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The History and Economics of Suretyship*

BY WILLIS D. MORGAN†

EARLY HISTORY OF THE CONTRACT OF SURETYSHIP

The contract of suretyship antedates the Christian era by more than 2500 years.¹ The Library of Sargon I, king of Accad and Sumer (*circa* 2750 B. C.) contains a tablet which records the making of such a contract. This contract, although made nearly 4700 years ago, contains features which are strikingly modern. A farmer, who resided in the suburbs of Accad, had been drafted into the military service of the king. He entered into a contract with a second farmer by the terms of which the latter agreed to cultivate the soldier's farm for the period of his absence. He also agreed to fertilize the land properly and to maintain the property and return it to the owner upon the expiration of the lease, in as good condition generally as when received by him. The lessee, in return, was to receive one-half of the produce from the farm. The owner, of course, would be in no position to personally supervise the performance of the contract by his lessee, and, in order that he might be properly secured, the tablet states that a merchant of the city of Accad, as a surety for the lessee, guaranteed the performance of this contract by him.²

But contracts of suretyship were probably in common use long prior to the reign of Sargon I. The code of Hammurabi (*circa* 2250 B. C.), enacted only 500 years after the time of Sargon I, provided for a system of state fidelity insurance which belonged rather to the 19th century than to the year 2250 B. C. Sections 22 and 23 of this code read:

*This article will appear in the CORNELL LAW QUARTERLY in two installments. The first installment, which appears herein, covers the history of the contract of suretyship from the year 2750 B. C. to 1720 and that of the corporate surety from 1720 to 1875. The second installment will continue the history of the corporate surety to date and will discuss the social and economic significance of the corporate surety.

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¹STORY, CONTRACTS, (2d Ed. 1874) p. 319, note 1; William H. Lloyd, *The Surety* (1918) 66 U. PA. L. REV., 40; Earl C. Arnold, *The Compensated Surety* (1926) 26 COL. L. REV. 171.

²See Jarvis W. Mason, *Radio Talks*, Season 1923-1924, p. 5; Jarvis W. Mason, *Origin and History of Suretyship*, p. 4. This tablet was not a memorandum of the agreement. The names of the parties, if such were the case, would have been set out. Mr. Mason, in both these pamphlets, mentions another contract from the same source and period.

22. "If a man has committed highway robbery and has been caught, that man shall be put to death."³

23. "If the brigand be not captured, the man who has been robbed shall, in the presence of God make an itemized statement of his loss, and the city and the governor, in whose province and jurisdiction the robbery was committed, shall compensate him for whatever was lost."⁴

Under this latter section, the city and the governor were placed in the position of a surety. But more than this, the section applies the insurance principle to contracts of suretyship; it substitutes group responsibility for individual responsibility. The city insured the fidelity of any person who came within its jurisdiction and, in turn, every person who came within the jurisdiction of the city was insured against the dishonesty of others. The persons who would benefit most directly from this legislation, however, would be the inhabitants of the city and, to meet the expenses incident to acting in this new capacity, the city would be forced to increase its taxes. The persons who would bear this burden of taxation would also be, we assume, the inhabitants of the city. If, in the kingdom of Hammurabi, taxes on property were apportioned according to the total value of the property owned by each individual, (and this is not improbable) the beneficiaries of this state insurance may be said to have paid a premium, in the form of a tax, the computation of which rested upon a substantial scientific basis—the amount of property protected against embezzlement or theft. But whether or not this was the case, it is evident that under this section of the code of Hammurabi the city performed functions which are analogous to those now performed by the corporate surety. The surety company, a product of the 19th century, had been anticipated by more than 4000 years.

The contract of suretyship is usually an instrument of trade. By section 32 of this code, however, it was made to serve the purposes of war. This section provides:

"If such an official has been assigned to the king's service (and captured by the enemy) and has been ransomed by a merchant and helped to regain his city, if he has had means in his house to pay his ransom, he himself shall do so. If he has not had means of his own, he shall be ransomed by the temple treasury (that is, the temple treasury shall reimburse the merchant).⁵ If there has not been means in the temple treasury of his city,

³C. H. W. JOHNS, *BABYLONIAN AND ASSYRIAN LAWS, CONTRACTS AND LETTERS* (Library of Ancient Inscriptions) 46. For a history of this inscription see page 5 of the above.

⁴BOTSFORD, *SOURCE BOOK OF ANCIENT HISTORY*, 29.

⁵Writer's insertion.

the state will ransom him."⁶ (that is, the state will reimburse the merchant).

Under this section, the temple treasury of the city, as surety for the official, was subject to all the duties of a surety, and the state, as a surety for the temple treasury, was also subject to those duties. It should be observed, however, that the temple treasury and the state were both denied an important right of the surety. Under this section, the official was relieved of all liability if he had no means of payment. The very contingency, upon the happening of which the temple treasury would be called upon to pay, terminated the liability of the official. The temple treasury, therefore, would not be in a position to demand recoupment from a principal who, by the express provision of the section, was not primarily liable. Thus the very important right of the surety, that of reimbursement, was denied to the temple treasury. Likewise, this right was denied the state. In all other respects, however, both the temple treasury and the state were in the position of a surety.

It is a justifiable inference that the common use of contracts of suretyship over many preceding centuries was the basis of and the inspiration for such legislation.

