GUARANTEES, GOOD FAITH AND GAPS IN THE LAW: A CRITICAL STUDY OF SURETY RIGHTS

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ABSTRACT

The law of guarantee under the Indian Contract Act, 1872, represents an important juncture between contractual duties, equitable principles, and the allocation of commercial risk. Of its provisions, Sections 130, 143, and 145 have a decisive bearing on the rights and liabilities of the surety, creditor, and principal debtor. Section 130 governs the revocation of a continuing guarantee and allows the surety to withdraw liability for future transactions by giving notice to the creditor. It enshrines the voluntary nature of suretyship and protects the surety against perpetual and indeterminate liability. It operates only prospectively and applies only to a continuing guarantee within the meaning of Section 129, which means it cannot be extended to particular guarantees. The section tacitly confirms that ordinary guarantees are never revocable after execution. This arrangement maintains commercial certainty for the creditor while also respecting the surety's autonomy. Nevertheless, the section has serious omissions to its credit. Section 143 invalidates guarantees obtained through the creditor's concealment of material facts and represents a significant departure from the general rule under Section 17, which holds that silence does not amount to fraud unless there is a duty to speak. This provision elevates passive silence to a form of legal misconduct in guaranteed contracts, recognizing the surety's vulnerable position, who often relies on the creditor's superior knowledge of the debtor's financial standing. The absence of a statutory definition of "material fact" creates interpretative uncertainty and judicial inconsistency. This selective approach dilutes the protective purpose of the section and raises concerns of procedural unfairness. Section 145 codifies the implied promise of indemnity owed by the principal debtor to the surety and reinforces the equitable foundation of guarantee contracts. While this provision strengthens the surety's position, its operational limitations are significant. The phrase "rightfully paid" remains undefined, thereby extending judicial discretion and casting doubt on which payments are lawful.

Cumulatively, Sections 130, 143, and 145 demonstrate that guarantee law in India is not strictly contractual but profoundly imbued with equitable considerations of trust, good faith, and restitution. However, these provisions reflect legislation devised for a pre-digital, creditor-centric commercial order. This paper calls for immediate statutory reform and doctrinal clarification to

quell the interpretative conflicts that undermine commercial certainty and procedural fairness from these sections. Through this process of judicial interpretation and statutory analysis of these provisions, the present research reveals the pressing demand for legislative updation. The aim is to realign the law on guarantees with contemporary commercial realities while retaining its equitable foundation.

MAPPING THE TERRAINS OF GUARANTEE

There are two pools of words that have similar roots but prove to be starkly distinct from one another. Both comply with the relation of a third person who attempts to secure an obligation created by two other persons, which has been the source of considerable confusion at various times and places. It is stoutly asserted that the ideas expressed by them are the same and maintained with even greater vigor than they are different.[1] Typically, these forms of security find applications where money is borrowed, and the resultant debt is to be secured through collateral security, with a surety or guarantee (or both) being typical forms of security demanded.[2]

A suretyship is an accessory contract in which a person known as the "surety" promises the creditor that the principal debtor will fulfill their obligation, such as repaying a debt. If the debtor fails to perform, the surety becomes liable to perform in their place. Since a suretyship is dependent on the main contract, its validity is directly linked to the existence of a valid principal obligation. If the principal contract between the debtor and the creditor is declared invalid or ceases to exist, the surety is automatically discharged from liability. This is because the surety cannot assume greater responsibility than that of the principal debtor. The surety only accepts the risk of a breach of a valid contract, not the consequences arising from an invalid obligation. Whereas a guarantee operates as an independent and primary obligation. In a guarantee, the guarantor directly undertakes to compensate the creditor for losses upon the occurrence of certain specified events. The guarantor's liability is separate from that of the debtor and is not dependent on the validity of the principal contract. Thus, unlike a suretyship, where liability is conditional upon the validity of the principal obligation, a guarantee remains enforceable as a standalone commitment.

