Creditor-Guarantor Relationship Under Ethiopian Law

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> The lender must first claim his property from the borrower, and claim it from the guarantor only if the debtor does not pay him. . . . The lender must (first) sue the debtor and (then) the latter's guarantor. [1]

The quotation above cites the basic principles of suretyship according to the *Fetha Negast*, the ancient law of Ethiopia, from which some of our customary law also derives.

Since secular principles laid down in the *Fetha Negast* are largely of Roman origin, the precepts embodied therein naturally reflected the prevailing state of Roman law at the time of the writing of the original Arabic version. (This date is generally placed between the fifth and ninth centuries A.D. [2])

Quite evidently, this was long after the Romans abandoned their harsh practice whereby a creditor could hold a guarantor hostage until the defaulting debtor (or the guarantor himself) performed the obligation. Confronted with a situation where few would be willing to guarantee any debt under such a condition, the Romans had to swing to the other extreme: the guarantor would be proceeded against only after the creditor sued the principal debtor and failed to recover the debt. Essentially, therefore, the guarantor guaranteed against the insolvency of the principal debtor.

As far as the creditor was concerned, this was of course an adverse development. He was not spared the trouble of pursuing an uncooperative debtor by first resorting to the guarantor, where the latter is more solvent and less difficult to deal with. (As the saying goes, the creditor does not choose the debtor but his guarantor).

That, then, was the law of suretyship that was imported into Ethiopia around the middle of the fifteenth century through the *Fetha Negast*. The new legal arrangement worked tolerably well for a largely peasant society, where the individual's mobility was limited and most transactions took place among people whose whereabouts and background were generally known to one another. Besides, the influence of traditional institutions on their members were strong enough to facilitate enforcement of contractual obligations. With increased modernization, however, the influence of those institutions diminished, and people's mobility increased considerably. Especially with the growth of large urban areas, transactions took place among "faceless" individuals.

This change in social and economic conditions, in turn, necessitated a mechanism that would restore reliability to contractual relationships. To that end, modern business practice evolved various means, among which the use of commercial documents is now widespread. Yet, for the great majority of people, those are simply too technical, so that the remedy has to be sought in the old and familiar mechanism of suretyship. Hence, the pendulum has swung once again, this time in favour of the creditor. If business transactions in the impersonal world of today were not to be hampered, it was believed that creditors should be provided with a more reliable guarantee.

Surety is a form of insurance which a creditor takes out so as to minimize the risk of non-payment. Non-payment, in turn, generally occurs for one of two reasons: either because the debtor is insolvent or he is simply unwilling to discharge his obligation. The question is, therefore, whether a simple guarantor undertakes to pay on behalf of the debtor in both those circumstances.

As noted earlier, the history of suretyship under Roman law has been shifting from one extreme to the other, dictated by social and economic developments of the times. It has gone through distinct phases: the early times, when a guarantor's obligation was absolutely primary, gave way to a period when the guarantor's obligation was strictly subsidiary. When it was discovered that even this was out of step with social and economic developments, a movement towards the earlier arrangement was effected.

But there could be no going back to the ancient position, so extremely harsh on the guarantor. That would not have served the purpose of stimulating business transactions. Hence, a compromise arrangement was worked out whereby the creditor would be protected, not only against the insolvency of the principal debtor, but also against a mere non-performance, for whatever other reason.On the other hand, the guarantor would be armed with the necessary means to compel the creditor to proceed against the principal debtor before asking him to discharge the obligation.

It is this compromise arrangement, which will be explained subsequently, that is currently the law of suretyship in most European countries, including France. As the present Ethiopian law of suretyship is largely copied from the French Civil Code, it reflects essentially the same characteristics.

Yet, over two decades after a modern Civil Code came into force in Ethiopia the influence of the *Fetha Negast*, and hence the traditional conception of suretyship, lingers on. Some judges and litigants still believe that a simple guaranter should not be compelled to perform unless it is established that the principal debtor is unable to discharge his obligation. In the opinion of such judges, the creditor should first bring action against the principal debtor and fail to recover before he can proceed against the simple guarantor. [3]

While this is another example of the tension between local custom, on the one hand, and the imported body of law on the other, one may also attribute the incongruency between the law and the practice to the fact that a great majority

of our judges and members of the legal profession are not trained in the modern law. (In 1981, only 6% of the judges and 7% of the advocates had law degrees)

In this paper, an effort will be made to shed some light on one aspect of the Ethiopian law of suretyship - the relationship between the simple guarantor and the creditor. It will be argued that the Civil Code of 1960 has radically altered the old concept of the law of suretyship, so that the creditor can bring action against the guarantor without first suing the principal debtor.

