obligation was assumed.

If, however, 6(d) does not pick up the subsequently identified secondary obligor situation, it does seem to apply to the case in

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\textsuperscript{35} Stearns, \textit{supra} note 1, § 2.7, at 19 (footnotes omitted).
\textsuperscript{36} Restatement (Third) of Suretyship § 6(d) (Tent. Draft No. 1).
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which the main contract was induced by the promise of the secondary obligor to give the guaranty. If the subsection fits the case in which the obligee deals with the principal obligor because the secondary obligor has offered the guaranty, what is there left for subsection 6(a) but to be applied by the less-than-careful court to make enforceable a guaranty that relates to the contract between the obligee and principal obligor whether or not the obligee entered into that contract in reliance on the secondary obligor’s undertaking? Certainly 6(d) is broader in scope than 6(a). Its operation should cover sufficiently the field within the purview of 6(a), particularly in light of illustrations 4 and 5 to subsection 6(a), which do not concern the subsequently identified secondary obligor. Therefore, a separate subsection 6(a) is unnecessary. In fact, it becomes something of an attractive nuisance—the means for a court to find no consideration requirement when the secondary obligation was part of the exchange for which the obligee bargained, even when the law should otherwise require the provision of a separate consideration to the secondary obligor. Further, we know that such cases do arise, because the apposite portion of the Reporter’s note cites them and acknowledges that “[i]f a subsequent guaranty was not bargained for initially . . . separate consideration is required.” Succinctly, given the apparent breadth of 6(a), it would just be too difficult for a court to determine when such a separate consideration would be required.

The Reporter’s note cites several cases pertinent to an appreciation of the consideration for subsequent guaranty rule. The next two sections of the Article review these cases and their relation to the rule formulated in subsection 6(a). A careful reading of the cases discloses that they do not support the formulation of the subsection.

37. See supra note 31 and accompanying text.
38. See supra note 34.
A. Later Created Secondary Obligation Does Not Fail for Lack of Consideration

The most recent case cited by the Reporter in support of subsection 6(a), Medley v. Southtrust Bank,\textsuperscript{41} involved a father's guaranty of both the existing indebtedness of his son and the debts of the son to the obligee that would arise after the execution of the guaranty.\textsuperscript{42} The holding of the case on the consideration issue may be narrower than subsection 6(a), and further, dictum in the opinion may contradict the Tentative Draft of the Restatement. The father argued that there was no consideration supporting his guaranty to answer for the debts of the son that predated execution of the guaranty.\textsuperscript{43} The obligee argued that the obligee's provision of additional credit to the son, subsequent to the execution of the guaranty, would support the father's undertaking to answer for all of the son's debt arising prior and subsequent to the father's assuming the secondary obligation.\textsuperscript{44} At first glance, the issue seems to be a matter of suretyship contract construction: did the secondary obligation of the father include the undertaking to answer for all of the son's debt? Certainly the father simply could have agreed to make good any future extension of credit to the son. The terms of the guaranty in Medley, however, covered all indebtedness of the son—the debt existing at the time of the guaranty as well as the debt arising subsequently.\textsuperscript{45} Clearly the general consideration rule would render enforceable the father's undertaking to answer for the prospective debts of his son.

The question becomes, then, whether the consideration supporting the prospective liability also supports the undertaking to answer for the preexisting indebtedness. It is difficult to imagine any reason why it should not. It is not clear, however, that subsection 6(a) advances the inquiry. The subsection seems to concern only the situation in which the later created secondary obligation is an undertaking to answer for a prior indebtedness; there is no provi-

\textsuperscript{41} 500 So. 2d 1075; see supra note 40.
\textsuperscript{42} Medley, 500 So. 2d at 1076-77.
\textsuperscript{43} Id. at 1078.
\textsuperscript{44} Id.
\textsuperscript{45} Id. (finding the contract term providing for guaranty of past and future debts unambiguous and therefore not subject to construction by the court).
sion of a consideration separate from that provided to the principal obligor prior to the secondary obligation’s arising. Surely if there is an advance to the principal obligor subsequent to the guaranty, that is consideration for the guaranty. The consideration requisite is satisfied; there is no need for an “exception” to the consideration requirement. All that remains to be determined is whether the secondary obligation, enforceable and supported by consideration, extends by its terms to the preexisting indebtedness of the principal obligor. If the secondary obligor intercedes so that the obligee will forebear from bringing a mature legal action against the principal obligor, then subsection 6(a) does not matter because that type of forbearance would be a separate and certainly sufficient consideration supporting the secondary obligation.  

It is difficult to see how Medley supports or is even pertinent to the rule of subsection 6(a). The court observed that “[w]hen dealing with a guarantee of a preexisting debt, consideration is essential to sustain the obligation.” This language could plausibly be read as contradicting the conclusion of subsection 6(a) because the subsection validates the later creation of a guaranty without the provision of separate consideration in some cases. It is probably better, however, to construe the dictum as referring to the guaranty of preexisting debt supported neither by the obligee’s forbearance nor the terms of the original bargain between or among (i) the obligee and principal obligor, (ii) the obligee and secondary obligor, or (iii) the obligee, principal obligor, and secondary obligor. But the case seems to be only tangentially related to the proposition of subsection 6(a).