According to *Stearns, the law of suretyship,* "A surety undertakes to pay the debt of another. A guarantor undertakes to pay if the principal debtor does not or cannot. A surety joins in the contract

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[1] Radin, Max. "Guaranty and Suretyship." *California Law Review* 17, no. 6 (1929): 605–22. https://doi.org/10.2307/3475469

[2] Suretyship vs Guarantee: What's the Difference?, PHINC (last visited Dec. 8, 2025), https://www.phinc.co.za/Our-Insights/ArticleDetail?Title=Suretyship-vs-Guarantee-Whats-the-difference

of the principal and becomes an original party with the principal. A surety promises to do the same thing which the principal undertakes; the guarantor promises that the principal will perform his agreement, and if he does not, then he, the guarantor, will do it for him. The liability of the surety is immediate and direct. Both the surety and the guarantor agree to pay the debt of another, but the liability to pay in the case of the surety starts with the agreement, whereas the liability of the guarantor does not start with the agreement, except as a contingent liability, and is established for the first time by default."[3]

FORMS OF GUARANTEE

Guarantee is a vast concept with nearly 15 forms of its kind, spanning from specific guarantee to unlimited guarantee; deferred payments guarantee to advance payment guarantee, and so on. The most relevant of all, which shall be catered to this discussion, is a specific and continuing guarantee. A specific guarantee is a contract that covers only a single transaction or obligation, and it comes to an end once that transaction is completed or the liability is discharged. In contrast, a continuing guarantee extends to a series of transactions over a period of time, making the surety liable for multiple dealings until the guarantee is revoked or terminated.[4] The key distinction lies in the duration and scope: a specific guarantee is limited and irrevocable for its defined purpose, while a continuing guarantee is broader and can be revoked prospectively by notice to the creditor for further transactions.[5]

Other forms of guarantee: Personal Guarantee, Corporate Guarantee, Bank Guarantee, Performance Guarantee, Financial Guarantee, Advance Payment Guarantee, Deferred Payment Guarantee, Conditional Guarantee, Unconditional Guarantee, Joint Guarantee, Several Guarantee, Limited Guarantee, Unlimited Guarantee

UNILATERAL EXIT: THE SURETY'S RIGHT TO WALK AWAY

Section 130 of the Indian Contract Act, 1872, which is regarding the revocation of continuing guarantee, allows a surety to unilaterally revoke a continuing guarantee, a type of guarantee that applies to a series of transactions rather than a single transaction. If a person is serving as a guarantor (surety) for an individual's continuing transactions, he has the option of no longer being liable for any new transactions by informing the individual or firm you gave your guarantee to

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[3] Cook's (3d ed. 1922), §§6 and 5.
[4] Student at School of Law, Bennett University
[5] Tanisha Gautam, *Continuing Guarantee: Nature and Modes of Revocation*, iPleaders (Apr. 23, 2021), https://blog.ipleaders.in/continuing-guarantee-nature-modes-revocation/

(creditor). This section provides grounds of discharge of suretyship & rights of surety in terms of continuing guarantee.

MAIN INGREDIENTS ARE -

- As to further transactions- Prospective in nature
- Notice to the creditor
- Operendi (necessity) - continuing guarantee

Example- Suppose 'A', who owns an eatery store, has a frequent customer by the name of 'B' who buys supplies on credit. 'A' is interested in the credit risk, so she requests that Swati provide a surety for the credit purchases. 'B's friend 'C' agrees to be the surety and assures 'A' that he will pay any overdue debt by Swati up to Rs 2 lakhs. Now it's upon 'C' to voluntarily revoke the guarantee agreement and dispose himself from the position as guarantor from further transactions, only with a said notice.

A continuing guarantee covers a series of transactions as mentioned in Section 129 of the Indian Contract Act, 1872 (unlike a specific guarantee, which is limited to a single obligation). A guarantee of this kind is intended to cover some transactions over a period of time. The surety undertakes to be answerable to the creditor for his dealings with the debtor for a certain time. The distinction between an ordinary and a continuing guarantee is important with reference to the duration of the liability of the surety. The most important aspect of consideration of a guarantee as continuing guarantee is the intention of the parties, and not merely the written contract, not considering the circumstances in which the guarantee was given.[6] Hence, continuing guarantee is the most essential element for revocation of guarantee. A guarantee for a single specific transaction comes to an end as soon as the liability under the transaction ends.[7] As the section starts with the very word of "continuing guarantee" and its revocation. It can be implied that ordinary guarantee remain irrevocable in nature. It has no scope of being cancelled or nullify thereby. It stays concrete, serious, sovereign and solemn.[8]

This section remains prospective in nature. The surety remains fully liable for obligations prior to the date of revocation. Surety remains liable for transactions already entered into. Past transactions that created a liability before revocation remain enforceable against the surety. When a person

[6] Continuing Guarantee: Contemporary Context, International Journal Of Advanced Legal Research
[7] (1829) 6 Bing 276: 130 ER 1287.
[8] Avatar Singh, Contract and Specific Relief pg.636

guaranteed the payment of rent by his servant and revoked it as soon as the servant left his employment, he was held not liable for rents which became due after the revocation.[9] The extinction of suretyship happens only in future transactions, and previous dealings remain untouched outside the purview of amendments and discussions.

