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DOES THE GUARANTOR GUARANTEE? LENDER, BEWARE!

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It might be assumed that the relationship between the guarantor and the holder of a promissory note is a rather settled and predictable area of commercial transactions. The recent Superior Court of New Jersey decision in *Ligran, Inc. v. Medlawtel, Inc.*,[1] however, does violence to that relationship by creating uncertainty over the guarantor's obligation to pay. The decision, if permitted to stand, challenges the common assumption that the guarantor unconditionally guarantees payment. It is an anomalous departure from New Jersey case law, accepted common law tenets, and a fair and purposive reading of New Jersey's Article 3 of the Uniform Commercial Code[2] dealing with commercial paper.

I. The Case

The underlying facts were essentially undisputed.[3] In April of 1969 the plaintiff, Ligran, Inc., agreed to lease two motels to the defendant Medlawtel, Inc., for a five year period beginning on May 1, 1969 with an option to renew.[4] The lessee was to provide a $25,000 security deposit for the premises of which half would be paid in cash and half would be in the form of a promissory demand note.[5] There was no reference in the lease to the note.[6] On April 28, 1969

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[1] 174 N.J. Super. 597, 417 A.2d 100 (App. Div.), *certif. granted*, — N.J. —, — A.2d — (1980).

[2] N.J. Stat. Ann. §§ 12A:3-101 to 3-805 (West 1962).

[3] 174 N.J. Super. at 599, 417 A.2d at 101.

[4] *Id.*

[5] *Id.*; Brief for Defendant-Appellant at 5 [hereinafter cited as Defendant's Brief].

[6] Defendant's Brief at 5-6.

defendant Elizabeth Butkus, a principal of the defendant corporation, executed a note for $12,500 made payable to plaintiff Martin Anger, a principal of the plaintiff corporation.[7]

Significantly, defendant Butkus signed the note both as maker and guarantor, both on the face of the note as sole maker and on the reverse side as sole guarantor.[8] A printed notice of guarantee of payment provided:

> For value received the undersigned and each of them forever waives presentment, demand, protest, notice of protest and notice of dishonor of the within note and the undersigned, and each of them guarantees the payment of said note with interest at maturity or any time thereafter and consents without notice to any and all extensions of time or terms of payment made by holder of said note.[9]

There was some disagreement whether demand for payment actually was made, and if so, whether made prior to the lapse of the statutory period for filing suit.[10] The plaintiff contended that in March of 1975 its attorney learned from the tax collector that the defendant was in arrears on property tax payments owed under the lease terms.[11] Sometime thereafter plaintiff's attorney called defendant's counsel, notified him of the tax "default," and "inquired about payment of the promissory note."[12] Defendant's attorney replied that the note could not be collected since the statute of limitations had expired.[13] Denying that this conversation constituted a demand for payment and subsequent refusal, the defendant argued that payment merely was "discussed," but that no actual demand was made until June of 1975 when plaintiff turned over the note to its attorney.[14]

In June of 1975, plaintiff took back the leased premises and three months later filed a multi-count complaint which included a charge

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[7] 174 N.J. Super. at 599, 417 A.2d at 101.

[8] *Id.*

[9] *Id.*

[10] *See id.* The court did not discuss this disagreement. *See* Brief for Plaintiffs-Respondents at 5 [hereinafter cited as Plaintiff's Brief]; Defendant's Brief at 6. There were actually two defendants, the corporation, Ligran, Inc. and Mr. Anger, and two plaintiffs, the corporation Medlawtel, Inc. and Mrs. Butkus. Since both corporations were closely held, the courts focused on the individuals. For purposes of simplicity, this article will refer to one "defendant" and one "plaintiff." The trial court, however, ruled in favor of plaintiff on this point. *See* note 16 *infra* accompanying text.

[11] Plaintiff's Brief at 5.

[12] *Id.*

[13] *Id.*

[14] Defendant's Brief at 6.

that defendant Butkus was individually liable as guarantor on the note.[15] Agreeing with plaintiff's arguments that filing of the suit was timely, the Law Division of the Superior Court of New Jersey held defendant Butkus liable.[16] Butkus appealed from that decision and the plaintiff cross-appealed from a dismissal of other counts.[17] The parties did not dispute the application of the general statute of limitations[18] providing that suit must be brought within six years of accrual of a cause of action.[19]

The only issues which the appellate division considered were when the cause of action on a demand promissory note begins to accrue against the guarantor, for purposes of triggering the six year statute, and whether the fact that the maker and guarantor were the same person was of significance.[20]

Before turning to the arguments, the pertinent problems inherent in N.J. STAT. ANN. §§ 12A:3-101 to 3-805 should be outlined briefly. These statutes embody Article 3 of the Uniform Commercial Code, an elaborate set of rules governing virtually all aspects of commercial paper.[21] The court focused particular attention on section 3-122, "Accrual of Cause of Action,"[22] but found no definitive answer in the section itself.[23] The problem was that in drafting section 3-122 the draftsmen were silent on the salient issue as to when a cause of action accrues against a guarantor. The section clearly sets forth rules for accrual of a cause of action against a "maker,"[24] "acceptor,"[25]

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[15] 174 N.J. Super. at 599, 417 A.2d at 101.

[16] *Id.* at 600, 417 A.2d at 101.

[17] *Id.* at 599, 417 A.2d at 101.

[18] N.J. STAT. ANN. § 2A:14-1 (West 1952).

[19] *See* 174 N.J. Super. at 600, 417 A.2d at 101.

[20] *Id.* at 598, 417 A.2d at 100. The court dismissed the cross-appeal in one sentence: "As to the cross-appeal, we are satisfied that the record as a whole supports the determination reached." *Id.* at 603, 417 A.2d at 103.

[21] *See* note 77 *infra* and accompanying text.

[22] N.J. STAT. ANN. § 12A:3-122.

[23] *See* 174 N.J. Super. at 600-03, 417 A.2d at 101-03.

[24] N.J. STAT. ANN. § 12A:3-122(1). Section 3-122 provides in part:

> (1) A cause of action against a maker or an acceptor accrues
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> (a) in the case of a time instrument on the day after maturity;
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> (b) in the case of a demand instrument upon its date or, if no date is stated, on the date of issue.
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> (2) A cause of action against the obligor of a demand or time certificate of deposit accrues upon demand, but demand on a time certificate may not be made until on or after the date of maturity.
>
> (3) A cause of action against a drawer of a draft or an indorser of any instrument accrues upon demand following dishonor of the instrument. Notice of dishonor is a demand.

Id. § 12A:3-122.

[25] *Id.*

"drawer,"[26] and "indorser,"[27] but makes no mention of a "guarantor." The entire case on appeal turned on how to classify the defendant, *qua* guarantor, within the section 3-122 scheme.[28] In summary the plaintiff argued that the indorser provision—accrual date on maker's dishonor—applied, thus avoiding any statutory bar.[29] The defendant, on the other hand, asserted that the maker provision—accrual date on the note's making—applied, thus barring plaintiff's suit. The court agreed with the defendant.[30]

Plaintiff conceded that neither statute nor case law provides significant guidance on the application of the statute of limitations to the guarantor of a note. They found much comfort, however, in the superior court's construction of section 3-122 in *Central Jersey Bank & Trust v. Lady Van Industries, Inc.*,[31] the facts of which were similar, but not identical, to the instant case. In *Lady Van* the defendant signed a promissory demand note both as agent for the corporate maker and individually as guarantor.[32] The maker defaulted, and the holder sued the guarantor for the balance owed.[33] The issue was whether the six year statute of limitations barred the action.[34] The *Lady Van* court asserted that the guarantor's liability is the same as the indorser's and that section 3-414, "Contract of Indorser," applied to the guarantor.[35] This section provides that the indorser's obligation to pay on the note arises upon the maker's default.[36] This led the court to conclude that the section 3-122(3) indorser provision—accrual date on maker's dishonor—applied.[37] The court, therefore, held that the suit against the defendant as guarantor was timely since it was brought within six years of the maker's default.[38]

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[26] *Id.* § 12A:3-122(3).

[27] *Id.*

[28] *See* 174 N.J. Super. at 600, 417 A.2d at 101.

[29] *See* notes 39-42 *infra* and accompanying text.

[30] *See* notes 48-54 *infra* and accompanying text.

[31] 154 N.J. Super. 459, 381 A.2d 831 (Law Div. 1977).