The Reporter’s note also relies on the decision of the United States Court of Appeals for the Fifth Circuit in United States v. Burgreen, which concerned a loan guaranty controversy involving

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46. See Simpson, supra note 1, at 77 (“Where performance of the principal’s obligation is already due, the consideration for the surety’s promise generally is forbearance to sue the principal.”); Stearns, supra note 1, § 4.9, at 72 (discussing the rule that forbearance is sufficient consideration: “Such a rule perhaps may be supported on the ground that a party who has had all the benefits of the proposal should be estopped from escaping its burdens.”) (footnotes omitted).

47. Medley, 500 So. 2d at 1078 (citing Zadek v. Forcheimer, 77 So. 941 (Ala. Ct. App. 1918)).

48. 591 F.2d 291 (5th Cir. 1979); see supra note 40.
the Small Business Administration (SBA). This case comes closer than Medley to a holding that uses terms that support subsection 6(a), but it still does not rely completely on the fact that the later created secondary obligation was a part of the bargain between the obligee and the principal obligor. The decision, like Medley, was governed by Alabama law. The court began its analysis by applying the general rule recognized in Medley that a subsequent guaranty requires the provision of a new and separate consideration, unless there was agreement at the creation of the principal obligation that the guaranty would be furnished as security for the principal obligation.49

The court in Burgreen determined that "the guaranty was simply the final component in the closing of a permanent loan."50 The obligor would not have made the loan or completed the closing of the loan without the guaranty. Moreover, from the court's rendition of the facts, the guaranty only appeared to postdate the principal obligation.51 The other loan documents bore an earlier date because the parties had thought that the loan would be closed at the earlier date when in fact the loan was not closed until the date of the guaranty.52 So, if one construes the terms and chronology of the transaction as the court did, then this case might not even involve the later creation of a secondary obligation.

The court offered an alternative basis for its decision that militates against reliance on the decision as support for the rule of subsection 6(a). It stated that at the same time the guaranty was executed, the secondary obligor acquired a one-third interest in the stock of the principal obligor from the existing coguarantors.53 Consideration provided by a third party, in this case coguarantors, is certainly sufficient to support a secondary obligation. There is no requirement that the consideration be supplied to the secondary obligor by the obligee.

The Reporter's note also cites United States v. Lowell,54 another decision involving an SBA loan. Once more, the court did not con-

49. Burgreen, 591 F.2d at 296.
50. Id.
51. Id. n.5.
52. Id.
53. Id. at 296-97.
54. 557 F.2d 70 (6th Cir. 1977); see supra note 40.
front directly the type of facts that would require a rule such as that formulated in subsection 6(a). The guaranty in issue was deemed by the court to have been an inducement to the obligee to enter into the underlying transaction. The form of guaranty expressly recited that the guaranty was provided, in the court's words, "to induce the bank to make the loan and provide security for the loan." This type of recital would bring the terms of the secondary obligation within the scope of subsection 6(b): no consideration is necessary "if . . . the promise of the secondary obligor is in writing and signed by the secondary obligor and recites a purported consideration." There is no requirement that such a recital in fact be reinforced by the actual provision of the consideration represented in the terms of the recital.

In Lowell, the court found that the subsequent secondary obligors, a husband and wife, were party to the negotiations giving rise to the principal obligation. In fact, the husband was a stockholder of the principal obligor and "was the prime mover between [the principal obligor] and the [obligee] for this loan." The secondary obligor, in the court's view, was only technically a "later creation," and the fact that the secondary obligation was not obtained at the time the loan was made was deemed to be a clerical error. With that principle established, it is at least arguable that subsection 6(a) would not have come to the rescue of the obligee in Lowell.

The later created guaranty in Lowell was not the secondary obligation "part of the exchange for which the obligee bargained." The obligee did, certainly, bargain for a guaranty at the time the underlying obligation was assumed by the principal. The bank had

55. Lowell, 557 F.2d at 72.
56. Id.
57. Restatement (Third) of Suretyship § 6(b) (Tent. Draft No. 1, 1992).
58. Id. § 6 cmt. c ("This section goes further and precludes inquiry into whether the consideration recited in a written contract establishing a secondary obligation was mere formality or pretense, or whether it was in fact given."); see infra part III (discussing § 6(b) further).
59. Lowell, 557 F.2d at 72.
60. Id.
61. Id.
62. See Restatement (Third) of Suretyship § 6(a) (Tent. Draft No. 1); supra notes 21-22 and accompanying text.
obtained the secondary obligations of two of the intended guarantors.\textsuperscript{63} Then, when the third intended guarantor balked, or at least became “unavailable,” the bank decided that the other two guaranties would suffice.\textsuperscript{64} Only later, when the bank realized that a third guaranty was necessary to satisfy the SBA, did the bank seek and obtain the guaranty of the Lowells.\textsuperscript{65} The Lowells, for that matter, testified that they had executed the guaranty only after being informed by the bank/obligee that the requirement of their guaranty was only a technicality and that they would not be called upon to perform pursuant to the guaranty.\textsuperscript{66}

It would seem, then, that the secondary obligation of the Lowells, though perhaps later created, was not part of the exchange for which the obligee bargained in any real sense. The \textit{Lowell} case, therefore, might well have been decided in a different way if subsection 6(a) governed the consideration issue.\textsuperscript{67}

\begin{footnotesize}
\begin{enumerate}
\item [63] \textit{Lowell}, 557 F.2d at 71.
\item [64] \textit{Id.}
\item [65] \textit{Id.}
\item [66] \textit{Id.} Professor Gilmore described Lord Mansfield’s understanding of the relation between consideration and deal-policing mechanisms:
\begin{quote}
In the late eighteenth century, indeed, Lord Mansfield suggested that in English law, as in the civil law, all promises seriously made should be taken as legally binding, subject to a broad theory of what might be called invalidating cause or excuse for fraud, duress, coercion, and perhaps, change of circumstance.
\end{quote}
\textsc{Gilmore, supra} note 9, at 18. It may be, then, that relaxation of the consideration doctrine in suretyship contracts would be attended by a counterbalancing expansion of principles such as unconscionability. \textsc{Cf. U.C.C.} § 2-302 (1990) (permitting courts to refuse to enforce goods contracts they find unconscionable).