If we are to give credence to the Greek historian Herodotus, who is not always to be relied upon, the surety played an important role in the Babylonian marriage. Every year the maidens of marriageable age were assembled in the market place to be sold into marriage by a crier. He first selected the most beautiful maiden of the group and sold her to the highest bidder. He then selected the next in beauty and disposed of her in like manner. This procedure was continued until the quality of the group had so far deteriorated that the most beautiful of those remaining unsold would not draw a bid. She was then sold to the man who demanded the least dowry as a condition to taking her as his wife. In this way all of the crippled and the ugly were disposed of, their dowries being paid out of the proceeds from the sale of their more favored sisters. But whether she was beautiful and without dowry or ugly or crippled and commanding a large dowry, "No man," says the historian, "could take away the woman whom he had purchased without first producing a surety that he would make her his wife."⁷ Even our modern surety company, with its 500 odd varieties of bonds, cannot boast of a bond of this nature.

The fact that no written contracts of suretyship are to be found executed prior to 670 B. C., leads to the belief that such contracts

⁶C. H. W. JOHNS, *BABYLONIAN AND ASSYRIAN LAWS, CONTRACTS AND LETTERS* (Library of Ancient Inscriptions) 47.

⁷Herodotus Vol. I, 196.

weré, until that time, merely verbal undertakings.⁸ By the year 670 B. C., however, the practice of executing written contracts of this nature had at least been initiated. The British Museum collection of Cuneiform texts contains a tablet which is the oldest written contract of suretyship of which we have record. This document first recites that a loan of silver had been made by one *Silim Ašur* to *Pudu-Pīati*. It then adds, "*Mīnuhdi-ana-ili* shall pay the silver to *Silim-Ašur* if *Pudu-Pīati* does not pay it."⁹ That is, *Mīnuhdi-ana-ili* became surety for *Pudu-Pīati*. This document was executed in the year 670 B. C., and in the presence of four witnesses.

A second written contract of suretyship, dated the 8th of March-ésvan in the 40th year of the reign of Nebuchadnezzar (November 8, 564 B. C.), was recovered by the Third Babylonian Expedition of the University of Pennsylvania in 1893. This document reads in part as follows: "On the 5th of Kislev, *Ardu-Ninib* * * * shall bring *Nabi-Ellil* * * * *Shum-ukēn* * * * and *Shamash-ahē-iddina* * * * to the house of *Nergal-iddina* * * * together with the document which *Nergal-iddina* took out against *Nābi-Ellil*, *Shum-ukēn* and *Shamash-ahē-iddina*. They shall perform the transaction for the benefit of *Nergal-iddina*. *Ardu-Ninib* * * * hath sworn that, according to the agreement, we will come on the 5th of Kislev, and the transaction for the benefit of *Nergal-iddina* we will perform." The names of three witnesses are inserted at this point. The tablet then reads, "If he does not bring (them), everything, according to the document which (has been taken out) against *Nabi-Ellil*, *Shum-ukēn* and *Shamash-ahē-iddina* he shall make good; *Ardu-Ninib* shall pay in full."¹⁰ The name of a fourth witness is then added.

This contract, if literally construed, is somewhat similar to a modern bail bond. Under it *Ardu-Ninib* guaranteed the appearance of three principals at a certain time and place, and contracted that, in the event of their failure to appear, he would pay a sum certain—the amount owed the creditor by these three principals. But apparently the appearance of the principals was identical with performance, that is, the instrument was not a guaranty of their appearance but a guaranty of payment by them.

The practice of giving hostages was a common form of suretyship

⁸The Hebrews entered into such contracts by striking hands in the presence of friends; that is, it was an oral undertaking made in the presence of witnesses. Proverbs 17:18; Job 17:3.

⁹C. H. W. JOHNS, ASSYRIAN DEEDS AND DOCUMENTS, Tablet No. 99 in Vol. I, translated in Vol. 3 at p. 165.

¹⁰Babylonian Expedition of the University of Penn. Series A, Vol. 8, Pt. 1, Assyrian, Neo-Babylonian and Persian Records, Translations of Selected Texts by Albert Tobias Clay, Text No. 25, p. 22.

among the Ancients. An instance of this is recorded in the Old Testament. Ten of Jacob's sons had sold their brother Joseph as a slave to the Ishmaelites, who took him to Egypt where, some thirteen years later, as a result of his interpretation of a dream of the Pharaoh, he was appointed governor. Seven years later, a famine swept over the land of Canaan and the ten brothers who had sold Joseph into slavery went into Egypt to buy grain. When they were brought before Joseph, he recognized them immediately but because of his foreign dress and manners they did not recognize him. His brother Benjamin, who had not participated in his sale and of whom Joseph was very fond, had not accompanied his brothers to Egypt. Joseph wished to see him and accordingly demanded that his brothers, immediately upon their reaching the land of Canaan, return to Egypt and bring Benjamin with them. This they promised to do and Simeon, one of their number, remained in Egypt as a hostage and as a surety for his brothers in respect of this promise.¹¹

In the Book of Proverbs are to be found such pithy remarks as, "He that is surety for a stranger shall smart *for it*; and he that hateth suretyship is sure;"¹² "A man void of understanding striketh hands, *and* becometh surety in the presence of his friend,"¹³ and "Be not thou *one* of them that strike hands, *or* of them that are sureties for debts."¹⁴ These bits of wisdom evidence an extensive use of the contract of suretyship among the Hebrews of the time of King Solomon; such an extensive use, in fact, that the king deemed it necessary to warn against its dangers.¹⁵

The Persians, like the Assyrians, borrowed their civilization from the Babylonians. It is, therefore, not surprising to find abundant evidence of the use of the contract of suretyship in the empire of Cyrus and Darius. The Third Babylonian Expedition of the University of Pennsylvania recovered three contracts of this nature at the site of Susa, the ancient capital of the Persians. The oldest of these is dated the 8th of Nisan in the 6th year of Cyrus (April 8, 552 B.C.).