REVOCATION BY NOTICE

Revocation is effective only upon notice to the creditor. The Act does not specify a mode of notice, but written notice is recommended to ensure clarity and proof. Until the creditor receives the notice, the surety remains liable. "Notice to the creditor" means a clear and specific notice intended to terminate liability under the guarantee. A denial of liability in a previous suit was held to serve as a notice. The traditional notice varies from the notice specified in this section with certainty in a way that traditional notice involves consequences, informing the grounds, coupled with the element that something is expected from the concerned party once the notice is provided. Additionally, the surety is free to revoke the guarantee at any time before a liability has arisen under a future transaction. No prior consent of the creditor is needed for revocation. Section 130 does not apply to the security given by a guardian under the Minor's Act XX of 1864, so a surety cannot be released from his obligation as surety on account of the guardian's maladministration of the minor's estate, that being the very object of the security. But the surety may apply to the court to revoke his/her guardianship. The same was distinguished in the case of *Narain v. Fulkumari*[10], where it was held that a surety in charge of administration may discharge himself from the liability by giving notice. A surety can withdraw where the guarantee is a continuing guarantee, but where the surety is given by a definite case, the liability continues till the time the surety is discharged by the court.

DEATH AND AUTOMATIC REVOCATION: THE END OF LIABILITY

Though not part of Section 130 itself, Section 131 provides that a continuing guarantee is automatically revoked by the death of the surety, unless there is a contract to the contrary. The liability of the deceased person (here, surety) can be imposed against his legal heirs, but only to the extent of the property inherited by them. If an individual who had agreed to act as a guarantor (surety) for another's continuous obligations or debts dies, and there is no agreement to the

[9] Wingfield v De. St Croix (1919) 35 T.L.R. 432
[10] Narain v. Fulkumari ILR 29 Cal 69.

contrary, their obligation as a guarantor automatically ceases for any obligations or debts which occur after their death.[11]

THE DUTY TO DISCLOSE: CREDITOR'S BURDEN OF TRANSPARENCY

The law entails certain situations where the creditor has an onus to inform the surety about the material facts. *"A creditor must reveal to the surety every fact which under the circumstances the surety would expect not to exist; for the omission to mention such a fact does exist is an implied misrepresentation."*[12] A principal feature of this section is to prove that firstly, there was silence concerning a material circumstance and secondly, the guarantee was obtained through such silence.[13] This section also promulgates a slight conflict between General law and Specific law, and which shall prevail in case of dispute.

Fraud complies with the provisions of Section 17 of the Indian Contract Act, 1872. It encompasses various actions by a contracting party or their accomplice or agent to deceive or entice another party or their agent into entering an agreement. These actions mainly include presenting facts as true, something that is known not to be true, or actively hiding a fact when one has knowledge or belief of its existence and even making a promise without any intention of fulfilling it.[14] Section 143 talks about passive concealment, which is characterized by remaining silent or omitting to disclose relevant information. It happens when a party does not disclose important facts that they are required to reveal. Simply being silent or failing to share information usually does not constitute Fraud unless there is a specific duty to speak, or the silence itself acts like a statement. Since there is already a provision that addresses this issue, there is no need for an additional one, such as Section 143.

PASSIVE SILENCE, ACTIVE FRAUD: DRAWING THE LINE

The general law says that in case of fraud, the agreement remains void at the discretion of the injured party, whereas the specific law says that, as per Sec 143, the guarantee which the creditor has obtained remains "invalid". The term "invalid" is not defined in the Indian Contract Act 1872, which creates unnecessary confusion among the readers.

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[11] Indian Contract Act, 1872

[12] Vashisht, Divita and Gupta, Riya, Bridging the Gap: A Comprehensive Study of Invalid Guarantees and the Extent of the Creditor's Duty of Disclosure under Sections 142 and 143 of the Indian Contract Act, 1872 (May 2, 2024). Available at SSRN: https://ssrn.com/abstract=4815182 or http://dx.doi.org/10.2139/ssrn.4815182

[13] Secretary of State for India v. Nilamekam Pillai, (1911) 21 MLJ 132.