\item [67] The fourth case cited in the Reporter’s note is \textit{United States v. Interlakes Machine & Tool Co.}, 400 F. Supp. 59 (E.D. Mich. 1975), rev’d \textit{sub nom. United States v. Lowell}, 557 F.2d 70 (6th Cir. 1977), the lower court opinion that was reversed by the \textit{Lowell} decision. \textit{Lowell}, however, did not reverse the portion of \textit{Interlakes} concerning consideration for the later created secondary obligation. \textit{Lowell}, 557 F.2d at 72. The district court in \textit{Interlakes} recognized that the consideration supporting the principal obligation may support as well a later created secondary obligation bargained for at the same time as the principal obligation, so long as the secondary obligation was “executed pursuant to an understanding had before and is an inducement to the execution of the principal contract.” \textit{Interlakes}, 400 F. Supp. at 61 (citing 38 C.J.S. \textit{Guaranty} § 26b, at 1164). It would be difficult to see, on the facts of \textit{Lowell/Interlakes}, how the Lowells’ secondary obligation was “executed pursuant to an understanding had before” the loan documents were executed by the principal obligor. \textit{Id.} at 61-62.
\end{enumerate}
\end{footnotesize}
B. When Subsequent Secondary Obligation Requires
Independent Consideration

The consideration rule or, rather, the exception to the consideration rule, of subsection 6(a) of the Restatement of Suretyship does not apply if the secondary obligation is assumed after and separate from the assumption of the principal obligation, when the suretyship is subsequent to and distinct from the underlying obligation. Illustration 5 offers an example of the nonbargained-for subsequent guaranty rule:

C agrees with P Corp. to lend P Corp. $100,000 if the indebtedness is guaranteed by S1 and S2, who are the sole shareholders of P Corp., and S3, who is the spouse of S1. (At the time of the agreement, S2 is unmarried.) On March 28, at a meeting in C’s offices, P Corp. executes the loan agreement, S1 and S2 execute guarantees, and C advances P Corp. $100,000. On April 6, S3 and S4 (S4 married S2 on April 1) appear at C’s offices and execute guarantees. The guarantee of S3 need not be supported by consideration because it was part of the exchange for which C bargained. The guarantee of S4, must be supported by consideration because it was not part of the exchange for which C bargained. 68

The Reporter’s note explains that the illustration is based on United States v. Meadors, 69 which also involved an SBA loan. 70 The court observed that no independent consideration would be necessary to support a secondary obligation, the guaranty in the instant case, as long as the guaranty was signed at the same time that the principal obligation was assumed. 71 The secondary obligation in Meadors was signed simultaneously with the execution of the contract giving rise to the principal obligation. 72 Between the time of the principal obligor’s application to the SBA and bank lender and the date the loan was to be closed, one of the parties

68. RESTATEMENT (THIRD) OF SURETYSHIP § 6 cmt. b, illus. 5 (Tent. Draft No. 1, 1992).
69. 753 F.2d 590 (7th Cir. 1985).
70. RESTATEMENT (THIRD) OF SURETYSHIP § 6 reporter’s note, cmt. b (Tent. Draft No. 1) (citing Meadors).
71. Meadors, 753 F.2d at 597.
72. Id. at 591.
designated as a secondary obligor on the application was married.\footnote{Id.} When the SBA and bank brought the principal and secondary obligors together to execute the loan and guaranty documents, each of the intended guarantors appeared with his wife, including the newlywed spouse whom the original application had not contemplated.\footnote{Id.} At that closing, all five originally intended secondary parties and the new spouse signed the guaranty agreement.\footnote{Id.} This was not, then, a case in which the secondary obligation was "later created." It was created, in fact, at the same time as the principal obligation. The rule of subsection 6(a) would be wholly inapplicable apart from the "part of bargain" requirement because the secondary obligation was not later created.

\textit{Meadors} was decided by reference to a much more fundamental consideration doctrine: the additional spouse's undertaking was neither bargained for nor supported by any separate consideration flowing to her.\footnote{Id.} That much is revealed by the court's extended essay on the history and nature of the consideration doctrine.\footnote{Id.} It is clear, then, why the facts of \textit{Meadors} had to be adjusted in order to work as the illustration to support the distinction between the rule of subsection 6(a) and the more general rule stated in the Reporter's note: "If a subsequent guaranty was not bargained for initially, . . . separate consideration is required."\footnote{Id. at 594-99 (citing Hamer v. Sidway, 27 N.E. 256 (N.Y. 1891) (considering whether the promisor suffered a detriment on account of a promise made to him, not whether consideration in fact benefited the promisee); CHARLES FRIED, CONTRACT AS PROMISE 36-37 (1981) (claiming that state interest in the marketplace would not extend to intrafamilial and noncommercial contracts); HOLMES, supra note 17, at 293-94 (suggesting a look at "the relation of reciprocal conventional inducement, each for the other, between consideration and promise"); Melvin A. Eisenberg, The Principles of Consideration, 67 CORNELL L. REV. 640, 643 (1982) (claiming the state has an interest in enforcing promises that have been bargained for); Richard A. Posner, Gratuitous Promises in Economics and Law, 6 J. LEGAL STUD. 411, 412 (1977) (criticizing Eisenberg's state interest theory because unilateral promises increase surplus)).} That the Reporter adjusted the facts of the case to suit the purpose of the illustration is not at all troubling. It is, however, note-
worthy that the facts of the case do not support the statement of that general rule because the secondary obligation at issue in *Meadors* was not subsequent to the principal obligation though it may have been subsequent to the original application concerning the underlying obligation. It probably would have been better to cite in support of the general rule a case that in fact concerned a substantial but subsequent and unbargained-for secondary obligation.79