¹¹Genesis 37, 39, 41, 42; The familiar story of Damon and Pythias, the subject of the play by that name, written by Richard Edwards about 1550, is a similar instance of suretyship. See Henrietta Gerwig, *Handbook for Readers and Writers*, 177; Jarvis W. Mason, *Radio Talks*, Season 1923-1924, p. 6; *Origin and History of Suretyship*, pp. 4, 5.

¹²Proverbs 11:15.

¹³Proverbs 17:18.

¹⁴Proverbs 22:26. See also Proverbs 6:1-5; 20:16; Genesis 43:9; 44:32; Job 17:3.

¹⁵See J. F. McCurdy, *HISTORY, PROPHECY AND THE MONUMENT*, par. 596, where the opinion is ventured that this denunciation of suretyship in the proverbial literature evidences dishonesty in business transactions among the early Hebrews.

By its terms, one *Balatu* became surety for one *Shamash-ah-iddina* in respect of a debt owed by the latter to *Balâtu's* father, *Ellil-Shum-iddina*. This contract was executed in the presence of five witnesses.¹⁶ The second of these Persian contracts is dated the 15th of Elul in the 1st year of Barzia (September 15, 525 B. C.) and, like the first, is a guaranty of the payment of a debt.¹⁷ The third of these documents is a promissory note for 1 Mina, 5 shekels of silver, and bearing interest at the rate of 1 shekel upon 1 Mina per month (20 per cent per annum). The brother of the maker of this note was named therein as a surety for its payment. This tablet is dated the 23rd of Sivan in the 4th year of Darius (June 23, 517 B. C.), and the names of four witnesses are subscribed.¹⁸

We have already referred to certain sections of the code of Hammurabi, under which the state acted as a surety. The first treaty between Rome and Carthage contained similar provisions. This treaty was made in 509 B. C., during the consulship of Lucius Junius Brutus and Marcus Horatius, the first consuls after the expulsion of the kings. As recorded by the Greek historian Polybius, the pertinent provisions of this treaty read: "Men coming to trade may conclude no business except in the presence of a herald or town clerk, and the price of whatever is sold in the presence of such shall be secured to the vendor by the state, if the sale take place in Libya or Sardinia."¹⁹ From this treaty, as from the code of Hammurabi, we may infer that the contract had been in use for many preceding centuries.

When Gaius wrote his Commentaries (*circa* 150 A. D.), the Romans had developed a highly technical law of suretyship. The *adpromissor*, or surety, was of three varieties; the *sponsor*, the *fidepromissor*, and the *fidejussor*.²⁰ *Sponsores* and *fidepromissores* could act as such only on verbal contracts, whereas the *fidejussor* could be a surety on any undertaking "whether *re verbis*, *litteris*, or *consensu*."²¹ A *sponsor* had also to be a Roman citizen.²²

The modern doctrine of contribution had a counterpart in Roman law. The *Lex Apuleia* (102 B. C.) provided that a *sponsor* or a

¹⁶*Supra* note 10, Text No. 67, p. 31.

¹⁷*Supra* note 10, Text No. 101, p. 29.

¹⁸*Supra* note 10, Text No. 105, p. 30. The word "amêl urkin" was used by the Persians of this period to designate the surety. C. H. W. JOHNS, ASSYRIAN DEEDS AND DOCUMENTS, Vol. 2, p. 146. This testifies to the importance of the surety at that early date.

¹⁹W. R. PATON, THE HISTORIES OF POLYBIUS, Bk. III, Ch. 22.

²⁰Gaius III, 116; The *constitutum* and *mandatum* were also surety contracts but were little used. HUNTER, ROMAN LAW (2d Ed.) 566.

²¹Gaius III, 119.

²²Gaius III, 93, 119, 179.

fidepromissor who had paid more than his share, was entitled to recover the excess from his *co-sponsores* or *co-fidepromissores*. But the *Lex Apuleia* did not apply to *fidejussores* and they had no right of contribution.²³ The harshness of this rule was somewhat alleviated by an epistle of the emperor Hadrian, which provided that, in an action against a *fidejussor*, he could demand that his *co-fidejussores* be joined as defendants and that the recovery against him be limited to his proportionate share. But, if a *fidejussor* had not taken advantage of this law and had paid more than his share, he could not compel his *co-fidejussores* to contribute.²⁴ The Roman Law also gave to the surety (whether *sponsor*, *fidepromissor* or *fidejussor*) the right of reimbursement from his principal; this action was known as *mandate*.²⁵

At the time of Gaius, as today, the surety was the favorite of the law. But he was then protected by laws which are strange to modern times. The *Lex Cornelia* (81 B. C.) provided that a surety (*sponsor*, *fidepromissor*, or *fidejussor*) could not bind himself in one year for a sum exceeding 20,000 sesterces, when the sum so secured was owed by one principal to one creditor. If a surety did become liable for a sum greater than this, he was not wholly discharged, but was liable only to the extent of 20,000 sesterces.²⁶ Also by the *Lex Cicereia* (173 B. C.) a creditor, before entering into a contract of suretyship, was required to make a public declaration, setting out the nature of the principal obligation and the number of persons who were to become sureties on the obligation. If this declaration had not been made, the surety was discharged. This law mentioned only *sponsores* and *fidepromissores* but Gaius says that a like practice was followed where the surety was a *fidejussor*.²⁷

The *Lex Furia*, (95 B. C.) which applied only to the province of Italy, also favored the Roman surety. Under it, *sponsores* and *fidepromissores* were discharged after two years from the date when they had become obligated. This law did not apply to *fidejussores*. They continued to be liable until the principal obligation had been discharged.²⁸ In fact, the liability of the *fidejussor* descended to his heir while that of the *sponsor* and *fidepromissor*, as at common law, terminated at death.²⁹

The Roman contract of suretyship was a parole undertaking. In the time of Gaius, the surety could become bound only by solemnly repeating a set formula of words.³⁰ But when Justinian's Institutes

²³Gaius III, 122.