[32] *Id.* at 460, 381 A.2d at 832. The guarantee of payment clause in *Lady Van* was essentially the same as its counterpart in *Ligran*. *Id.* *See* text accompanying note 9 *supra*.

[33] 154 N.J. Super. at 461, 381 A.2d at 832.

[34] *Id.* at 460, 381 A.2d at 832. The statutory provision in *Lady Van* and *Ligran* was the same. *Id.* at 461, 381 A.2d at 832; 174 N.J. Super. at 600, 417 A.2d at 101.

[35] 154 N.J. Super. at 462, 381 A.2d at 833.

[36] Section 3-414 provides in pertinent part:

> (1) Unless the indorsement otherwise specifies (as by such words as "without recourse") every indorser engages that upon dishonor and any necessary notice of dishonor and protest he will pay the instrument according to its tenor at the time of his indorsement to the holder or to any subsequent indorser who takes it up, even though the indorser who takes it up was not obligated to do so.

N.J. STAT. ANN. § 12A:3-414(1).

[37] 154 N.J. Super. 461-63, 381 A.2d at 832-33.

[38] *Id.* at 463, 381 A.2d at 833.

Relying on the *Lady Van* rationale, the *Ligran* plaintiff equated the liability of the *Lady Van* and *Ligran* guarantors.[39] Both were indorsers under sections 3-414 and 3-122(3).[40] Suit was brought against both within six years of the maker's default.[41] Both suits were timely.[42]

Arguing in the alternative to estop the defendant from raising the statutory bar, plaintiff invoked the "discovery rule."[43] Explaining the rule, plaintiff contended that the statute of limitations, as a statute of repose for denying stale claims, should not defeat actions in which the plaintiff did not know or have reason to know that it had a valid cause until after the expiration of the statutory period.[44] Plaintiff maintained that in the absence of prejudice to the defendant, the court should invoke its equitable powers to estop the defendant from pleading the statutory bar.[45] As a corollary to the equitable argument, the plaintiff claimed that the defendant effectively waived the six year statute of limitations because the obligation underlying the promissory note was a ten year lease.[46] The parties intended the note to be valid throughout the lease term since the defendant acknowledged the debt on the note through rent payments on the lease.[47]

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[39] Plaintiff's Brief at 10-12.

[40] *Id.*

[41] *Id.*

[42] *Id.* On petition for certification to the Supreme Court of New Jersey plaintiff asserted that one person may simultaneously serve in the dual capacities of maker and guarantor. Plaintiff contended that the exigencies of modern business practices frequently require one individual to serve in several capacities in the same transaction. Elaborating on the argument, plaintiff argued that there were actually two separate and distinct contracts within the promissory note. The first was defendant's contract as maker of the note, and the second was her contract to guarantee payment which she signed in order to induce the plaintiff to execute the lease agreement. Breach of the first contract was a condition precedent to defendant's obligation to perform on the second contract. Thus the plaintiff applied a contract theory to reach the same conclusion that since a guarantor's obligation to pay does not arise until the maker dishonors demand for payment, the cause of action on the guarantee does not accrue until dishonor. Tacitly conceding that its cause of action against the defendant as maker was time barred, plaintiff asserted that defendant was liable as guarantor. Petitioners' Brief for Certification at 7-9 [hereinafter cited as Petitioner's Brief]. Again, there were two petitioners for certification but for simplicity this article will refer to only one "petitioner."

[43] Plaintiff's Brief at 7-9.

[44] *Id.* Plaintiff relied heavily upon New Jersey case law development, particularly Lopez v. Sawyer, 62 N.J. 267, 300 A.2d 563 (1973); Farrell v. Votator Div. of Chemetron Corp., 62 N.J. 111, 299 A.2d 394 (1973); and Bowler v. Fidelity & Cas. Co. of N.Y., 99 N.J. Super. 184, 239 A.2d 22 (App. Div. 1968). The "discovery rule" will be explored further. *See* notes 182-94 *infra* and accompanying text.

[45] Plaintiff's Brief at 8.

[46] *Id.* at 8-9.

[47] *Id.* Plaintiff has developed the equitable argument in its petition for certification. It contends that when a party, such as the plaintiff, detrimentally relies upon the promises of another,

Defendant countered that the six year statute of limitations accrued against the guarantor on the date of the making of the note, claiming that the statute had run before the action was filed, thereby barring it.[48] Confronting the ambiguity of section 3-122, the defendant argued that section 3-416, "Contract of Guarantor," applied to the guarantor and that the guarantor's liability is the same as the maker's.[49] This section provides that the guarantor of payment agrees to pay the note according to its tenor, without the holder resorting to any other party and without need of words of guarantee.[50] The defendant cited New Jersey Study Comment 1 to that section which provides that: "One who by indorsement guarantees payment waives the conditions precedent that usually attach to the indorsement contract and become for all practical purposes a co-maker."[51] Defendant claimed that she was a guarantor of payment within the purview of section 3-416 because both by the specific terms of the note's guarantee clause and by operation of law, she waived any condition precedent to her obligation to pay the note.[52] This led the defendant to conclude that she should be placed squarely within section 3-122(1)—accrual date on note's making.[53] Thus, plaintiff's action should have been time-barred since it was commenced beyond six years from the making of the note.[54]

The defendant argued alternatively that unlike the instant case, the *Lady Van* maker partially paid on the note thereby tolling the

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such as the defendant, the promissor should be estopped from invoking a statutory bar in order to escape his duties. This principle is particularly applicable because the statutory period had run only a few months before the action was brought. Finally, the plaintiff asserted that allowing the defendant the statutory bar would be "unrealistic and inequitable" in the context of modern business needs. Petitioner's Brief at 10-11.

[48] Defendant's Brief at 9.

[49] *Id.* at 9-11.

[50] Section 3-416 provides in pertinent part:

> (1) "Payment guaranteed" or equivalent words added to a signature mean that the signer engages that if the instrument is not paid when due he will pay it according to its tenor without resort by the holder to any other party.

N.J. STAT. ANN. § 12A:3-416(1). It is significant that the phrase "if the instrument is not paid when due" in the above section implies that it was intended to apply to a note with a specific maturity date rather than a demand note, as in the instant case. *See* notes 146-47 *infra* and accompanying text.

[51] N.J. STAT. ANN. § 12A:3-416, N.J. Study Comment 1.

[52] Defendant's Brief at 11.

[53] *Id.* at 9-10. The defendant claimed that her interpretation of liability under section 3-122 would apply to any indorser who, like the defendant, waived demand for payment. Arguing that the label "guarantor" is irrelevant in this instance, the defendant asserted that the waiver effectively placed her liability on the same basis as that of the maker. *Id.* at 12.

[54] *Id.* at 15. The defendant distinguished the instant case from *Lady Van* by claiming that the testimony revealed no positive evidence that demand for payment ever was made before plaintiff commenced the action. *Id.*

statutory bar.[55] The corporate maker of the note had made regular payments within four months of the plaintiff's action.[56] Such payments beyond the statutory period were considered an acknowledgment of the debt on the note.[57] The *Lady Van* court asserted that it would place a commercial burden and inequity on the holder of the note if the guarantor were relieved of liability where payments had been made on a regular basis.[58] The court held that the payments tolled the statute of limitations.[59] The *Ligran* defendant interpreted the *Lady Van* holding to mean that the guarantor's liability had continued only because the maker's liability had not been extinguished.[60] In the instant case, however, defendant claimed that the maker made no payment on the note, that she did not acknowledge the debt, and therefore her liability was extinguished.[61] Defendant contended that it would be "illogical," "inconsistent," and "commercially unfair and unreasonable" to subject the guarantor of payment to a liability beyond the period during which the maker was liable.[62] Thus, the lower court should have applied the statutory bar which defendant, as guarantor, had claimed.[63] The defendant did not address plaintiff's contention that the discovery rule applied.

The appellate division accepted the defendant's argument that the action against her as guarantor of the note was time barred, and overruled *Lady Van*.[64] The court held a cause of action against the guarantor of a demand note accrues on the date of the note's issuance, and not upon demand and dishonor.[65]

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[55] *Id.*

[56] *Id.* at 13.

[57] *Id.* at 14.

[58] *Id.*

[59] *Id.* In a parenthetical argument the defendant noted that *Lady Van* overturned the 1938 decision, Marinelli v. Lombardi, 16 N.J. Misc. 71, 196 A. 701 (Sup. Ct. 1938), which held that a maker's payment on the notes does not serve to extend a guarantor's liability beyond the statutory period even though a guarantor may waive notice of such extension. *Id.* at 73, 196 A. at 702-03 (cited in Defendant's Brief at 14). It should be noted, however, that the *Marinelli* holding, which the defendant cited, was a pre-U.C.C. case. Furthermore, the defendant did not elaborate on the holding, but rather merely left the implication that the *Lady Van* decision was improper. Defendant's Brief at 14.