The other case cited by the Reporter in support of the general rule to which subsection 6(a) is an exception—the unenforceability of later created secondary obligations—is *Finn v. Heritage Bank & Trust Co.*80 The plaintiff/secondary obligor in *Finn* was the guarantor of his cousin’s indebtedness to the defendant bank/obligee.81 The secondary obligation in issue was in fact subsequent to the underlying obligation and the court realized that in order for the subsequent secondary obligation to be enforceable, the obligee would have to demonstrate the obligee’s provision of some new and separate consideration supporting the later created secondary obligation.82 The court, however, was able to find the requisite consideration and did not have to hold a later created secondary obligation unenforceable absent new and separate consideration.83

The secondary obligor signed the guaranty agreement about fifteen months after the principal obligation arose, and only after the loan officer represented to the secondary obligor that the loan officer would lose his position with the bank if the secondary obligor did not sign the guaranty.84 At the time the loan officer first processed the loan application, the bank’s loan committee approved the extension of credit without any requirement of a collateral guaranty.85 The loan officer later altered the loan committee’s

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79. See, e.g., First Nat’l Bank v. Chapman, 366 N.E.2d 937 (Ill. App. Ct. 1977) (holding that when debt is incurred and thereafter a third party guarantees it, additional consideration is necessary to support the guaranty); Harr v. Perkins, 6 A.2d 534 (Pa. 1939) (holding that a mere promise of the endorser of an old note to guarantee a new note is unenforceable for lack of consideration).
81. Id. at 540.
82. Id. at 541 (citing *Chapman*).
83. Id. at 542.
84. Id. at 540.
85. Id.
memorandum to make it appear that the committee did in fact require the guaranty.\textsuperscript{86}

Nonetheless, the secondary obligor signed the guaranty and the court found that the later created (though back-dated) secondary obligation was supported by a sufficient new consideration: the secondary obligor signed to save the loan officer’s job.\textsuperscript{87} The court also found additional consideration, of a \textit{very} subsequent type. Some time after the principal obligor had gone into bankruptcy, the secondary obligor approached the same loan officer at the obligee to obtain a new home construction loan that would be replaced upon completion by permanent financing provided by the bank/obligee.\textsuperscript{88} When the secondary obligor went to sign that loan agreement, the loan documents included the unpaid loan to the principal obligor.\textsuperscript{89} The obligee contended that it would not have approved the mortgage financing and the loan would not have been made at such a favorable rate had the mortgage note not included the secondary obligation liability.\textsuperscript{90} Therefore, the secondary obligor’s execution of the mortgage loan documents constituted, in the estimation of the court, a second secondary obligation supported by a new and separate consideration—the mortgage loan at an interest rate lower than the rates generally given by the obligee.\textsuperscript{91}

The case was a close one, and another court may have had more trouble finding a new and separate consideration on the same facts. It is at least curious that the court considered the secondary obligor’s execution of the loan documents to be an independent guaranty, the assumption of a distinct secondary obligation supported by contemporaneous consideration (i.e., the attractive terms of the mortgage financing). The court did note that the mortgage financing had been approved before the outstanding debt of the principal obligor was incorporated into the documentation but was only “officially approved” after that debt had been included.\textsuperscript{92}

\begin{itemize}
\item \textsuperscript{86} \textit{Id.}
\item \textsuperscript{87} \textit{Id.} at 542.
\item \textsuperscript{88} \textit{Id.}
\item \textsuperscript{89} \textit{Id.}
\item \textsuperscript{90} \textit{Id.}
\item \textsuperscript{91} \textit{Id.}
\item \textsuperscript{92} \textit{Id.}
\end{itemize}
If that indeed was a second guaranty, supported by new and separate consideration, it was subsequent even to the obligee's assignment of its claim against the principal obligor to the secondary obligor. The obligee had obtained a nondischargeable judgment against the principal obligor in the principal obligor's bankruptcy proceeding, and then, for a reason not explained in the opinion, it assigned that claim to the secondary obligor, who collected the judgment, in part, from the proceeds of the bankruptcy estate liquidation. Did the court, in effect, find that the undertaking in the mortgage loan documentation on account of the unsatisfied underlying obligation was in some way payment for the assignment of the obligee's judgment against the principal obligor almost two years earlier? The decision is not a paradigm of clarity and certainly not the best source of support for the rule that "[i]f a subsequent guaranty was not bargained for initially . . . separate consideration is required." 