²⁴Gaius III, 121.

²⁵Gaius III, 127.

²⁶Gaius III, 124.

²⁷Gaius III, 123.

²⁸Gaius III, 121.

²⁹Gaius III, 120.

³⁰Gaius III, 116.

were written (482-565 A. D.), this requirement had been abolished—"coincident intent on both sides, * * * expressed by any words whatever"³¹ was sufficient.

Creditors naturally preferred the more complete liability of the *fidejussor*. For this reason, by the time of Justinian, the contract of the *sponsor* and of the *fidepromissor* had practically passed out of use—so much so, in fact, that in his Institutes he speaks only of the *fidejussor*.

A peculiar feature of the Roman law of suretyship is found in the rule that a *fidejussor* was bound even though the principal obligation was, in law, a nullity. Thus says Justinian, "Nor does it at all matter whether it be a civil or natural obligation to which the *fidejussor* is attached; so that he can be bound even on behalf of a slave * * *"³² This rule is foreign to modern systems of jurisprudence.

A peculiar form of suretyship came from the rule of the Roman law that the debts of a Roman, upon his death, descended to his heirs in proportion to their shares in his estate. In many cases, the estate would be insufficient to pay the debts and the heirs would be called upon to pay the balance due. They were thus subject to all the duties of a surety but, if they had a right of reimbursement, they would profit little by its exercise.³³

It was a common practice of the Roman slave owner to advance capital to a worthy slave, who could invest it in any enterprise which he might select. The master was legally entitled to the profits from the investment but was also liable, to the extent of the capital advanced, for the debts incurred by the slave in his undertaking. Under Roman law, the master was a surety for the slave despite the latter's incapacity to contract. But in modern law, the principal obligation being a nullity, he would not be so considered.³⁴

The surety ordinarily acts as such on private undertakings. In Anglo-Saxon England he was a means of enforcing the criminal laws. Every man was required to have a *borh* or surety, who was responsible for the criminal acts of his principal.³⁵ The origin of this form of suretyship is found in the ancient responsibility of the *maegh* or clan for the injuries inflicted by any of its members upon the members of

³¹Justinian, Inst. Bk. III, Tit. XV, 1.

³²Justinian, Inst. Bk. III, Tit. XX, 1.

³³ANDREW STEPHENSON, A HISTORY OF ROMAN LAW, p. 129.

³⁴HADLEY, INTRODUCTION TO ROMAN LAW, p. 114.

³⁵THORPE, ANCIENT LAWS AND INSTITUTES OF ENGLAND, Ethelred, I, 1; Athelstan, V, 4. Romans were also required to have sureties but only to protect civil rights. Thus the Roman tutor and the curator, in certain cases, were required to give surety for their "proper conduct of the affairs of the ward."—*supra* note 33, p. 369. Also a Roman freeholder had to furnish surety for his appearance at trial.—*supra* note 33, p. 126.

another clan.³⁶ But the clan obligation was inadequate; men in some cases had no kindred or, if they had kindred, the latter on occasions would be unable to meet their responsibility. This situation was remedied, by the formation of groups known as *gegildan* or gild brethren, who are mentioned in the laws of Ine and also in the laws of Alfred. As sureties, one for each other, they supplemented the responsibility of the clan; the total liability being divided between the latter and the gild brethren.³⁷ Thus we find a law of Alfred reading:

“If a man, kinless of paternal relatives, fight, and slay a man, and then if he have maternal relatives, let them pay a third of the ‘wær;’ his gild brethren a third part; for a third let him flee (that is, he was banished).³⁸ If he have no maternal relatives, let his gild brethren pay half, for half let him flee.” And further, “If a man kill a man thus circumstanced, if he (the murdered man)³⁹ have no relatives let half be paid to the king; half to his gild brethren.”⁴⁰

From this latter provision it is evident that the gild brethren were not kindred.

This system of suretyship reached a further development about the year 960 under a law of Edgar, which required that every man have a surety, and provided that, if a criminal escaped, his surety was subject to the punishment which would have been imposed upon him. “And let every man so order that he have a *borh*; and let the *borh* then bring and hold him to every justice; and if any one then do wrong and run away, let the *borh* bear that which he ought to bear.”⁴¹

To meet these requirements and as a further development of this peculiar system of suretyship, the frankpledge made its appearance about the year 1150. A definition of this institution is given by the earliest writer on the subject. “It is of this sort,” he says, “* * * that all men in every ville of the whole realm were by custom under obligation to be in the suretyship of ten, so that if one of the ten commit an offense, the nine have him to justice.”⁴² In this manner did the Anglo-Saxons insure compliance with their criminal laws.

³⁶WILLIAM ALFRED MORRIS, *THE FRANKPLEDGE SYSTEM*, Harvard Historical Studies, Vol. 14, p. 15.

³⁷*Supra* note 36.

³⁸Writer's insertion.

³⁹Writer's insertion.

⁴⁰THORPE, *ANCIENT LAWS AND INSTITUTES OF ENGLAND*, Alfred, 27, 28; See also Ine, 16, Athelstan, VIII, 6.

