

## Bankruptcy and Guarantors

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### *Middle District of North Carolina Bankruptcy Seminar*

A guarantee is a form of surety and its basic terms are governed by state law. A guarantee is subject to the statute of frauds and with a few exceptions must be in writing. N.C. Gen. Stat. § 22-1. The primary exception to the writing requirement is the “main purpose rule.” This exception applies where the guarantor or promisor “has such a direct, immediate, pecuniary interest in the subject matter of the principal debtor’s contract so as to indicate that the guarantor has intended to adopt the original contract as his own.” Burlington Industries, Inc. v. Foil, 19 N.C. App. 172 (1973), aff’d, 284 N.C. 740.

### Guarantee of Collection Versus Guarantee of Payment

There are generally two types of guarantees – a guarantee of collection and a guarantee of payment. A guarantee of payment is an absolute and unconditional promise to pay the debt at maturity if not paid by the principal debtor. Credit Corp. v. Wilson, 281 N.C., 140, 145 (1972); see also Jennings Communications Corp. v. PCG of Golden Strand, Inc., 126 N.C. App. 637, 640 (1997). The obligation of the guarantor is separate and independent from the obligation of the principal debtor. Investment Properties v. Norburn, 281 N.C. 191, 195 (1972). The creditor may pursue the guarantor immediately upon the failure of the principal debtor to pay the debt at maturity and the creditor need not first pursue the principal debtor without success before seeking payment from the guarantor. Cameron-Brown v. Spencer, 31 N.C. App. 499, 502 (1976), disc. review denied, 291 N.C. 710 (1977). On the other hand, a guarantee of collection is a promise by a guarantor to pay a debt on condition that his or her creditor shall first diligently prosecute principal debtor without success. Credit Corp., 281 N.C. at 145. Such a guarantee will often have a condition precedent before the creditor can go against the principal debtor. Jennings Communications, 126 N.C. App. at 641.

It can be important to distinguish between the two types when the principal obligor is a debtor in bankruptcy – either under Chapter 7 or 11. Because, the automatic stay of § 362 prevents a creditor from seeking payment from the debtor, if a creditor is the beneficiary of a collection guarantee where the conditions precedent for collection from the debtor have not been met, absent relief from the automatic stay, the creditor may be precluded from collecting from the guarantor. Whereas under a guarantee of payment, no such impediment would exist to prevent a creditor from proceeding against the guarantor or co-debtor, regardless of the bankruptcy of the principal obligor.