[60] Defendant's Brief at 14-16. The defendant claimed that this interpretation of *Lady Van* accords with her contention that the liability of the guarantor of payment is coextensive with the maker's. *Id.*

[61] *Id.* at 14-15. The defendant explained that the lower courts did not reach the question of whether the statute of limitations against her in her capacity as maker had expired. The court considered the issue moot because of its finding that she was liable as guarantor. *Id.* at 8.

[62] *Id.* at 12-13.

[63] *See id.* at 15.

[64] 174 N.J. Super. at 598-99, 417 A.2d at 100.

[65] *Id.*

The court confronted the choice of whether to classify the defendant in her capacity as guarantor as a maker or as an indorser in the section 3-122 scheme for accrual date.[66] It disapproved the trial judge's reliance on the *Lady Van* view that the indorser clause controlled.[67] The court broadly held that the section 3-122(1) maker accrual date applies to a guarantor of payment on a demand note, even if the maker and guarantor are two different persons.[68] It reasoned that since 3-122(1) provides for accrual of a cause of action against the maker of a demand note upon its issuance date, the statutory period for commencing the action had expired against the defendant both in her capacity as maker and as guarantor.[69]

The court declared that the note's guarantee clause did not alter the fact that the guarantor's liability was coextensive with the maker's.[70] The court accepted defendant's equitable claim that to extend the defendant's liability as guarantor would necessarily extend her liability as maker since she served in both capacities.[71]

The court failed to consider plaintiff's application of the discovery rule to estop defendant from pleading the statutory bar. It also dismissed plaintiff's estoppel argument that the note's underlying lease obligation had a ten year term and that it would be unfair to apply the statute of limitations as a bar to actions within that period.[72] The argument was said to be without merit because it was "irrelevant to the maker-guarantor question" in which the maker certainly would not have been statutorily liable had she not guaranteed.[73] Furthermore, the court agreed with the defendant that the plaintiff had made a bad business judgment.[74] The plaintiff easily could have required replaced security upon the lease's renewal or simply could have demanded cash security under the lease terms.[75] The court concluded that having made the decision to accept the note in lieu of cash security, the plaintiff was "subject to the ordinary legal predicates surrounding the instrument."[76]

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[66] *Id.* at 600, 417 A.2d at 101.

[67] *Id.* at 599, 417 A.2d at 100.

[68] *Id.* at 601, 417 A.2d at 102. The court asserted that the concept of a single person serving both as the maker and guarantor is an "anomaly" and a "conceptual redundancy" which contradicts the view that the guarantor's liability should not exceed the maker's. Essentially considering the guarantor a comaker, the court asserted that "the guaranty by the maker of his own obligation is essentially surplusage." *Id.*

[69] *See id.* at 600-01, 417 A.2d at 101-02.

[70] *Id.* at 600, 417 A.2d at 101.

[71] *Id.*

[72] *Id.* at 602, 417 A.2d at 102-03.

[73] *Id.*, 417 A.2d at 103.

[74] *Id.*

[75] *Id.*

[76] *Id.*

It is submitted that the opinion of the appellate division is unsound.

II. Common Law, Prior Statutes, and Definition of Terms

The drafters of Article 3 of the Uniform Commercial Code intended it to be a complete codification and revision of the law covering commercial paper replacing the Uniform Negotiable Instruments Law (N.I.L.).[77] Despite these intentions, the U.C.C. writers recognized the need for retaining common law principles and equities and expressly preserved these precedents in section 1-103, "Supplementary General Principles of Law Applicable."[78] This section provides:

> Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.[79]

The drafters declared that these sources may be applied "to render valid any right or transaction."[80]

Though section 1-103 provides considerable flexibility for use of common law principles and equities, courts must adhere to the "particular provisions" of the Code which displace them.[81] A court, therefore, must apply the accepted canon of statutory construction first examining the statute for its clear and unambiguous import.[82] Where the Code is silent or ambiguous on the matter in controversy, the court then should resort to section 1-103 to expand the sources of guidance and construction to include common law, prior law, and

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[77] U.C.C. § 3-101, Comment. The New Jersey Commission to Study and Report on the Commercial Code also adopted this view:

> The Uniform Negotiable Instruments Law (N.I.L.), the earliest American uniform commercial law, was drafted in 1896, adopted in New Jersey in 1902. . . . Until its repeal by the Uniform Commercial Code it had not been changed for sixty years, but it had long been overdue to revision and modernization. The Commercial Code was designed to be an integrated statute covering the entire field of commercial law and the displacement of the N.I.L. was an essential part of the scheme.

N.J. Stat. Ann. § 12A:3, Introductory Commentary. New Jersey adopted the N.I.L. in 1902 (N.J. Rev. Stat. §§ 7:1-1 to 6-28 (1934)) and repealed it in 1961 with the adoption of N.J. Stat. Ann. §§ 12A:1-101 to 10-106.

[78] N.J. Stat. Ann. § 12A:1-103.

[79] *Id.*

[80] U.C.C. § 1-103, Comment 1. New Jersey adopted this comment in full in N.J. Stat. Ann. § 12A:1-103.

[81] N.J. Stat. Ann. § 12A:1-103.

[82] 82 C.J.S. *Statutes* § 322 (1953).

consistent provisions of repealed statutes.[83] New Jersey Code cases have consistently adhered to this view.[84]

The instant case involved a Code section which is silent on the matter in controversy,[85] and even a construction of the section *in pari materia* with other sections produces ambiguous results.[86] An extra-Code analysis seemed to be required to assist the court in determining which clause in 3-122 properly should apply.

The early law of commercial instruments developed outside the legal establishment.[87] European law refused to apply legal standards to a credit instrument for reasons of non-assignability,[88] privity,[89] and in order to discourage litigation.[90] Such inflexibility ignored the exigencies of increasing commerce throughout the late Middle Ages and early Renaissance and forced the development of a separate body of extra-legal rules for commercial intercourse.[91] Italian merchants are credited with developing the precursor of the modern bill of exchange in order to facilitate the exchange of one country's currency

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[83] R. ANDERSON, ANDERSON ON THE UNIFORM COMMERCIAL CODE, § 1-103:3, § 1-103:5 (1970). Anderson states in his commentary on section 1-103:

> Code § 1-103 recognizes that the Code does not purport to declare those general principles of law which are applicable not only to commercial law but which run through many branches of areas of the law and in some instances are fundamental to the American system of jurisprudence and its legal philosophy. It is therefore specifically provided that areas not covered by the Code are to be governed by the prior law.

Id. § 1-103:3. Anderson further provides that "[r]epealed statutes may be examined for the purpose of concluding what the law should be where the Code does not make an express provision relating thereto." *Id.* § 1-103:5.

[84] *See, e.g.*, Clarkson v. Selected Risks Ins. Co., 170 N.J. Super. 373, 406 A.2d 494 (Law Div. 1979) (concepts in other fields of law should be considered when interpreting Code); Pavesi v. Ford Motor Co., 155 N.J. Super. 373, 382 A.2d 954 (Ch. Div. 1978) (where Code is silent general equitable principles apply); Demos v. Lyons, 151 N.J. Super. 489, 376 A.2d 1352 (Law Div. 1977) (common law equities apply to interpretation of clause in Code).

[85] N.J. STAT. ANN. § 12A:3-122, "Cause of Action," is silent on the obligation of the "guarantor." *See* notes 22-27 *supra* and accompanying text.

[86] The court implicitly recognized the section 3-122 dilemma as a choice between applying clause (1) (maker-accrual date) or clause (3) (indorser-accrual date). 174 N.J. Super. at 600, 417 A.2d at 101. *See* text accompanying notes 28-30 *supra*.

[87] *See* M. BIGELOW, THE LAW OF BILLS, NOTES AND CHEQUES, 1-8 (2d ed. 1900); W. BRITTON, HANDBOOK OF THE LAW OF BILLS AND NOTES, 1-4 (1943).