⁴¹*Supra* note 40, Edgar, II, 6. See also *supra* note 36, p. 19, and *supra* note 40, Cnut, II, 20, Edgar, Supp. 3.

⁴²See *supra* note 36.

The frankpledge represents the final development of this system of suretyship.

But the surety had other functions to perform in Anglo-Saxon England. "No man" says a law of Ethelred, "could either buy or exchange unless he have 'borh' and witnesses."⁴³ The surety was thus an indispensable factor in every business transaction. And a law of Hlothhaere and Eadric provided: "If a husband die, * * * it is right that the child follow the mother; and let there be sufficient *borh* given to him from among his paternal kinsmen, to keep his property till he be ten years of age."⁴⁴ As under modern statutes guardians *ad litem* were required to be bonded.

By the time of Queen Elizabeth the evils of the system of private suretyship were beginning to be felt. Sir Walter Raleigh had apparently acted as a surety with unfortunate results. He wrote:

"If any desire thee to be his surety, give him a part of what thou hast to spare; if he press thee further, he is not thy friend at all, for friendship rather chooses harm to itself than offereth it. If thou be bound for a stranger, thou art a fool; if for a merchant, thou puttest thy estate to learn to swim; if for a churchman, he hath no inheritance; if for a lawyer, he will find an evasion by a syllable or word to abuse thee; if for a poor man, thou mayest pay it thyself; if for a rich man, he needs not; therefore, from suretyship, as from manslayer or enchanter, bless thyself; * * *"⁴⁵

Shakespeare's "Merchant of Venice" is evidence of the wide use of the contract in Elizabethan England. The central subject of this play was the contract of suretyship between Antonio and Shylock under which the latter was to take his pound of flesh if Antonio's friend, Bassanio, failed to pay his debt to Shylock on the date when due. We must remember that this play was written, as were all of Shakespeare's plays, not as a literary production but primarily for presentation to Elizabethan audiences. Shakespeare, the actor and the dramatist, would have chosen as the center of his plot only a subject which would have been familiar to London's play-goers.

THE CORPORATE SURETY IN ENGLAND—THE PERIOD OF EXPERIMENTATION.—(1720-1875)

The system of private suretyship, which we have traced to the very dawn of history, was attended with much which was undesirable. The disadvantages of this system had always been present, as witness the biblical denunciations of it, and it seems strange that the modern

⁴³Ethelred, I, 3.

⁴⁴*Supra* note 40, Hlothhaere and Eadric, 6.

⁴⁵60 BANKERS' MAGAZINE, 216.

system of the compensated surety did not make an appearance at an earlier date. New institutions, however, are born only of necessity and not until the time of the industrial revolution, with its additional demands upon the private surety, do we find a departure from the old order.⁴⁶

The first step in this direction is recorded in an advertisement appearing in the *London Daily Post* of June 10, 1720, and reading as follows:

“Whereas notwithstanding the many excellent Laws now in force for punishing hired servants for Robbing their masters, or mistresses, yet noblemen as well as commoners are daily sufferers; and seldom a Sessions but great numbers are convicted, to the utter ruin of many families, as also a scandal to the Christian religion. This is to give notice that at the request of several house-keepers, Books will be open'd next Saturday at the Devil Tavern, Charing Cross, at 10 a clock, wherein any person may Subscribe, paying 6d. p. c. for a share call'd a £ 1000 stock; no more shares than 3000, and the call for a stock not to exceed 10s. p. c. the first year by quarterly payments. This So. will ins. to all masters and mistresses whatever loss they shall sustain by Theft from any servant that is Tick'd and Register'd in this So. * * * ”⁴⁷

In connection with this advertisement, it should be noted that the word “servant,” as then used, included not only those whom we now so designate but also “clerks” and “all other persons holding positions of trust and not themselves principals.”⁴⁸ This company, which “mixed religion in its prospectus and held its first meeting in a public house, which rejoiced in being named after his satanic majesty,”⁴⁹ proposed to transact only a purely fidelity business. From its prospectus it is clear that its operations were not to be on any scientific basis. History does not relate its fate. The bursting of the South Sea Bubble occurred but a short time after its organization and it is generally believed that, like many other projects, it collapsed in the panic which followed.⁵⁰ Perhaps it is more than a coincidence that this first attempt to break away from the old system of the private surety was made where he had played his most important part—in England.

⁴⁶Charles A. Dean, *Fidelity and Surety Insurance*, 63 SPECTATOR 120; D. P. Bailey, Jr., 32 BANKERS' MAGAZINE, 590.

⁴⁷WALFORD, THE INSURANCE CYCLOPAEDIA, 282; Jarvis W. Mason, *Radio Talks*, Season 1923-1924, p. 10; ORIGIN AND HISTORY OF SURETYSHIP, p. 6; James A. Brady, *Fidelity Insurance and Corporate Suretyship*, THE INSURANCE YEAR BOOK (1888) p. 356; HENRY E. SMITH, SURETY BONDS, p. 3.

⁴⁸WALFORD, THE INSURANCE CYCLOPAEDIA, 282.

⁴⁹A. E. Kirkpatrick, *Guarantee Insurance*, PROCEEDINGS OF INSURANCE INSTITUTE OF TORONTO (1908-1909) 44.

⁵⁰*Supra* notes 47 and 49.