93. Id. at 541.
94. RESTATEMENT (THIRD) OF SURETYSHIP § 6 reporter's note, cmt. b (Tent. Draft No. 1, 1992). Throughout the Reporter's commentary to the Restatement, reference is made to nonuniform state statutes governing surety relationships. Two such state statutes are cited with regard to the § 6 consideration issues, id. reporter's note, cmt. a. (citing CAL. CIV. CODE § 2792 (West 1974); S.D. CODIFIED LAWS ANN. § 56-1-3 (1988)), and their terms reveal something about the Restatement's provision of an "exemption" to the consideration requirement. The California and South Dakota statutes state:

[California:] Where a suretyship obligation is entered into at the same time with the original obligation, or with the acceptance of the latter by the creditor, and forms with that obligation a part of the consideration to him, no other consideration need exist. In all other cases there must be a consideration distinct from that of the original obligation.

CAL. CIV. CODE § 2792.

[South Dakota:] Where a guaranty is entered into at the same time with the original obligation or with the acceptance of the latter by the guaranteee and forms with that obligation, a part of the consideration to him, no other consideration need exist. In all other cases there must be a consideration distinct from that of the original obligation.

S.D. CODIFIED LAWS ANN. § 56-1-3. For additional examples of nonuniform state statutes, with language very similar to the California and South Dakota statutes, see MONT. CODE ANN. § 28-11-103 (1991) (referencing CAL. CIV. CODE § 2792 in the history); N.D. CENT. CODE § 22-01-03 (1991) (derived from CAL. CIV. CODE § 2792); OKLA. STAT. ANN. tit. 15, § 323 (West 1966).

It is noteworthy that both of those exemplary provisions treat the consideration issues in a single paragraph, rather than in the multiple paragraphs formulated in § 6 of the Restatement. It is therefore likely that the California and South Dakota enactments would not be coextensive with the Restatement rules. In the Reporter's note, these two state statutory
C. Consequences of the "Part of Exchange" Exception

Were the only problem with subsection 6(a) of the Restatement of Suretyship a certain inelegance, or the Reporter's failure to cite cases that in fact support the exception's formulation, then there would be little reason to be concerned with the potential uncommercial consequences that could flow from the courts' construction and application of the provision. The difficulty may be more signif-

provisions are cited only in support of the general rule that consideration supporting the principal obligation also supports the secondary obligation. See Restatement (Third) of Suretyship § 6 reporter's note, cmt. a (Tent. Draft No. 1). Nevertheless, the annotations to the two state provisions go beyond the general consideration-requirement rule by including cases that construe and apply rules that are treated in the subsections to § 6.

The California enactment is exemplary. In all cases other than the simultaneous principal and secondary obligation case, a separate consideration is required. But California cases, in order to satisfy the statutory contemporaneity requirement, have found that a principal and subsequent secondary obligation are legally simultaneous. See Stroud v. Thomas, 72 P. 1008, 1009 (Cal. 1903) (holding that a surety signing a note after the original transaction was liable without additional consideration where execution of the note was deemed to have taken place coincident with the original underlying transaction); Miller v. Smith, 3 Cal. Rptr. 492, 494-95 (Dist. Ct. App. 1960) (holding that consideration for a lease was consideration for a guaranty on the theory that the guaranty was executed as part of the lease transaction); Pacific States Sav. & Loan Co. v. Stowell, 46 P.2d 780, 781 (Cal. Ct. App. 1935) (stating that, in the context of making and delivering a trust deed note, the transfer of consideration from lender to borrower and the guaranty was one transaction even though the guaranty was not signed until after execution of the note); Citizens' Trust & Sav. Bank v. Bryant, 200 P. 823, 824 (Cal. Ct. App. 1921) (finding that a guaranty entered into three weeks after the underlying mortgage note was signed was supported by the same consideration as the note). These cases effectively vindicate the better reading of the rule of § 6(a) of the Restatement of Suretyship. The statutory provision is also supported by cases that have required the provision of a new and separate consideration when the guaranty in fact is subsequent to the underlying transaction and was not a part of the bargain struck in that underlying transaction. See In re Thomson's Estate, 131 P. 1045, 1048 (Cal. 1913) (stating that where a guaranty is given after execution of the principal contract, new consideration is necessary to support the guaranty); Bank v. Wetzel, 255 P. 254, 256 (Cal. Ct. App. 1927) (stating that a guaranty for payment of notes entered into after original obligation requires separate consideration).

The annotations to the South Dakota provision include a reference to a case supporting the general rule that no separate consideration is necessary if the principal and secondary obligations are contemporaneous. See Schanzenbach v. Stoller, 161 N.W. 329, 330 (S.D. 1917) (holding that a guaranty agreement executed as part of a sale needs no independent consideration). The annotations also include a decision consistent with the exception described in § 6(a) of the Restatement of Suretyship. Commercial Nat'l Bank v. Rich, 223 N.W. 193, 194 (S.D. 1929) (holding that when a bank accepts a debtor's replacement note with a new third-party guaranty for a past-due note, the extension given by the bank is sufficient consideration for all parties because it was part of the exchange for which the obligee bargained).
icant. The unfortunate combination of providing an “exception” to the consideration requirement, applicable when the secondary obligation is “part of the exchange for which the obligee bargained,” is problematic. Too broad a construction of the exception could yield results inimical to commercial interests.