[88] W. BRITTON, *supra* note 87, at 3. Britton explained that early European law regarded the credit instrument as a chose in action with no tangible form and therefore not assignable. *Id.*

[89] *Id.* Britton stated: "The debtor-creditor relation was regarded as too personal to permit the first creditor to substitute another in his place." *Id.*

[90] *Id.* Britton wrote: "Later, the idea that the enforcement of an assignment would tend to encourage litigation was used to support the rule of non-assignability." *Id.*

[91] *See, e.g.*, Bank of Conway v. Stary, 51 N.D. 399, 408-09, 200 N.W. 505, 509 (1924). The opinion emphasized that the law merchant, or *lex mercatoria*, developed separately from the common law:

with another's.[92] As commerce developed, the need to exchange money increased, and the great fairs of the Middle Ages became the places to settle accounts and disputes among merchants.[93] Necessity led to the establishment of Fair Courts, comprised of fellow merchants, who would adjudicate disputes based on accepted trade custom and practice.[94] It was in these courts that the law merchant, the early law of commercial transactions, first developed.[95]

The law merchant had become so predominant as the accepted means of settling commercial disputes that when English sovereigns finally recognized its legitimacy in 1353, a separate system of courts was established which administered the law merchant exclusive of common law principles.[96] The founding of this system, called the staple courts, marked a new period in the regulation of commercial conduct, and lasted until the nineteenth century, though its influence declined markedly after about 1670.[97] The most significant part of this development was that the law merchant grew independently of English common law, which ultimately adopted the basic law merchant for its treatment of commercial transactions.[98] American

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> It should be noted that the lex mercatoria was originally a separate body of law. . . . Though its principles were adopted into the common law by Lord Mansfield, the law merchant still remained a body of rules applicable to a certain class of transactions and international in character.

Id. at 408-09, 200 N.W. at 509.

[92] W. BRITTON, *supra* note 87, at 4.

[93] *Id.*

[94] *Id.*

[95] *Id.*

[96] Burdick, *What Is The Law Merchant?*, 2 COLUM. L. REV. 470, 470-74 (1902). The author observed that when Edward III established the staple court system in 1353 for adjudicating the law merchant, the Statute of Staples provided that, unlike common law, disputes would be settled quickly by judges learned in the law merchant. *Id.* at 472. Burdick explained: "The procedure, then, in the statutory courts of the staple was that of the law merchant, and was very different from that of the common law." *Id.* at 474.

[97] Beutel, *The Development of Negotiable Instruments In Early English Law*, 51 HARV. L. REV. 813, 813-14 (1938). The writer suggested that there were roughly four fairly discernible periods in the early development of the law of commercial instruments. The first, which he dubbed "the primitive stage," spanned from the time of the landing of William the Conqueror to the establishment of the staple court (1353). The second, "the staple jurisdiction," continued as late as the nineteenth century but overlapped the third and fourth periods. Throughout the third "transition period," 1524 to 1670, the staple courts battled other courts for jurisdiction. The fourth period began when the admiralty courts finally lost their jurisdiction in 1670 to the common law courts which attempted exclusive jurisdiction and development of commercial instrument law. *Id.*

[98] Burdick, *supra* note 96, at 473-82; W. BRITTON, *supra* note 87, at 5-6. Professor Burdick stated:

> It is apparent . . . that for several centuries there was a true body of law in England which was known as the law merchant. It was as distinct from the law administered by the common law courts, as was the civil or the canon law.

statutory codifications of common law soon embodied the law merchant, albeit in modified form, and expressly accepted its continued validity.[99] The principles of the law merchant, therefore, have a settled place in the American jurisprudence of commercial paper, particularly where a search beyond the statute is required.

One of the dominant features of the law merchant throughout its development was its insistence on speedy, simple adjudication which stressed the equities of the parties involved.[100] This emphasis should not be surprising in light of the fact that the law merchant sprang into being to imbue commercial transactions with a high degree of certainty.[101] The early courts of the law merchant recognized a wide variety of negotiable instruments in use including assignable bonds, bills of exchange, and promissory notes.[102] The promissory note, in fact, may have been the first negotiable instrument which an English court recognized.[103] Historical records further indicate that the law merchant enforced the liability of a drawer, and possibly enforced the liability of the indorser and transferor to the holder of a note.[104]

As the staple court system deteriorated,[105] the admiralty courts adopted the law merchant for commercial cases accepting such concepts as the right of third party beneficiaries to promissory notes.[106] Recognition of this right predated similar common law development by over three hundred years.[107] Later English statutory and common

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Burdick, *supra* note 96, at 478. Burdick further noted that "Lord Mansfield's habit, of applying the principles of the law merchant to the decision of cases, brought in the common law courts, has been followed for a century and a half by English and American judges." *Id.* at 482.

[99] W. BRITTON, *supra* note 87, at 15-16. The N.I.L., the first American codification of commercial law, had two primary sources. One was American colonial statutes and the other was British common law decisions. W. BRITTON, *supra* note 87, at 15-16. As discussed earlier, the British common law decisions embodied the law merchant. *See* note 98 *supra* and accompanying text.

The N.I.L. specifically provided for the continued force and effect of the law merchant in section 1-6; "Rules of Law Merchant. In any case not provided for in this subtitle the rules of the law merchant shall govern." N.J. REV. STAT. § 7:1-6 (1934) (repealed 1961). This was the predecessor clause to present N.J. STAT. ANN. § 12A:1-103, "Supplementary General Principles of Law Applicable." *See* text accompanying notes 78-79 *supra*.

[100] Beutel, *supra* note 97, at 815-16. Beutel explained that though the Fair Courts meted out justice in a speedy and simple fashion, "they were carefully conducted courts of record." As an example of their stress on fair treatment, the courts provided juries which included foreign merchants when cases involving foreigners were considered. *Id.*

[101] *See* notes 87-91 & 94 *supra* and accompanying text.

[102] Beutel, *supra* note 97, at 828-30.

[103] *Id.* at 830. Beutel reported: "There are records of these instruments as early as year 1300. A bearer was allowed to sue on such an instrument in the courts of London in 1414." *Id.*

[104] Beutel, *supra* note 97, at 831 & 831 n.1.

[105] *See* note 97 *supra* and accompanying text.

[106] Beutel, *supra* note 97, at 835-36.

[107] *Id.* at 836.

law subsumed the equities embodied in the law merchant.[108] It appears that the commonly understood intent of the parties was enforced in the interest of facilitating commerce and to fulfill the reasonable expectations of parties to commercial paper.

The early commercial law decisions of American courts reflect the common sense and practical approach to business disputes inherent in the law merchant.[109] This is evidenced in both federal and state court decisions which exhibited a predilection to apply a common understanding of the terms of the agreement and to adhere to the intent of the parties.[110] This approach reflected the accepted precept that to serve business needs, the law should be predictable, expeditious, and compatible with commercial expectations.[111]

Early American cases do not directly examine the issue of the accrual of a cause of action against the guarantor of a demand promissory note. Except for *Lady Van*[112] neither early nor modern New Jersey decisions have considered the matter.

Cases which considered the liability of a guarantor uniformly involved the default of the maker or principal.[113] Some event,

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[108] *Id.* at 844-45. The common law courts did not consistently apply these equities leading to considerable dissatisfaction among the merchant class which prevailed upon Parliament for redress. This resulted in the enactment of the Commercial Arbitration Act in 1698 and the Statute of Anne in 1704 which adopted the law merchant. *Id.* at 845. Beutel concluded in his discussion of the development:

> Thus the merchants finally won their victory and the law merchant was brought into the law of England by statute as it had been four hundred years before the Statute of Staples. . . .
>
> The Statute of Anne, which thus formed the starting points of the new movement in the common law, has been widely copied in various forms throughout the United States, and the doctrine of broad construction of this act has made it the most important factor in the growth of the law of negotiable instruments.

Id. at 844-45.

[109] *Cf.* cases discussed in notes 114-27 *infra* and accompanying text. The practical American colonists established law merchant courts similar to those in England. W. BRITTON, *supra* note 87, at 15.

[110] *Cf.* cases discussed in notes 114-27 *infra* and accompanying text.

[111] *Id.* This has been a major theme throughout the development of commercial law and was summarized well in the observation of the nineteenth century British jurist Lord Bowen: "'Law' then 'should follow business'; it should not divert or anticipate the course of business, except for most urgent reasons." M. BIGELOW, *supra* note 87, at 7 (quoting Mogul Steamship Co. v. McGregor, 23 Q.B.D. 612 (1892)).

[112] *See* notes 31-38 *supra* and accompanying text.