This flurry having passed, no further progress was made in the field of fidelity insurance until the year 1840. In the August issue of the *Dublin Review* of that year, appeared an article by Professor De Morgan of London University, in which it was proposed to apply the principle of averages to the writing of fidelity insurance. De Morgan believed that this principle applied as well to dishonesty as to death or fire or any other subject of insurance; that "the number of persons out of a thousand taken at hazard, who cannot resist a given temptation, should be found to be nearly the same as those out of another thousand who cannot resist it."⁵¹ He argued that, "If a thousand banker's clerks were to club together to indemnify their securities, by payment of one pound a year each, and if each had given security for £500, it is obvious that two in each year might become defaulters to that amount, four to half the amount, etc., without rendering the guarantee fund insolvent." And so he adds, "If it be tolerably well ascertained (*i. e.*, from past experience)⁵² that the instances of dishonesty (in each year)⁵³ among such persons amount to one in five hundred, this club would continue to exist, subject to being in debt in a bad year, to an amount which it would be able to discharge in the good ones."⁵⁴ In conclusion he proposed the organization of a company, which was to act as surety for clerks, secretaries, and others holding positions of trust, with sufficient capital to meet this fluctuation of defalcations. In return, the company was to receive a premium to be applied toward the payment of losses, costs of management and a small dividend to the stockholders. The company was to accept only selected risks, "* * * none but those who could bring satisfactory testimony to their previous good conduct, should be allowed to join the club."⁵⁵

This plan was an innovation; it embodied the first proposal to organize a fidelity insurance company, the operations of which would be in accordance with the established insurance principle, that of averages. But it contemplated only a fidelity business, the least important of modern surety lines. Three years previously, an American, William L. Haskins, had published a pamphlet entitled, "Considerations on the Project and Institution of a Guarantee Company, on a New Plan, with some general views on Credit, Confidence and Currency,"⁵⁶ in which the organization of a company

⁵¹P. 61.

⁵²Writer's insertion.

⁵³Writer's insertion.

⁵⁴P. 61.

⁵⁵P. 62.

⁵⁶A copy of this pamphlet is to be found in the Library of Congress, Washington, D. C. It was published by D. Felt and Co., 245 Pearl St., New York City, in 1837.

named, "The New York Guarantee Co." was proposed. This company was to have a capital of ten million dollars "secured to be paid by the several persons composing the Company, on Real Estate of undoubted value, * * * the Real Estate pledged to the Company, to be vested, in and held by Trustees."⁵⁷

The proposed functions of this company are briefly stated in Section 10 of the plan. "The object and business of the Association will be to *guarantee* the payment of notes and *other written obligations or contracts*, whether of individuals, corporations, or private associations; to undertake the strict fulfillment and execution of trusts, escrows, wills, and endowments; to exercise other duties of Financial Mediation and Agency, and to do other things relative thereto."⁵⁸ And later it is said, "Wherever this system may be adopted, there would be an end to the system, and the necessity, of individual endorsement; a species of accommodation ever dangerous,—always to be avoided,—laying the parties who yield to it under mutual obligations that, in their interchange, often lead to serious mutual injury."⁵⁹ From these provisions of the plan as well as from the name of the proposed company, it is clear that an institution whose main function would be to act as a guarantor or surety, was contemplated. It is true that a fidelity business was not intended but contract bonds, fiduciary bonds and credit guarantees generally are definitely mentioned. Other and similar lines were also proposed. The author clearly was not in error when he said of his project, "In its essential features and leading characteristics, it is without a precedent—standing alone upon its own merits, an entire novelty."⁶⁰

To this American, Haskins, is thus to go all credit for having first conceived of the corporate surety, in its broader and more significant aspects.⁶¹

The New York Guarantee Co. never became a reality. But De Morgan had said in his article, "We have some reason to suppose that an attempt will be made to establish a society for insuring the honesty of clerks, secretaries,"⁶² etc., and, true to his prediction, two companies were organized in London in the very year during which this article made its appearance. The first of these, the British Guarantee of Trust Co., had a proposed capital of £100,000, but it

⁵⁷P. 20.

⁵⁸P. 21; Italics the writer's.

⁵⁹P. 28.

⁶⁰P. 19.

⁶¹This plan has never been mentioned by any other writer on the history of corporate suretyship.

⁶²P. 61.

never operated. The second, the Guarantee Society of London was an immediate success and is still functioning.⁶³ This latter company was patterned after De Morgan's plan; in fact there is every reason to believe that, at the time he was writing his article for the Dublin Review, De Morgan was actively engaged in its promotion. As appears from an early prospectus of the company, it proposed to transact only a fidelity business, this business to be based upon the principle of averages. "Considerable pains have been taken," says the prospectus, "to acquire a knowledge of the average amount of defalcation with various public and private institutions and banking houses, both in London and the provinces, whereby an average has been obtained upon which the Directors place a confident reliance."⁶⁴

On June 18, 1842, less than two years after this company was incorporated, an act was passed by Parliament entitled "An Act for regulating Legal Proceedings by or against 'The Guarantee Society,' and for granting certain powers thereto."⁶⁵ In addition to regulating the business of this company, the act provided, "Be it therefore enacted, That from and after the passing of this Act it shall and may be lawful to and for the Lord High Treasurer and Commissioners of the Treasury, or any three or more of them, or the principal officer or officers of *any other public office or department*⁶⁶ in which any person or persons shall be required to give security by bond or otherwise, * * * to take and accept * * * the guarantee or security of the said Guarantee Society * * *." This act was a decided stimulus to the business of the company. Fidelity insurance had received the stamp of government approval.