Consider the situation in which an obligee and principal obligor enter into a loan agreement that includes a provision to the effect that if the principal obligor’s net worth falls below a certain figure, the principal obligor will provide a secondary obligor or be in default. When the principal’s net worth falls below the predetermined figure and the principal then obtains a secondary obligor, is there consideration supporting that secondary obligation? Need there be? Is the obligee’s forbearance from bringing an action on the principal obligation requisite consideration? Must the obligee forbear or lose the secondary obligor? In other words, was the consideration supporting the principal obligation—the extension of loan funds—sufficient to support the later created secondary obligation, or must there have been a separate consideration? Does subsection 6(a) even apply to the scenario or is it limited by the caption on the apposite comment: “Delayed execution of secondary obligation?”

Though the secondary obligation may in some way have been a “part of the exchange for which the obligee bargained,” this would seem to be much more than a simple case of delayed execution. Recall that the illustrations focus on delayed execution rather than on the bargained-for exchange. Subsection 6(a) should be clarified to apply clearly to the later identified surety and should avoid any broader application. It would also be appropriate to revisit the Reporter’s note to include citations of cases that support the formulation of the exception rather than cases that are, at best, ambiguous, and at worst, contradict the terms of the subsection.

III. Recitation of Purported Consideration

Subsection 6(b) of the Restatement recognizes a peculiar “exception” to the consideration requirement: no showing of a real

95. See Restatement (Third) of Suretyship § 6 cmt. b (Tent. Draft No. 1).
96. See, e.g., supra note 68 and accompanying text (discussing Restatement (Third) of Suretyship § 6 cmt. b, illus. 5 (Tent. Draft No. 1)).
consideration is necessary as long as the writing evidencing the secondary obligation recites the existence of a consideration, whether or not that recitation is truthful. To say the secondary obligation exists is enough. The comment to subsection 6(b) refers to the provision of a nominal consideration—something, no matter how insubstantial. The comment then explains that the actual provision of such a nominal consideration does not matter any more than the actual provision of a substantial consideration, but the exception operates as long as the parties merely recite a purported consideration. The rule makes a good deal of commercial sense. The fact that a consideration, albeit nominal, is recited confirms that the parties came to terms on the consideration issue.

There is, however, something particularly striking about the comment that confirms the broad sweep of the exception in terms that could give the courts trouble: “[Subsection 6(b)] precludes inquiry into whether the consideration recited in a written contract establishing a secondary obligation was mere formality or pretense, or whether it was in fact given.” Does that mean that if the writing evidencing the secondary obligation recites a consideration of, say, $50,000, the guaranty is enforceable whether or not the check in payment of that $50,000 is honored by the payor? Illustration 6 seems to confirm that the guaranty would not fail for want of consideration:

97. Restatement (Third) of Suretyship § 6(b) (Tent. Draft No. 1) (“A secondary obligation does not fail for lack of consideration if . . . the promise of the secondary obligor is in writing and signed by the secondary obligor and recites a purported consideration . . . .”).

98. Id. § 6 cmt. c (“This section . . . precludes inquiry into whether the consideration recited in a written contract establishing a secondary obligation was mere formality or pretense, or whether it was in fact given.”).

99. See id.

100. See Holmes, supra note 17, at 293 (“[C]onsideration may be given and accepted, in fact, solely for the purpose of making a promise binding. But, nevertheless, it is the essence of consideration, that, by the terms of the agreement, it is given and accepted as the motive or inducement of the promise.”); Lon L. Fuller, Consideration and Form, 41 Colum. L. Rev. 799, 801, 803 (1941) (stating that consideration functions as evidence of the existence of a contract and “offers channels for the legally effective expression of intention . . . . He who is compelled to do something which will furnish a satisfactory memorial of his intention will be induced to deliberate. Conversely, devices which induce deliberation will usually have an evidentiary value.”).

101. Restatement (Third) of Suretyship § 6 cmt. c (Tent. Draft No. 1).
G executes a written guaranty to C of a debt then due from D. The guaranty is stated to be "in consideration of one dollar paid to me by C, the receipt of which is hereby acknowledged." The guaranty is binding whether the dollar is in fact paid or not.\textsuperscript{102}

The subsection 6(b) rule and the illustration of its operation are taken directly from section 88 of the \textit{Restatement (Second) of Contracts}.\textsuperscript{103} Comment b to section 88 explains that the portion of the rule stating that the guaranty is enforceable, whether or not the recited consideration is ever paid, is drawn from the portion of the second \textit{Restatement of Contracts} concerning option contracts.\textsuperscript{104} Professor Farnsworth, a Reporter for the \textit{Restatement}, explained in his treatise the general rule of contract consideration concerning the recital of consideration:

[It is not] within the [contract] drafter's power to change falsehood into truth by reciting that an act has been done as consideration in a promise if the act has not been done. In spite of a recital that a performance has taken place (e.g., that the price has been paid), it can be shown that the performance has not taken place—that the recital is false.\textsuperscript{105}

\textsuperscript{102} Id. illus. 6.

\textsuperscript{103} Id. § 6 cmt. c & reporter's note (citing \textit{Restatement (Second) of Contracts} § 88 & illus. 1 (1981)). Section 88 states: "A promise to be surety for the performance of a contractual obligation, made to the obligee, is binding if the promise is in writing and signed by the promisor and recites a purported consideration." Id. § 88(a); see supra note 97 (reproducing \textit{Restatement (Third) of Suretyship} § 6(b) (Tent. Draft No. 1)).