[113] *E.g.*, Lee v. Dick, 35 U.S. (10 Pet.) 482 (1836); Douglass v. Reynolds, Byrne & Co., 32 U.S. (7 Pet.) 113 (1833); Drummond v. Prestman, 25 U.S. (12 Wheat.) 514 (1827); Aud v. Magruder, 10 Cal. 282 (1874); Perkins-Goodwin Co. v. Hart, 83 N.J.L. 471, 83 A. 877 (E. & A. 1912); Ligran, Inc. v. Medlawtel, Inc., 174 N.J. Super. 597, 417 A.2d 100 (App. Div. 1980); Central Jersey Bank & Trust Co. v. Lady Van Indus., Inc., 134 N.J. Super. 439, 381 A.2d 831 (Law Div. 1977); Marinelli v. Lombardi, 16 N.J. Misc. 71, 196 A. 701 (Sup. Ct. 1938); Hoey v. Jarman, 39 N.J.L. 523 (Sup. Ct. 1877).

therefore, took place before the guarantor's obligation arose. Based on such case law it is illogical to hold, as in the instant case, that the cause of action against the guarantor can accrue before a default.

In the 1833 United States Supreme Court case, *Douglass v. Reynolds, Byrne & Co.*,[114] the Court, considering the guarantor liability, held that "by the general principles of law, the guarantors are only collaterally liable upon the failure of the principal debtor to pay the debt."[115] An 1858 California case, *Aud v. Magruder*[116] also involved the maker's default. That case bears an interesting similarity to the instant case because in it, too, the court was compelled to classify the indorser's liability.[117] The California court, which held that the issue must be decided according to the law merchant, described the distinction between the maker and guarantor: "The difference between a maker and an indorser or guarantor is, that the contract of the first, *by its terms*, imports an unconditional obligation to pay money—that of the last, by its terms, imports a conditional obligation."[118] The court explained that identifying words such as "maker," "guarantor," or "surety" do not define the relationship, but rather the words and agreement of the parties control.[119] Similarly, the New Jersey Supreme Court in 1912 in *Perkins-Goodwin Co. v. Hart*[120] adopted the commonly understood definition of a guarantee as either a commitment to pay "in the given event" or "a promise to be answerable for the default of another." Clearly, the common law recognized that whether or not the guarantor's obligation is considered primary or secondary, it is at least conditioned upon the failure of the maker to fulfill his obligation.

Reflecting a fundamental law merchant precept of ensuring commercial predictability and certainty,[121] the United States Supreme Court long has stressed the importance of the intent of the parties to the instrument.[122] In 1836, the Court explained: "A guaranty is a mercantile instrument, and to be construed according to what is fairly to be presumed to have been the understanding of the parties, without any strict technical nicety."[123]

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[114] 32 U.S. (7 Pet.) 113 (1833).

[115] *Id.* at 127.

[116] 10 Cal. 282 (1874).

[117] *Id.* at 284-85.

[118] *Id.* at 290 (emphasis added).

[119] *Id.*

[120] 83 N.J.L. 471, 473, 83 A. 877, 878 (E. & A. 1912).

[121] *See* note 100 *supra* and accompanying text.

[122] *See* text accompanying notes 123 & 124 *infra*.

[123] Lee v. Dick, 35 U.S. (10 Pet.) 482, 493 (1836). A similar rule of construction is applied in the earlier Supreme Court decision in Douglass v. Reynolds, Byrne & Co., 32 U.S. (7 Pet.) 113

While the intent of the parties is central in determining their liabilities, the courts also have held that the terms of the guarantee should be accorded the meaning which most obligates the guarantor.[124] This presumption against the guarantor is reflected in an 1827 United States Supreme Court decision which declared that "[i]t is a rule, in expounding instruments of this character, 'that the words of the guarantee are to be taken as strongly against him as the sense will admit.'"[125] New Jersey courts have accepted this rule of construction; in 1877 the Supreme Court of New Jersey held that like many other written contracts, a guarantee first should be viewed as to effect the clear intent of the parties.[126] When, however, the terms of the contract of guarantee are ambiguous or unclear, then the instrument taken as a whole should be construed "'*potius contra proferentem*; that is, against the party giving the contract.'"[127]

The adoption of the N.I.L. established clear provisions for the liability of the parties to negotiable instruments.[128] Article 5 of the N.I.L. defined these obligations: that the maker engages to make payment on the instrument according to its tenor,[129] and that the indorser agrees to make payment upon due presentment or if the maker dishonors demand for payment.[130] Section 7:1-3 of the N.I.L. stated that a person is considered "primarily" liable on an instrument when the terms absolutely require his payment while "all other parties are 'secondarily' liable."[131] It is interesting that, similar to the U.C.C. which followed it, there is no definition in the N.I.L. for the term "guarantor." Professor Britton, in his treatise *Handbook of the Law of Bills and Notes*, provides some indication of the guarantor's liability under section 7:1-3: "The maker of a note and the acceptor of a bill thus become primary parties . . . and the indorser on bills, checks and notes thus become secondary parties."[132] This construction of the N.I.L. would categorize the guarantor as a secondary party to a note who is collaterally liable for payment. Professor Brannan in his treatise on the N.I.L. submitted that the weight of authority

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(1833). The court held that "[t]he whole words and clauses are to be construed together, and that sense is to be given to each, which best comports with the general scope and intent of the whole." *Id.* at 123-24.

[124] *See* text accompanying notes 125-27 *infra*.

[125] Drummond v. Prestman, 25 U.S. (12 Wheat.) 514, 518 (1827) (quoting an uncited source).

[126] *See* Hoey v. Jarman, 39 N.J.L. 523, 525-26 (Sup. Ct. 1877).

[127] *Id.* at 526 (quoting BURGE, SURETYSHIP 46 (1847)).

[128] N.J. REV. STAT. §§ 7:2-60 to 7:2-69.

[129] *Id.* § 7:2-60.

[130] *Id.* § 7:2-66.

[131] *Id.* § 7:1-3.

[132] W. BRITTON, *supra* note 87, at 778.

considered a guarantee of payment with waiver of presentment as an indorsement.[133]

In summary there are clear and persistent principles for the adjudication of commercial instrument disputes which run throughout the development of the law merchant, common law, and uniform statutes. Commercial certainty and predictability have consistently been favored, leading to a marked tendency to support the intent of the parties where ambiguity arises. Common law further construes the guarantor's liability most strictly against him. The endurance of these principles is due to the fact that they are founded upon long-established and accepted modes of commercial intercourse which succeeded in facilitating trade. It would ill-serve commerce to tamper with a scheme which has enjoyed hundreds of years of successful practice. The appellate division may have done just that.

III. Critique of Court's Decision

The court's decision was a narrow and lenient reading of guarantor liability because it effectively eliminated her obligation to the holder of the note.[134] To reach its conclusion, the court defined the guarantor as a comaker and considered her guarantee "surplusage" to her contract as maker on the note.[135] In so holding, the court did not apply the clear meaning of indorser liability under section 3-122, misapplied and upset the section 3-416, "Contract of Guarantor," scheme of guarantor liability, and otherwise dismissed the intent and equities of the parties.

It is submitted that a purposive reading of section 3-122 shows that the indorser accrual provision of the section[136] subsumes a guarantor. The fact that the section specifically delineates the liabilities of many classes of parties to instruments,[137] but omitted the term "guarantor," raises a presumption that the drafters' omission was deliberate[138] and that a "guarantor" should be treated like any other

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[133] J. Brannan, The Negotiable Instruments Law Annotated, § 31 at 425 (5th ed.).

[134] Ligran, 174 N.J. Super. at 598-99, 417 A.2d at 100.

[135] *See* notes 68 & 71 *supra* and accompanying text.

[136] For the text of section 3-122(3), the indorser accrual provision, see note 26 *supra*.

[137] *See* notes 24-27 *supra*.

[138] This conclusion accords with the express mention and implied exclusion canon of statutory construction as articulated in 82 C.J.S. *Statutes* § 333 at 666-68 (1953):

> [W]here a statute enumerates the subjects or things on which it is to operate, or the persons affected, or forbids certain things, it is to be construed as excluding from its effect all those not expressly mentioned . . . the specification of one particular class excludes all other classes.

Id.