The obligation of the Simple Guarantor

It is no longer a subject of controversy that the obligation of the simple guarantor is subsidiary to that of the principal debtor. He undertakes to discharge the obligation, "*should the debtor fail to discharge it*" (Art. 1920).

But the central question, as to *when* the creditor can proceed against the guarantor, very much depends on our construction of that last phrase of Art.1920. In other words, when is the principal debtor deemed to have failed to discharge his obligation? At least three time references can be considered:

(a) Soon after performance is due;
(b) After the debtor has been placed in default;
(c) After the creditor brings action against the debtor and fails to obtain performance.

Let us first consider the last possibility. As noted earlier, the *Fetha Negast* prescribed that the creditor should sue the debtor before he proceeds against the guarantor. It has also been noted that the conception of the law of suretyship still lingers in the minds of many Ethiopians.

Yet, Art. 1920 talks about the debtor merely failing to discharge his obligation. In the literal and direct interpretation of this term (this mode of interpretation is preferred where the language of the law is not ambiguous), a debtor fails to discharge his obligation soon after the date of performance falls due (the period is calculated in accordance with Arts. 1857 ff.).

Unlike earlier laws, the Civil Code does not talk in terms of the debtor being unable to discharge his obligation, nor does it anywhere require the creditor to first bring action against the debtor before he can proceed against the guarantor As a matter of fact, Art. 1934(1) repeats the term by stating that a "(simple) guarantor shall not pay the creditor unless the principal debtor fails to discharge his obligation,"

This line of argument also finds support in other provisions of the code. One among these is Art. 1933, which brings out very clearly the distinction between a simple guarantee and a joint guarantee. Under a joint guarantee situation, the creditor "may *sue* (the guarantor) without previously *demanding* payment from the debtor..." (emphasis added). One may note the careful use of the words sue and *demand payment* in the same sentence of this provision. One privilege of a creditor who gets the obligation of the debtor secured by a joint guarantee is that

he can bring action against the guarantor even before demanding payment from the debtor. In other words, where the guarantee is not a joint guarantee, the creditor may not sue the guarantor before demanding payment from the debtor. A guarantee that is not a joint guarantee is clearly a simple guarantee. Thus, the foregoing deduction from Art. 1933 applies to a simple guarantee situation : hence the conclusion that in a simple guarantee situation, the creditor may not sue the guarantor without previously demanding payment from the debtor. A further deduction would lead to a final conclusion : as long as he first demands payment from the debtor, the creditor can sue the simple guarantor before he sues the debtor.

Thus, Art. 1933 provides additional clues as to what is meant by "fail" in Art. 1920. For the purpose of bringing action against the guarantor, the debtor is deemed to have failed to discharge his obligation if he does not perform, in spite of the creditor's demand to that effect, upon the expiry of the time fixed for the payment of the debt (Art. 1932 (1)).

What constitutes "demanding payment" ? Is a simple reminder by the creditor that the time for payment has lapsed adequate, or should he properly place the debtor in default before he sues the guarantor ? From a reading of Art. 1772, which is in the nature of a mandatory provision, with Art. 1932 (2&3), coupled with a consideration of the social and economic purposes underlying the requirement of notice, we are inclined to conclude that, where notice is necessary (Arts. 1772-1775), the creditor should first place the debtor in default before he can proceed against the simple guarantor. (Of course, he should also realize the real securities at his disposal.)

If placing in default and realizing the real securities are the only conditions the creditor needs to fulfil before he can sue the guarantor, wherein lies the compromise earlier noted ? It lies primarily in the concept of benefit of discussion.

Benefit of Discussion

It has been noted above how recently the European jurisprudence shifted in favour of the creditor, so that he could proceed against the guarantor without first suing the principal debtor. But it has also been observed that this move was accomplished without depriving suretyship its accessory character. The apparent anomaly was resolved by arming the guarantor against whom action is brought with a device known as "benefit of discussion." By use of this mechanism, the guarantor can compel the creditor to first seize the property of the debtor and recover what is owed him from its proceeds before bringing action against him (Art. 1935). In effect, the creditor would be forced to suspend his action against the guarantor and proceed against the debtor.

If the guarantor could, with such ease, force the creditor to first proceed against the principal debtor, what then is the purpose of entitling the creditor to sue the guarantor before suing the debtor ?