\textsuperscript{104} See \textit{Restatement (Second) of Contracts} § 77 cmt. 6 (citing id. § 87). Section 87 of the \textit{Restatement (Second) of Contracts} provides:

(1) An offer is binding as an option contract if it

(a) is in writing and signed by the offeror, recites a purported consideration for the making of the offer, and proposes an exchange on fair terms within a reasonable time; or

(b) is made irrevocable by statute.

(2) An offer which the offeror should reasonably expect to induce action or forbearance of a substantial character on the part of the offeree before acceptance and which does induce such action or forbearance is binding as an option contract to the extent necessary to avoid injustice.

Id. § 87; see id. cmt. c ("A recital in a written agreement that a stated consideration has been given is evidence of that fact as against a party to the agreement ").

\textsuperscript{105} E. ALLAN FARNSWORTH, \textit{Contracts} § 2.17, at 89 (2d ed. 1990) (footnotes omitted).
The two footnotes supporting the excerpt are interesting insofar as they cite substantial authority opposed to that general rule but do not refer specifically to the suretyship law exception.\(^{106}\)

The first of the two footnotes advises the reader to consult a separate portion of the treatise "[a]s to the important question of the applicability of this general statement to option contracts."\(^{107}\) The portion of the treatise concerning the recital of consideration in option contracts reports that courts have gone both ways on the issue of whether a false recital nonetheless binds that party to whom the nonexistent consideration was alleged to have gone.\(^{108}\) Some courts have found a false recital to be ineffective\(^{109}\) and others have found that the recital itself, whether or not accurate, is legally sufficient.\(^{110}\) At least, then, the Reporter for the second *Restatement of Contracts* acknowledged that the inaccurate recital rule of section 87, in the option contract setting, is not so settled as the *Restatement* would suggest.\(^{111}\)

Section 88 of the *Restatement (Second) of Contracts*, concerning guaranty contracts, cites section 87 to support the rule on false recitals;\(^{112}\) subsection 6(b) of the *Restatement of Suretyship* is reproduced almost verbatim from the language of subsection 88(a) of the second *Restatement of Contracts*, concerning recitals of con-

\(^{106}\) *Id.* nn.8 & 9.

\(^{107}\) *Id.* n.8.

\(^{108}\) *Id.* § 3.23, at 187.

\(^{109}\) See, e.g., Colorado Nat'l Bank v. Bohm, 286 F.2d 494, 496-97 (9th Cir. 1961) (finding consideration lacking where the signature of a comaker on the note was given solely in exchange for payee's promise that the comaker would not be held liable on the note); Bard v. Kent, 122 P.2d 8, 10 (Cal. 1942) (finding a lack of consideration where the offeror did not agree to be bound in return for the consideration).

\(^{110}\) See, e.g., Smith v. Wheeler, 210 S.E.2d 702, 704 (Ga. 1974) (holding that a recital gives rise to an enforceable implied promise to pay); Real Estate Co. v. Rudolph, 153 A. 438, 440 (Pa. 1930) (holding that a recital, even if false, indicates the offeror's acknowledgment of receipt of nominal consideration).

\(^{111}\) Professor Gilmore has identified a commercial uneasiness with the consideration requirement in option contracts dating at least from the English decision in Dickinson v. Dodds, 2 Ch. D. 463 (Ch. App. 1876), and Justice Holmes' construction of the decision. *See* Gilmore, *supra* note 9, at 28-30.

\(^{112}\) *Restatement (Second) of Contracts* § 88 cmt. b (1981) ("Like § 87 on option contracts, this Section goes further and precludes inquiry into the question whether the consideration recited in a written contract of guaranty was mere formality or pretense, or whether it was in fact given.").
So does case law exist supporting the Restatement of Suretyship's assertion that even a false recital of consideration will suffice? The Reporter's note cites only one decision.

Beltran v. Groos Bank directly confronted the false recital issue. The secondary obligor was the principal obligor's attorney and signed a limited guaranty of the loan the obligee made to the principal obligor's restaurant business. The letter of guaranty recited that the consideration supporting the secondary obligation was to be one dollar plus the credit to be given to the secondary obligor. When the obligee tried to enforce the guaranty, the secondary obligor objected that he had never received the recited consideration. The secondary obligor did not receive the one dollar, but the court found that the obligee had not refused the guarantor credit. Because the court mentioned nothing else about the credit as consideration, we may infer that the consideration was an undertaking to make credit available to the secondary obligor upon the secondary obligor's request.

The court's opinion focused on the recital of one-dollar consideration, assumed arguendo that the dollar had not in fact been paid by the obligee, and then considered whether the nonpayment rendered the guaranty unenforceable. The court cited and reproduced all three subsections of the Restatement (Second) of Contracts and then expressed its holding in terms of the alternative subsections:

Clearly, under the restatement rule, [the secondary obligor's] point cannot be sustained. The guaranty agreement was in writing and signed by [the secondary obligor]. The agreement recites purported consideration. Further, we find, according to Section 88(c), that appellant should reasonably have expected that his

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113. See supra notes 94, 100.
115. 755 S.W.2d 944.
116. Id. at 945.
117. Id. at 948.
118. Id.
119. Id.
signature on the letter of guaranty would induce the bank to lend money to the [principal obligors].

The court then completed its treatment of the consideration issue by noting the general rule that the consideration supporting the principal obligation may support the secondary obligation as well.

It is difficult to discern the holding from the dictum. On which of the consideration rules was the court relying? Was the court’s invocation of the “mere recital of consideration” rule dependent on the fact that the court deemed the general rule applicable as well and that the court found a sufficient inducement to justify application of subsection 88(c)?