The fact that the Code writers did not even *refer* to the section 3-416, "Contract of Guarantor," further supports this statutory construction.

indorser for that section. To do otherwise disregards both the legal and common understanding that the term "indorser" includes any party who endorses the back of the note.[139] Furthermore, while there is no mention of the term "guarantor" in either the New Jersey or Uniform Commercial Code Comment, there is express delineation of the "indorser" obligation both in the section 3-122(3) and an accompanying U.C.C. Comment.[140] In particular, U.C.C. Comment 1 to the section provides in pertinent part:

> As to . . . *all* indorsers, the cause of action accrues, in conformity with their underlying contract on the instrument, (Sections 3-413 and 3-414), only upon demand made, typically in the form of a notice of dishonor, after the instrument has been presented to and dishonored by the person designated on the instrument to pay it.[141]

It is significant that the drafters declared that "all" indorsers are subject to the section's rules for accrual of a cause of action against that class of party. One of the introductory comments to New Jersey's Article 3 employs language similar to that of U.C.C. Comment 1 to section 3-122: "Secondary parties, the drawer of a draft or a check and *all* endorsers, under the Code as under the N.I.L., are persons to whose liability there are conditions precedent."[142] Nor does section 3-122 contain any cross-references to section 3-416, "Contract of Guarantor," upon which the defendant relied so heavily.[143] Both New Jersey and U.C.C. comments, however, refer the reader to sections involving the indorser's obligations and liabilities.[144] It is a reasonable conclusion, therefore, that the careful inclusion in section 3-122 of various parties' liabilities, including the indorser's, implies that the term "guarantor" was intended to be considered an indorser for these purposes.

Alternatively, even if section 3-122 is considered ambiguous concerning guarantor liability, the court should not have departed from the common law principle that the guarantor's liability should be construed most strongly against him.[145]

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[139] BLACK'S LAW DICTIONARY 597 (5th ed. 1979). The term "indorser" is defined as:

> He who indorses; i.e., being the payee or holder, writes his name on the back of a negotiable instrument. One who signs his name as payee on the back of a check to obtain the cash or credit represented on its face.

Id.

[140] U.C.C. § 3-122(3), Comment 1. New Jersey adopted this comment in full in N.J. STAT. ANN. § 12A:3-122 (3), Comment 1.

[141] U.C.C. § 3-122(3), Comment 1 (emphasis added).

[142] N.J. STAT. ANN. § 12A, Introductory Commentary, & Endorsements (e) (emphasis added).

[143] *See* text accompanying notes 49-52 *supra*.

[144] U.C.C. § 3-122; N.J. STAT. ANN. § 12A:3-122.

[145] *See* text accompanying notes 124-27 *supra*.

It is further submitted that the court incorrectly concluded that section 3-416 applied to the instant case. The defendant, who relied heavily upon section 3-416, cited 3-416(1) as the pertinent clause, which provides:

> "Payment guaranteed" or equivalent words added to a signature mean that the signer engages that if the instrument is not paid *when due* he will pay it according to its tenor without resort by the holder to any other party.[146]

By definition, a demand note has no specific due date;[147] therefore, it would appear that this section, which refers to time instruments with fixed maturities, *e.g.*, "when due," cannot apply in the section 3-122 context of a demand note.

Even if it be concluded that it applies to the instant case, section 3-416 should not be utilized to *relieve* the defendant of liability because such an interpretation contradicts the obvious purpose of the section to *create* liability.[148] The entire sense of section 3-416 is to assure that the guarantor liability exists when there is any cause for doubt.[149] Section 3-416 distinguishes between the liability created by terms such as "payment guaranteed"[150] and "collection guaranteed."[151] Section 3-416(1) provides:

> "Payment guaranteed" or equivalent words added to a signature mean that the signer engages that if the instrument is not paid when due he will pay it according to its tenor without resort by the holder to any other party.[152]

The clear meaning of section 3-416(1) is to provide the holder the greatest protection and to impose upon the guarantor the greatest liability as an indorser. Section 3-416(2), however, provides a lesser degree of holder protection and guarantor liability:

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[146] N.J. STAT. ANN. § 12A:3-416(1) (emphasis added).

[147] N.J. STAT. ANN. § 12A:3-108. This section provides: "Instruments payable on demand include those payable at sight or on presentation and those in which no time for payment is stated." *Id.*

[148] R. ANDERSON, *supra* note 83, § 3-416:3. Anderson explains that one of the purposes of section 3-416 is to enlarge and further specify the guarantor's liability:

> Code § 3-416 expands the area of statutory regulation of commercial paper to declare the effect, and the meaning of a guaranty of payment and of a guaranty of collection. The section is another of the Code's provisions which define the liabilities of the various parties to a negotiable instrument.

Id.

[149] N.J. STAT. ANN. § 12A:3-416. For example, section 3-416(3) provides: "Words of guaranty which do not otherwise specify guaranty payment." N.J. STAT. ANN. § 12A:3-413(3). The other clauses either create or presume liability. *Id.*

[150] N.J. STAT. ANN. § 12A:3-416(1).

[151] *Id.* § 12A:3-416(2).

[152] *Id.* § 12A:3-416(1).

> "Collection guaranteed" or equivalent words added to a signature mean that the signer engages that if the instrument is not paid when due he will pay it according to its tenor, but only after the holder has reduced the claim against the maker or acceptor to judgment and execution has been returned unsatisfied or after the maker or acceptor has become insolvent or it is otherwise apparent that it is useless to proceed against him.[153]

Though the clear intention of section 3-416(1) is to ensure that the holder obtain the greatest protection a guarantee may provide, the court inappropriately applied it to relieve the guarantor of liability.[154] Yet had the holder required the defendant to guarantee "collection," the court would have been forced to apply section 3-416(2). Under this section the defendant would not have been relieved of liability because the accrual of the cause of action would have commenced with dishonor of payment, and the action thereby would have fallen within the statutory period.[155] Applying the court's reasoning the holder of any note is placed in a paradoxical dilemma. If he requires the indorser to sign as guarantor of payment, he could well find himself statutorily barred from bringing action. If he chooses to require the indorser to sign as guarantor of collection, he would not be statutorily barred, but he first would have to sue the maker. For purposes of the statute of limitations, the normally lesser protection of "collection guaranteed" would afford the holder greater protection, and the normally greater protection of "payment guaranteed" would afford the holder lesser protection. The court effectively has turned the section 3-416 scheme upside down.

A close reading of the Code purposes similarly leads to the conclusion that the action of the *Ligran* court was improvident. To lend guidance for judicial interpretation of the Code, the drafters delineated purposes and rules of construction in section 1-102.[156] This

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[153] *Id.* § 12A:3-416(2).

[154] Ligran, 174 N.J. Super. at 600-02, 417 A.2d at 101-02.

[155] N.J. STAT. ANN. § 12A:3-416(2). *See* text accompanying note 153 *supra*. New Jersey Code comments support the extension of the court's reasoning in this manner: "A guarantor of collectibility also waivers formal presentment, notice of dishonor and protest, but the holder must first proceed against the primary party or show that such a proceeding would be useless, before turning to the guarantor." N.J. STAT. ANN. § 12A:3-416, New Jersey Study Comment. Anderson gives further evidence that the court's reasoning would require continuing liability should the guarantor be within section 3-416(2): "'Collection guaranteed' or similar words added to the signature of a party to a negotiable instrument imposes upon the signer a *secondary liability* for the payment of the instrument." R. ANDERSON, *supra* note 83, § 3-416.9 (emphasis added). Since the guarantor's liability is secondary, the section 3-122(3) provision clearly would have applied to set the accrual of the cause of action at the time demand for payment was dishonored. The statutory bar would not have occurred.

[156] N.J. STAT. ANN. § 12A:1-102.

section provided for liberal construction to effectuate the purposes and policies of the Code which include the encouragement of commercial growth.[157] This legislative articulation is consistent with the law merchant and common law precept that the law should facilitate commerce.[158] Certainly, one of the goals of the commercial law is to provide business with certainty and predictability.[159] It would seem illogical, therefore, for the court to upset the accepted and commonly understood concept of a guarantor in commercial usage as a party whose liability arises only upon the maker's default.[160] By classifying the guarantor as a maker rather than an indorser, the court has redefined the term and discarded the obvious application of the indorser clause.[161] It ill suits the course of commerce when a court deprives business of its understanding and expectation of a word's meaning. Such a court determination violates the principle of judicial construction which requires that a word should be accorded its plain and common meaning.[162]

In addition to disregarding commercial usage, the court's equation of the guarantor obligation with the maker of the note defeats the obvious intent of the parties. It is generally accepted that the intent of the parties in a commercial transaction should be effectuated.[163] The principle is also suggested in section 1-102.[164] In the instant case the defendant, in her capacity as guarantor, signed the guarantee clause on the back of the note in order to induce the plaintiff to execute the note and underlying lease agreement.[165] The

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[157] *Id.* *See* note 164 *infra.*

[158] *See* notes 91 & 111 *supra* and accompanying text.