[14] Aishwarya Agrawal, *Fraud under Indian Contract Act*, LawBhoomi (June 7, 2023), https://lawbhoomi.com/fraud-under-indian-contract-act/#Definition_of_Fraud

Section 143 of the Indian Contract Act, 1872, protects against fraud and unfairness in contracts of guarantee. Even though such contracts are not to be considered as those of uberrima fides (utmost good faith), the law still puts a minimum obligation of disclosure on the creditor regarding material facts. Where the creditor, in knowing silence as to a probable fact likely to affect the decision of the surety to enter into the contract, remains silent, the guarantee is void. This principle was upheld in *London General Omnibus Co. v. Holloway (1912)*[15] where the court invalidated a guarantee because the creditor failed to inform the surety of the employee's previous dishonesty. Similarly, in *Rouse v. Bradford Banking Co. (1894),* the court emphasized that silence on material facts could constitute misrepresentation if the creditor was aware of such facts.[16]Section 143 elevates passive silence into a form of misconduct in situations where there exists a legitimate expectation of disclosure between the creditor and the surety. Although silence is generally not treated as fraud under contract law, this provision makes an exception in the context of guarantees by recognizing that non-disclosure of material facts, even without active misrepresentation, can undermine the validity of the agreement.

SHORTCOMINGS IN SECTION 143: AMBIGUITY AND INEQUITY IN DISCLOSURE

Section 143 of the Indian Contract Act, 1872, which invalidates guarantees obtained by the creditor's concealment of material facts, is fraught with significant shortcomings. The Act does not define what constitutes a "material fact," forcing courts to determine its relevance on a case-by-case basis, which can lead to inconsistent rulings and uncertainty for both sureties and creditors. The section also fails to address misrepresentation or concealment by the principal debtor, leaving sureties without recourse if the debtor withholds or misrepresents crucial information, thereby violating principles of natural justice such as Nemo Judex in Causa Sua. Additionally, the law is silent on whether partial disclosure, revealing some facts while concealing others, amounts to concealment, allowing creditors to selectively disclose information without legal consequence.[17] Section 143 merely declares such guarantees invalid but provides no additional remedies, penalties, or damages for the injured party, unlike general fraud provisions, which allow for rescission and restitution under Section 64. Most critically, the burden of proving concealment or deception lies on the surety, who often lacks access to the creditor's information, making it difficult

[15] *London Gen. Omnibus Co. Ltd. v. Holloway*, [1912] 2 K.B. 72 (Eng.)
[16] *Rouse v. Bradford Banking Co.*, (1894) 2 Ch. 77 (Eng.).
[17] *Natural Justice*, Manupatra, https://articles.manupatra.com/article-details/Natural-Justice (last visited Dec. 8, 2025).

to establish the claim and leaving the surety vulnerable to unfair liability. These gaps highlight the need for legislative reform to ensure fairness and clarity in surety contracts.[18]

SILENT ON PARTIAL DISCLOSURE

Although the clause declares guarantees obtained by "concealment" are invalid, it is unclear whether partial disclosure, in which certain facts are concealed and only a few are revealed, qualifies as concealment. This creates an opportunity for a creditor to reveal favorable information while keeping bad information secret, all without breaking the law. When a guarantee is given by deception or concealment, Section 143 just declares it "invalid" and offers no recourse beyond this. There is no additional mention of damages or penalties made to the party responsible for the deception or concealment. In case of fraud in general law, the party deceived may rescind the contract to the degree it is not executed.

The onus to prove is the surety that there was deception or concealment. The creditor typically has greater information about the debtor's financial situation, past defaults, and other significant issues. The surety may lack the financial means, legal expertise, or reach necessary to properly uncover such facts or prove concealment. Despite the negative effects on the surety, the clause allows creditors to escape obligation based on ignorance or lack of intent.

IMPLIED INDEMNITY FOR THE SURETY

Section 145 is concerned with the right of indemnity of the surety over the principal debtor. It states that since a surety (guarantor) pays a debt or liability incurred on behalf of the principal debtor, the law implies a promise on the part of the principal debtor to compensate the surety. The surety can only recover money rightfully paid under the guarantee, not any amount paid voluntarily or wrongly.[19] Thus, when a surety does their act (i.e., settles with the creditor), the law considers that the surety owes the amount by the principal debtor.[20] Section 145 also establishes that in a contract of guarantee, there is an implied promise by the principal debtor to indemnify the surety. This means that even in the absence of an express clause, the law automatically presumes that the principal debtor is under an obligation to reimburse the surety for any lawful payments made by the surety under the guarantee. Hence, the principal debtor remains duty- bound to indemnify the surety's entitlement to recover from the principal debtor.