In this same year, with the organization of the British Surety Co. came the first proposal to combine life and fidelity insurance. This company was not authorized to transact a life insurance business but, to those who had insured their lives, or who proposed so to do, reduced rates on fidelity bonds were offered. The British Surety Co. never matured but the idea of combining life insurance, which at that time was well established, with fidelity insurance, was applied by the later companies.⁶⁷

In the following year, 1843, Mr. Charles Saunderson, Deputy-Chairman of the Guarantee Society, published a pamphlet entitled,

⁶³ WALFORD, THE INSURANCE CYCLOPAEDIA, 283.

⁶⁴See WALFORD, THE INSURANCE CYCLOPAEDIA, under, "Guarantee Society, The."

⁶⁵5 Vict., (Sess. 2) c. LXIV.

⁶⁶Italics the writer's.

⁶⁷*Supra* note 63, p. 284.

"Suretyship, The Dangers and Defects of Private Security and their Remedy." This article, as its name implies, points out the evils connected with the system of the private surety and shows that such evils do not exist where a corporation, in return for a small consideration, acts in that capacity. The article also discloses that, at this early date, the Guarantee Society was applying the same underwriting principles as are now applied by surety companies. On this point it reads, "Upon the appointment of an individual to any office * * * provided the applicant be found a person of moral worth, the Society are willing to incur the risk of becoming his bondsmen: the individual contributing to the funds of the Society a small percentage proportionate to the amount proposed to be named in the surety bond. *This per-centage, however, is not calculated upon the degree of honesty he may be supposed to possess: if his reputation for strict integrity and morality present any blemish, he is rejected altogether.*"⁶⁸ Independently of the personal character of the individual, the Society is also guided by the nature of the engagement, and the description of employment or business in which the bond of suretyship is required—the character of the referees and their connection with the party—the check under which the person will be placed for whom the security is sought, and the evidence the Society may obtain, that his conduct under these frequent and periodical checks will be observed by a wise and vigilant superior, and not abandoned to the common influences by which he may be surrounded."⁶⁹ Also the Society had shown a determination to prosecute any principal who had defaulted. The solicitors who represented the Association of London Bankers for the Prevention of Fraud, had been retained by the Society.⁷⁰ In the first three years of its existence the Guarantee Society had discovered the basic principles of surety underwriting.

In the year 1845, three new companies were projected. The most successful of these was the British Guarantee Association of Edinburgh. On May 26, 1845, the "form of policy" of this company received the approval of the "Privy Council for Trade" and on Feb. 16, 1847, of the Treasury. For the years 1855-1862, the company showed average earnings of 11% per annum and for the years 1859-1862, 15% per annum on its paid in capital of £ 50,000. In 1862, the company merged into the European Society No. 2. The West of Scotland Guarantee Association of Glasgow, and the Fidelity Guar-

⁶⁸Italics the writer's.

⁶⁹P. 5.

⁷⁰CHARLES SAUNDERSON, SURETYSHIP. THE DANGERS AND DEFECTS OF PRIVATE SECURITY AND THEIR REMEDY, 25.

tee So. of London, also projected in this year, did not mature.⁷¹

In 1847, Mr. James Knight published an article entitled "Private and Public Guarantee for Persons appointed to Offices of Trust considered." This article is a counterpart of that produced four years previously by Mr. Charles Saunderson, of which we have taken note. Two years later, Mr. Knight, in a second pamphlet entitled "Public Guarantee and Private Suretyship," revived the idea of combining life insurance with fidelity insurance. His plan however, contemplated the incorporation of one company which was to be empowered to transact both a life and fidelity business. And further, "The Life policies issued in conjunction with the Surety bonds, whether payable at death, or at a given age, or to secure a Deferred Annuity, or an Endowment for Children are in all cases, contingent upon the honesty of the Employed."⁷² He stated that "an elaborate investigation" of the principles of life and fidelity insurance had been conducted by Prof. De Morgan and Mr. James Ryley "in order that the practical introduction of their union might not, on the one hand, be a matter of speculation, and, on the other, deficient in the fulfilment of the various and important benefits which it comprises."⁷³

In this same year, the United Guarantee and Life Assurance Co. was founded. A prospectus of this company read: "The Main and distinguishing feature of this company is the union of Guarantee for Fidelity with Assurance on Life * * *. The union of the two principles of Public Guarantee with Life Assurance * * * affords (1) To Employers, additional security, by making the assured specially, and increasingly interested in their own good conduct, the value of the policy and the consequent incentive to honesty increasing annually; and to (2) the Employed or Assured, a greater share of confidence from their employers and independence to themselves, * * *."⁷⁴ As appears from this prospectus the company also proposed to write simple fidelity bonds. This company was the first to issue combination life and fidelity policies. It was successful and in 1854 merged into the Peoples Assurance So., the latter assuming the name of "Peoples Provident," later that of "European No. 2".

Two other companies were formed in 1849,—the Times Life and Guarantee and the London Mutual Life and Guarantee Society. They were followed by the United Service and General Assurance Co. and the National Guardian in 1851, and the Anglo-Australian Life

⁷¹*Supra* note 63, pp. 284, 285; HENRY E. SMITH, SURETY BONDS, 4.

⁷²P. 26.

⁷³P. 24.

⁷⁴*Supra* note 63, p. 285.

in 1853. These five companies also were empowered to issue combination policies.⁷⁵

The practice of combining life and fidelity insurance is characteristic of the early history of the English companies. It did not meet with general public approval however. Thus Walford in 1875 says, "It will be seen then that the contract of fidelity and life insurance combined is one requiring the most grave care and consideration, from many points of view; and it may be that these difficulties * * * have prevented the combination from becoming at all general in practice."⁷⁶ Like sentiments have been expressed by a recent writer,⁷⁷ "There are various objections" he says "that can be urged against the inclusion in one policy of various hazards. The different state departments require the companies to classify their various lines, showing premiums, losses, reserves, commissions, etc., separately for each line. It is essential to the company's interest that the experience of the various lines be kept separately, for otherwise there would be no means of telling where the profits were coming from, or at arriving at the sources of losses * * *."⁷⁸ Combination life and fidelity policies gradually passed out of use and today are practically unknown.