[159] *See* notes 101 & 111 *supra* and accompanying text.

[160] *See* notes 113-20 *supra* and accompanying text.

[161] *See* notes 136-42 *supra* and accompanying text.

[162] *See, e.g.*, 82 C.J.S. *Statutes* § 316 at 549 (1953).

[163] *See* notes 122-23 *supra* and accompanying text.

[164] N.J. STAT. ANN. § 12A:1-102, which applies to the entire Code, provides in pertinent part:

> (1) This Act shall be liberally construed and applied to promote its underlying purposes and policies.
>
> (2) Underlying purposes and policies of this Act are . . . (b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties.

Id. Also commenting on the objectives of the Code as a guide to construction, Anderson states in pertinent part:

> The Uniform Commercial Code was designed to bring the body of commercial law into line with the contemporary world of business. It was written in terms of current commercial practices, to meet the contemporary needs of a fast moving commercial society and to advance fair dealing.

R. ANDERSON, *supra* note 83, § 1-102:7.

[165] *See* notes 3-9 *supra* and accompanying text. Plaintiff noted in the Petition for Certification that:

> In the case at bar, defendant Elizabeth Butkus knew full well that she was signing a note as a maker thereof, and then signing a separate individual contract to guaran-

clear intent of the parties, therefore, was to create a contract to guarantee payment. Despite the obvious and intended import of the agreement, the court dismissed the defendant's guarantee as mere "surplusage."[166] The court rejected the concept that one person may serve in two or more capacities within the same agreement[167] and thereby overruled prior New Jersey holdings.[168]

The court, through its construction of the Code, effectively rewrote the note, redefined the parties' obligations under the Code, and overruled the intent of the contracting parties. In so doing the court deprived the holder of the note of his reasonable expectation of reliance on the defendant's guarantee.[169]

Though plaintiff should have prevailed on a statutory basis, equitable considerations dictate the same result. It was error, it is submitted, to refuse to even consider plaintiff's equitable claims.[170]

> tee the payment of the note should it have become necessary; the note, which she well knew, was to be used to secure or guarantee performance of a lease by the corporation in which she was a principal. . . . From the transcript, it is obvious that the plaintiff would never have agreed to execute the lease in this case without the appropriate guarantees. The note was signed as an inducement to plaintiff to become the lessor of the defendant.

Plaintiff's Petition for Certification at 7. Although contending that the act was a mere "formality," the defendant admitted to endorsing the note on the back following the words of guarantee. Defendant's Brief at 5-6. It is an ineffective argument for the defendant to suggest that as a "formality," she did not intend a separate contract of guarantee. *See* WILLISTON ON CONTRACTS § 610 at 1177 (1920). "In effect, therefore, it is not the real intent but the intent expressed or apparent in the writing which is sought." *Id.* According to Anderson the intent of the contracting parties concerning the guarantor's liability will continue to control the application of section 3-416.

> Whether there is a guarantee and whether it is a guarantee of collection or of payment, is a question of the intent of the parties. This intent is determined by the same standards as for any other contractual undertaking, that is, in accordance with the general principles of contract law which have not been displaced and therefore continue under the Code.

R. ANDERSON, *supra* note 83, § 3-416:4.

[166] Ligran, 174 N.J. Super. at 601, 417 A.2d at 102.

[167] *Id.*

[168] In *Lady Van* the court stated: "Nothing in the Code appears to preclude a person from being both an indorser and a guarantor." 154 N.J. Super. at 461-62, 381 A.2d at 832. Also, the Supreme Court of New Jersey in Newark Finance Corp. v. Acocella, 115 N.J.L. 388, 180 A. 862 (Sup. Ct. 1935), stated:

> The same person may be a guarantor and also an endorser of a note; and in such case, while failure to give him due notice of demand and non-payment will discharge him as an endorser, he will still be bound as guarantor.

Id. at 395, 180 A. at 865.

[169] *See* notes 192 & 195-205 *infra* and accompanying text.

[170] *See* text accompanying notes 72-76 *supra*.

The parties did not dispute that the general six year limitation for bringing a contract action applied.[171] Plaintiff, however, argued alternatively to the statutory (U.C.C.) basis for judgment, that on equitable considerations the court should have estopped the defendant from invoking the statutory bar.[172]

A statute of limitations is designed to bar stale or fraudulent claims and to promote timely and diligent actions.[173] Courts rarely hesitate to enforce a statutory bar even against claims with merit.[174] On the other hand, courts are expected to adhere to the general rules of statutory construction in applying a bar and avoid extending the bar to actions not within the statute.[175] It seems clear, then, that when there is doubt whether the statute of limitations applies in a particular controversy, it should not be applied.[176]

From the single standpoint of statutory construction, the *Ligran* court should have refrained from barring plaintiff's action in light of the considerable doubt whether section 3-122(1) applied to the defendant as guarantor of payment. Such judicial restraint would be particularly appropriate since the *Lady Van* court, which considered the same question, ruled that the guarantor could *not* invoke the section 3-122 bar.[177] Consistent with due process, it would seem that the

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[171] *See* text accompanying notes 18-19 *supra*. The applicable statutory bar provides in pertinent part: "Every action at law . . . for recovery upon a contractual claim or liability, express or implied, not under seal . . . shall be commenced within 6 years next after the cause of action shall have accrued." N.J. STAT. ANN. § 2A:14-1.

[172] *See* notes 43-47 *supra* and accompanying text.

[173] *See, e.g.*, 53 C.J.S. *Limitations of Actions* § 1 at 902-03 (1948).

> [T]he basic principle most generally relied on by the authorities is that statutes of limitations are statutes of repose, the object of which is to suppress fraudulent and stale claims from springing up at great distances of time and surprising the parties or their representatives when all the proper vouchers and evidences are lost or the facts have become obscure from the lapse of time or the defective memory or death, or removal of witnesses.

Id.

[174] *See, e.g.*, 53 C.J.S. *Limitations of Actions* § 1 at 903 (1948). "Such statutes apply with full force to the most meritorious claims." *Id.*

[175] *See, e.g.*, 53 C.J.S. *Limitations of Actions* § 3 at 912-13 (1948). "[I]t is a familiar principle that a statute of limitations should not be applied to cases not clearly within its provisions; it should not be extended by construction." *Id.*

[176] *Id. See* 51 Am. Jur. 2d *Limitations of Actions* § 50 at 630-31 (1970).

[177] Lady Van, 154 N.J. Super. at 463, 381 A.2d at 833. The court held:

> The application of the statute of limitations as urged by defendant would narrow the responsibility of a guarantor so that it would not be co-extensive with the liability of the maker or that of an indorser. . . . Such application would also mean that a guarantor invariably would not also be subject to the obligations of the Code pertaining to indorsers, whereas the common sense reading of the Code is to the contrary.

Id.

plaintiff was entitled to rely on the prior judicial interpretation of the statute.[178] This conclusion is further supported by the fact that plaintiff promptly brought suit after it believed its cause of action arose.[179] It is a settled principle that one cannot bring action prior to the accrual of the cause.[180] Thus it is clear that the plaintiff acted in a timely and expeditious fashion. This was not the type of stale or fraudulent claim which the statute is intended to exclude. Nor was the defendant prejudiced. For these reasons of statutory construction, the court should not have invoked the bar.[181]

New Jersey courts recently have become more willing to consider equitable considerations and legislative purpose before mechanistically applying the statute of limitations. Such considerations have developed into the "discovery rule" in which a plaintiff may be relieved of the harsh effects of the statutory bar where he neither knew nor had reason to know that he had a basis for a claim until the statutory period expired.[182] In her reply brief to the plaintiff's petition for supreme court certification, the defendant asserted that

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[178] This would seem particularly true since the *Lady Van* decision, like the instant case, involved: a guarantor who signed on the reverse side of a demand promissory note below a notice of guarantee like the instant one; a court's examination of sections 3-122 and 3-416; and a court's express rejection of the applicability of section 3-416 to 3-122. Plaintiff's reliance on *Lady Van* should be assumed on a "notice" basis. It is ironic that defendant declared: "It would be extremely prejudical to the defendant to say to her that her reliance on the law was misplaced." Defendant's Reply Brief at 4. This assertion that the party should not be deprived of reliance on the law is precisely the reason the court should have permitted the plaintiff's reliance on *Lady Van*.