Neither subsection 88(a) of the second Restatement of Contracts nor subsection 6(b) of the Restatement of Suretyship, the “mere recital” provisions, is limited in its application to recitals of a nominal consideration. The recital of a nominal consideration without actual payment of that inconsequential one dollar may be the commercial norm, something akin to a seal, and nothing more. The law, therefore, should not quibble about whether the one dollar is ever actually paid.

The commercial dynamic shifts when the consideration recited is not nominal. If the terms of the guaranty recite that the guarantor undertakes the secondary obligation in consideration for the principal obligor's or obligee's payment to the guarantor of $50,000, and that payment in fact is never made, then perhaps the law should quibble about whether the nonpayment vitiates the secondary obligor's undertaking. The terms of the Restatement of Suretyship do not seem to distinguish the recital of nominal consideration from substantial consideration. In either case, it would appear, the existence of a recital is sufficient, whether or not the consideration is in fact paid, because the recital provides an exception to the consideration requirement under the terms of section 6.

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120. Id. (citing Restatement (Second) of Contracts § 88(a)-(c) (1981)).
121. Id. (citing Hargis v. Radio Corp., 539 S.W.2d 230, 232 (Tex. Civ. App. 1976)). The court reasoned that “[i]t is not necessary that consideration for the guarantee pass to the guarantor, . . . for it is sufficient consideration if the primary debtor receives some benefit.” Id.
The rule should be limited to nominal-consideration cases. The consideration requirement should not be excused when the consideration recited is substantial though not in fact paid—but not because there is anything particularly vital about consideration *qua* consideration. Instead, the recital of $50,000 should matter and be accurate because that is the deal the guarantor has made. If she does not receive that payment and is nevertheless bound to the guaranty on account of the recital, then she is denied that for which she has bargained, and the obligee and perhaps principal obligor have received something for nothing. This untenable result is not justified by the fact that the secondary obligor would, if called upon to perform, have recourse against the principal obligor.\(^\text{122}\)

It is worthwhile to keep in mind, however, that the contract law has become generally and increasingly uncomfortable with the consideration requirement *ab initio*. To the extent that it satisfies certain "evidentiary" and "cautionary" purposes,\(^\text{123}\) consideration matters. But so long as there is a means to assure that the secondary obligor in fact assumed the guaranty obligation, satisfying the "evidentiary" purpose, and that the guarantor understood the consequences of his action, satisfying the "cautionary" purpose, then there is nothing else for the consideration requirement to support. Those two objects are also served by a writing requirement,\(^\text{124}\) and it would be unfortunate to confuse the writing requirement with the consideration requirement. The formulation of the subsection 6(b) exception to the consideration requirement, drawn as it is from the general *Restatement of Contracts*, can be justified on the same grounds that would be used to excuse a writing requirement. So understood, its limited utility in the case of recitals of substantial consideration will be better appreciated.

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122. *Restatement (Third) of Suretyship* § 6 cmt. c (Tent. Draft No. 1, 1992) ("The secondary obligor may never be called upon to perform the secondary obligation; moreover, if the secondary obligor is called upon to perform, it has recourse against the principal obligor.").

123. See Fuller, *supra* note 100, at 800 (recognizing that legal formalities of contract, including consideration, serve evidentiary functions by providing evidence of the existence of the contract and cautionary functions acting "as a check against inconsiderate action").

124. See *Restatement (Third) of Suretyship* § 8 (Tent. Draft No. 1).
IV. Conclusion

Formality might matter more when more than two parties are affected by the terms and performance of a contract. The suretyship law always contemplates the interrelation of three (or more) parties' interests. Therefore, concepts drawn from the general contract law may operate differently and matter more, or at least differently, in the suretyship law. That is the case with the consideration requirement. Any adjustment of consideration in suretyship law must be considerate of the unique challenges posed by three-party contracts. The evidentiary as well as cautionary aspects of consideration may well be more pronounced in the suretyship law.

There is a danger in relaxing the consideration requirement generally: deal-policing mechanisms may intercede when the protections afforded by the consideration doctrine are compromised. The disintegration of consideration may encourage broader application of unconscionability and fraud conceptions, with the uncommercial consequences that can attend the opening of that Pandora's Box.

The two exceptions to the consideration requirement treated in this Article are not drawn in terms that will assure their application in a manner consistent with commercial expectations. In fact, there is reason to believe that the effects of the exceptions have never been realized in the case law. It is not the fault of the Reporter or the Advisers to the Restatement of Suretyship that the suretyship case law is sparse. It is, however, imperative that the Reporter's notes indicate that particular sections of the Restatement are based on insubstantial precedent. Then it will be clear that the sponsoring organization is proposing the form that the suretyship law should take, rather than representing that the Restatement's formulation captures the law as it is.

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125. See supra note 66.
§ 6. Consideration
A secondary obligation does not fail for lack of consideration if:
(a) the underlying obligation is supported by consideration and the later creation of the secondary obligation was part of the exchange for which the obligee bargained; or
(b) the promise of the secondary obligor is in writing and signed by the secondary obligor and recites a purported consideration; or
(c) the promise of the secondary obligor is made binding by statute; or
(d) the secondary obligor should reasonably expect its promise to induce action or forbearance of a substantial character on the part of the obligee or a third person, and the promise does induce such action or forbearance.