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[18] "Retreat From Natural Justice: A Study On Evolution Of The Principle Of Natural Justice", CENTRE FOR ACADEMIC LEGAL RESEARCH | JOURNAL OF APPLICABLE LAW & JURISPRUDENCE

[19] AMERICAN LAW REGISTER.

[20] Contrast between Contract of Indemnity and Guarantee under the Indian Contract Act, International Journal of Science and Research (IJSR)

Only when the surety's payment is legitimate and compliant with the terms of the guarantee does the surety have the right to reimbursement. The phrase "rightfully paid" suggests that the money must be given in good faith, be legally owed in accordance with the guarantee's conditions, and not be made prematurely, excessively, or needlessly. The guarantor cannot claim indemnification if the payment is made without the principal debtor actually defaulting or in a circumstance where there was no legal obligation to pay. [21]The surety must really make payment under the guarantee for the surety to exercise its right under Section 145. The right to demand compensation from the principal debtor does not exist until the surety has released the liability. *For instance*, A cannot demand payment or indemnification from B in anticipation of a potential default if A has guaranteed B's debt and B has not yet defaulted. The right to indemnity under Section 145 does not accrue until A has made the payment.

Additionally, as observed, the section seems to have a broad criterion as it mentions “every contract,” thus comprising all trade transactions. Implies that the right to indemnity exists in all guarantee contracts, even without express wording. It also ensures that the surety is not left hanging after fulfilling their obligation. They are legally entitled to recover what they paid on behalf of the debtor. Also, this section is stringent as parties cannot create exceptions even if they intend to do so in spite of freedom of contract.

- **DUTIES** = In every contract of guarantee, there is an implied promise by the principal debtor to indemnify the surety.

- **RIGHTS=** the surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but no sums which he has paid wrongfully.

OVERLAPS AND OMISSIONS: INDEMNITY AND CO-SURETIES

Section 145 of the Indian Contract Act, 1872, which provides for the implied promise of indemnity to the surety, suffers from significant ambiguities and omissions. The term "rightfully paid" is not defined in the statute, leaving courts to determine, on a case-by-case basis, whether a payment qualifies for indemnity. This lack of clarity can result in contradictory rulings and increased litigation, as seen in various judicial interpretations where courts have struggled to define what constitutes a legitimate payment. Furthermore, the surety can only claim indemnity after making actual payment under the guarantee, which places the surety at a financial disadvantage, especially

[21] Statutory Omissions of Rights of Debtors under the Indian Contract Act, 1872 in Contra-distinction to the Insolvency and Bankruptcy Code, 2016: A Qualitative Analysis

when the principal debtor's insolvency is imminent. This rule offers no preventive remedy or anticipatory relief, forcing the surety to bear the loss before seeking recourse. The overlap between Section 145 and the general indemnity provisions in Sections 124 and 125 of the Act leads to interpretational confusion. While specific provisions like Section 145 prevail over general ones, the absence of a clear demarcation often results in inconsistencies in judicial decisions. Additionally, Section 145 is silent on the rights and obligations of co-sureties. Although Section 146 addresses contributions among co-sureties, the lack of cross-reference and integration between these sections can undermine the coherence of statutory protection for sureties.

Recent judicial and academic commentary suggests that guarantee law is evolving to reflect equity principles such as indemnity, good faith, and fair dealing, rather than being purely contractual. There is a growing call for legislative reform, including the recognition of electronic or email revocation notices under Section 130, to adapt to modern commercial realities and ensure greater protection for sureties.

POLICY RECOMMENDATIONS AND WAY FORWARD

To address the loopholes in the existing laws its essentially required that new legislative reforms must be motivated to clarify critical provisions in the Indian Contract Act, 1872. The act should explicitly define the form and proof of notice for revocation under Section 130, including recognition of electronic communication such as email, WhatsApp, to align with contemporary transactional practices. A clear legal definition of "material fact" and concealment under Section 143 is necessary to reduce judicial discretion and ensure consistent application. The law must also protect sureties from misrepresentations by the principal debtor, not just the creditor, to uphold fairness and justice. Additionally, Section 145 should define "rightfully paid" to avoid confusion and ensure fair claims for indemnity. Courts should have clear guidelines for handling partially executed or ongoing transactions when revocation occurs. The Act should offer remedies or penalties beyond simple invalidation for concealment. Courts must balance fairness and contract certainty in suretyship cases to protect all parties involved. In conclusion, the challenges sureties face highlight the urgent need for legal updates, clear standards, and the fair development of surety rights to match modern business practices and safeguard the interests of everyone involved.