It is a settled principle that the court should not apply the statute of limitations retroactively. *See, e.g.*, 53 C.J.S. *Limitations of Actions* § 4 at 913 (1948): "Under the fundamental rule for the construction of statutes, statutes of limitations ordinarily will not be given a retroactive effect unless it clearly appears that the legislature so intended. . . ." *Id.* (citations omitted). In effect, the court's ruling in the instant case is retroactive.

[179] *See* notes 182-94 *infra* and accompanying text. Plaintiff could not have brought suit until the maker's default, since there would have been no matter in controversy.

[180] 54 C.J.S. *Limitations of Actions* § 108 at 9 (1948). "The general rule . . . is that, unless a statute specifically provides otherwise, the statute of limitations begins to run at the time when a complete cause or right of action accrues or arises. . . ." *Id.*

[181] The fact that the court may have disagreed with the *Lady Van* decision does not justify the negation of plaintiff's reliance upon that ruling. If the court wished to overturn *Lady Van*, it might have applied the ruling prospectively to avoid prejudicing the plaintiff.

[182] An oft-cited case articulating the principle is Farrell v. Votator Div. of Chemetron Corp., 62 N.J. 111, 299 A.2d 394 (1973). In that case, involving a personal injury against a machine manufacturer, the Supreme Court of New Jersey declared:

> Where . . . the plaintiff does not know or have reason to know that he has a cause of action against an identifiable defendant until after the normal period of limitations has expired, the considerations of individual justice and the considerations of repose are in conflict and other factors may fairly be brought into play.

Id. at 115, 299 A.2d at 396.

application of the discovery rule has been restricted to personal injury claims.[183] This is incorrect, as New Jersey courts have applied the rule to a variety of cases including actions involving unfair labor practices,[184] recovery on a contract,[185] and property damage.[186] Indeed, the Supreme Court of New Jersey ruled over eight years ago that the rule may be appropriate "in varying situations and has been receiving ever increasing support elsewhere."[187]

There are several reasons why the facts of the instant case compel the application of the discovery rule. In light of a common sense reading of section 3-122,[188] there was no reason for the plaintiff to know or suspect that the cause of action accrued against the guarantor upon the date of the making of the note.[189] The plaintiff did not sleep on its claim, but pursued it promptly.[190] The purpose of the statute is best served by the court's refraining from invoking it.[191] The plaintiff had an equitable right to rely upon the contract of guarantee.[192] Finally, the defendant would not have been prejudiced since there is no indication that the delay in time would have resulted in loss of evidence, damage to defendant's ability to defend, or advantage to plaintiff.[193] As the Supreme Court of New Jersey declared in *Farrell v. Votator Division of Chemetron Corp.*:

> Justice impels strongly towards affording the plaintiffs their day in court on the merits of their claim; and the absence of prejudice, reliance or unjustifiable delay, strengthens the conclusion that this may fairly be done in the matter at hand "without any undue impairment of the (statute of limitations) or the considerations of repose which underlie it."[194]

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[183] Defendant's Reply Brief at 2.

[184] Kaczmarek v. New Jersey Turnpike Auth., 77 N.J. 329, 390 A.2d 597 (1978).

[185] Board of Educ., Asbury Park v. Hoek, 38 N.J. 213, 183 A.2d 633 (1962).

[186] Diamond v. New Jersey Bell Tel. Co., 51 N.J. 594, 242 A.2d 622 (1968).

[187] Farrell v. Votator Div. of Chemetron Corp., 62 N.J. 111, 116, 299 A.2d 394, 396 (1973) (citations omitted). The case was decided on January 22, 1973.

[188] *See* notes 136-44 *supra* and accompanying text.

[189] The plaintiff had no reason to know, particularly since the *Lady Van* court ruled that the cause of action did not exist from time of making. Thus, the exercise of the attorney's vigilance would not have resulted in knowledge of the existence of a cause of action. If the court had considered and rejected application of the discovery rule, it would have required the plaintiff to foretell the court's decision.

[190] *See* note 179 *supra* and accompanying text.

[191] *See* notes 173-81 *supra* and accompanying text.

[192] *See* notes 195-205 *infra* and accompanying text.

[193] This is particularly true since the parties agreed and the court concluded that the facts were essentially undisputed.

[194] 62 N.J. 111, 122-23, 299 A.2d 394, 400 (1973) (citations omitted).

The terms, both express and implied, of the note's underlying obligation should be considered. There was no dispute that defendant signed the note as maker and guarantor in order to provide a replacement for a cash security deposit on a lease agreement with the plaintiff.[195] It is irrelevant, as the defendant asserted,[196] that the note did not specifically refer to the lease. The reference was implicit, since the very purpose of the note was to secure the lease. The court should have considered the underlying obligation of the note. In fact, section 3-119, "Other Writings Affecting Instrument," provides in pertinent part:

> (1) As between the obligor and his immediate obligee or any transferee the terms of an instrument may be modified or affected by any other written agreement executed as a part of the same transaction.[197]

Here the note and the lease were inseparable obligations, since the plaintiff would not have agreed to the lease without the note.[198] Since the lease and note were part of the same transaction, they should be considered together. The U.C.C. commentary to section 3-119 explains that the section employs the settled rule that "writings executed as a part of the same transaction are to be read together as a single instrument."[199] The comment writers further noted that "a note may be affected by . . . any other relevant term in the separate writing."[200] A major term in the separate writing (the lease) to the note in this case is its five year term with an option to renew.[201] This term should be considered together with the defendant's guarantee to waive "any and all extensions of time or terms of payment made by holder of said note."[202] The guarantor effectively agreed that the due date of the renewed lease, ten years after the original date of the note, would waive the six year statute of limitations on the note.[203] It is well-settled that the waiver can be effectuated by words or

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[195] *See* text accompanying notes 3-9 *supra*.
[196] *See* note 6 *supra*.
[197] N.J. STAT. ANN. § 12A:3-119.
[198] Petition for Certification at 7-8.
[199] U.C.C. § 3-119, Comment 3.
[200] *Id.*
[201] *See* text accompanying note 4 *supra*.
[202] *See* text accompanying note 9 *supra*.
[203] *See* notes 46-47 *supra* and accompanying text.

conduct.[204] Here the defendant *both* as maker and guarantor waived the statutory bar by the terms of the lease.[205]

The conduct of the defendant in paying rent on the lease is evidence of acknowledgment of the debt on the note. Since the two documents should be read together as one contractual obligation,[206] the acknowledgment of the debt tolled the statute. It is generally accepted that acknowledgment or admission of the debt, as evidenced here by payment of rent, lifts the statutory bar because it implies a commitment to fulfill the terms of the debt.[207] Thus the defendant's express agreement and conduct tolled the statute.

CONCLUSION

The exigencies of modern business require that a person be entitled to rely on a settled and accepted understanding of another's contractual obligation. It ill-serves commerce to upset these practices and impose an unusual and novel construction of an old commercial term. Such a decision creates uncertainty—a bane to commercial intercourse. We agree with the court's observation in *Lady Van* that the ruling would "create added burden to commercial transactions."[208]

We see no reason why the court should impose needlessly complex and costly steps which this decision would require. It is illogical, in light of the Code purpose to encourage commercial development, that the term "guarantor" would be rendered a nullity, that the intent of the parties would be overthrown, and that common law expectations would be discarded.

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[204] *See, e.g.*, 53 C.J.S. *Limitations of Actions* § 24 at 958-60 (1948).

> Since a statute limiting the time within which actions shall be brought is for the benefit and repose of individuals and not to secure general objects of policy or morals, and it is regarded as a personal privilege, it is a general rule that the protection may be waived by one entitled to rely on it. . . . Waiver of Limitations may be shown by words or conduct.

Id.

[205] Defendant's lease obligations clearly extended throughout the renewal periods. Plaintiff did not recover the premises until June 1975. Ligran, 174 N.J. Super. at 599, 417 A.2d at 101.

[206] *See* notes 195-205 *supra* and accompanying text.

[207] *See, e.g.*, 54 C.J.S. *Limitations of Actions* § 321 at 423-25 (1948). "The principle or theory on which part payment removes the bar of the statute is that the payment is an acknowledgment or admission of the existence of the indebtedness, which raises an implied promise to pay the balance. . . ." *Id.*

[208] Lady Van, 154 N.J. Super. at 463, 381 A.2d at 833.