Three years after the combination policy had made its first appearance, a new line of surety underwriting was proposed. A prospectus of the Contract Guarantee Co., projected in 1852, provided, "The object for which this company is incorporated, is to supersede the necessity of individual security under commercial or trading contracts by providing that of an associated body."⁷⁹ Also, in the following year, a prospectus of the Achilles read, "The success of those companies which have been established to provide a substitute for personal guarantees for fidelity is well known; but no company at present exists securing the performance of contracts. * * * One of the objects of this Society, therefore, will be to take the place of the surety in those instances, so that any contractor of known respectability and ascertained credit may be able immediately to offer to his principal an undoubted and unquestionable security for the due performance of his contract."⁸⁰ But these proposals were premature;

⁷⁵*Supra* note 63, p. 286. The Mercantile Guarantee and Assurance Co., was founded three years later—in 1856. Its prospectus contained no unusual features.

⁷⁶*Supra* note 63, p. 295.

⁷⁷Frank Hasbrouck, *Combination Policies*, in 5 INSURANCE PAMPHLETS.

⁷⁸p. 4.

⁷⁹See WALFORD, THE INSURANCE CYCLOPAEDIA, under "Guarantee Insurance."

⁸⁰*Supra* note 79.

the Contract Guarantee Co. never was incorporated and the Achilles never entered upon this class of business.⁸¹ Even as late as 1875, as to contracts generally, no further advance had been made. But as to the contracts of public contractors, the practice of insuring their performance had apparently been initiated prior to that date. Walford writing in 1875 says "But the business (*i. e.*, the fidelity insurance business) has extended * * * to the guarantee of contractors for public works."⁸² The name of the company which first undertook this line is not stated.

Contracts of this latter nature are today the principal kind of contracts, the performance of which is guaranteed by surety companies. Thus to this period of experimentation we are to give credit for having first proposed and undertaken a most important present day line of surety underwriting.

While, during the years 1860-1875, ten⁸³ new companies entered the surety field, on the whole this period was uneventful. One development however, attributable to this period, is worthy of note. In 1869 the London Guarantee and Accident Co. initiated the practice of issuing "floating policies" under which the fidelity of a staff of clerks exceeding five in number, was insured. This form of policy obviates the necessity of "long lists of questions and personal inquiries"⁸⁴ and is extensively used by modern fidelity companies.

The Financial Insurance Co. Lim., founded in 1864, was perhaps the first company which contemplated a surety business in countries other than Great Britain. This company, in addition, was empowered to conduct its business in Europe, India and the Colonies. In 1866, however, the company was wound up and, as appears from a prospectus of the London Guarantee and Accident Co. of 1869, no further advances in this respect had, to that date, been made. "It is believed" says this prospectus "that these companies (*i. e.*, surety companies) have not extended their operations abroad—not even to India or the Colonies."⁸⁵

But the business had assumed real proportion in Great Britain. From the very first, the public official business had been extensive.

⁸¹*Supra* note 79.

⁸²*Supra* note 63, p. 290. Writer's insertion.

⁸³*Supra* note 63, pp. 287-289. The Provident Clerks and General Guarantee Association Lim. and the National Guarantee and Suretyship Association, Lim. in 1863; The Financial Insurance Co. Lim. in 1864, The General Accident and Guarantee Co. in 1868; The London Guarantee and Accident Co. and the British Guardian Life in 1869; The British National Insurance Corp. in 1871; The British Prov. Life and Guarantee Association in 1872; The Guarantee Association of Scotland in 1873, and the Commercial Guarantee So. Lim. in 1874

⁸⁴*Supra* note 63, p. 293.

⁸⁵*Supra* note 63, p. 288. Writer's insertion.

And as illustrative of the attitude of the larger corporations and business houses, it may be noted that before the year 1866 the Guarantee Society alone had been adopted by the Bank of England, The East India Company, the Corporation of the City of London, the Bank of Ireland, the North Western Railway, the Eastern Counties Railway, and many others.⁸⁶ An act of Parliament of the year 1867 providing that the heads of departments in the public service were authorized to accept the security only of companies which satisfied certain financial requirements, also testifies to the magnitude of the business.⁸⁷ The corporate surety was now an object of government regulation and control.

By the year 1875 the corporate surety had thus become an established institution. The fidelity business, as already noted, was extensive and was being written on sound underwriting principles. In this field the "floating policy," sponsored by the London Guarantee and Accident Co., had made its appearance. The companies had also ventured into the field of the contract bond. Walford says also that bonds were being given "for malt tax and * * * the securing of judgment debts."⁸⁸ But the business still was new; only in a measure had private suretyship "ceased to be one of the duties of life."⁸⁹ It remained for the New World to develop that which the Old World had introduced.

(To be continued)

⁸⁶Prospectus of The Fidelity Insurance Co. of New York, published in 1866. A copy of this is to be found in the New York Public Library, New York City.
5 BANKERS' MAGAZINE, 89.

⁸⁷30 and 31 Vict. c. 108.

⁸⁸*Supra* note 63, p. 290.

⁸⁹JAMES KNIGHT, PRIVATE AND PUBLIC GUARANTEE FOR PERSONS APPOINTED TO OFFICES OF TRUST CONSIDERED (1847).