At the outset, it should be noted that it is not all that easy for the guarantor to exercise the benefit of discussion. He has to fulfil a number of conditions, which include indicating to the creditor the debtor's assets located within the country of payment and not subject to litigation. He should also advance sufficient money to cover expenses the creditor may have to incur in his effort to discuss the property of the debtor.

Thus, the burden of identifying the debtor's property that can be discussed and also covering the cost of discussion, are borne by the guarantor - a compromise arrangement that neatly distributes responsibilities between creditor and guarantor.

When should the guarantor exercise the benefit of discussion? In the words of Art. 1935 (1), "as soon as he is first proceeded against." That is also the case in France, where it is considered "a dilatory plea that must be raised *in limine litis*, before the issue is joined." [4] Thus, it must be pleaded in the form of a preliminary objection, lest it be deemed to have been waived (Art. 244 (3) of C.P.C.) once the court embarks upon the task of framing issues.

If all goes well, and the guarantor effectively exercises the benefit of discussion, the court would, pursuant to Art. 278 (2) (b) of the C.P.C., suspend the suit against the guarantor and grant the creditor permission to institute fresh action against the principal debtor.

The creditor may later on revive his action against the guarantor, and demand payment from him, only to the extent the value of the discussed property may fail to satisfy the claim.

Joinder of Principal Debtor and Guarantor

Is joinder of both the principal debtor and the guarantor in the same suit probably the simplest solution to the above raised issues? As a matter of fact, the substantive laws of some legal systems expressly provide for this solution (Art 3051 of Louisiana Civil Code, for instance).

In Ethiopia, it is the procedural law that provides for the possibility of joining two or more defendants in the same suit, for a variety of reasons. Where, for instance, two or more persons are "severally or jointly and severally liable on the same contract" the plaintiff may join them as parties to the same suit (Art. 36 C.P.C.). Under the procedural law, therefore, it is conceivable for the principal debtor and the guarantor to be joined in the same suit. As a matter of fact, this approach is gaining popularity among most creditors.

Nevertheless, the fact that our substantive law does not stipulate joinder of debtor and guarantor gives rise to a number of questions. Most notably, can any one of the parties successfully object to a move to join debtor and guarantor? The creditor can argue, on the basis of the more specific law, that he is entitled to sue the simple guarantor without suing the principal debtor. He can further argue that, since it is of a procedural nature tailored to govern a particular legal relation-

ship, this law should prevail over the much more general provisions of the Civil Procedure Code. By so insisting, the creditor may wish to force the guarantor to invoke the benefit of discussion, whereby the latter will have to indicate the debtor's discussible assets as well as advance the necessary funds.

On the basis of essentially the same arguments, the guarantor may also refuse to remain a co-defendant by invoking his right to compel the creditor first to discuss the property of the principal debtor. If he does so, the court, as noted earlier will have to suspend the suit against the guarantor. The case will be revived only if the creditor fails to recover fully the debt, after having seized all the discussible property of the debtor. Therefore, the guarantor has good reason for choosing to stay out of the first round of the proceedings: he may never have to litigate the case, as the creditor may succeed in recovering from the debtor.

There is yet another reason why an enlightened guarantor may be adverse to being joined as a co-defendant with the principal debtor. As indicated above, he can remain in the suit, having waived his right to exercise the benefit of discussion The question is, once the court passes judgment against both defendants, can the guarantor urge that the judgement be first executed against the principar debtor?

Under Louisiana law, the creditor is entitled to join the debtor and guarantol in the same suit, and, upon judgment being passed against both, the guarantor can move that the judgment be first executed against the principal debtor.[5]

One should, however, note that the Louisiana law on this point is fundamenh tally different. It radically deviates from the French law of suretyship - on whic- it is largely based - by providing the substantive law that the creditor may join the debtor and the guarantor in the same suit. By so doing, it undercuts the benefit of discussion; but, having done so, the Louisiana law had to restore the balance by enabling the guarantor to retain his right to invoke the benefit of discussion even at the stage of execution of judgment. In effect, the Louisiana law simplifies matters by first determining the creditor's right against both debtor and guarantor in one action, thereby eliminating the possibility of two separate proceedings, while at the same time preserving the guarantor's right to compel the creditor to collect first from the principal debtor.

But the Ethiopian law of suretyship, which is also based on French law, remained loyal to the original. Hence, the benefit of discussion should be invoked in *limine litis*. Once the issue is framed, it is deemed to have been waived.

Thus, if a guarantor acquiesced in being joined in the same suit with the debtor, and if judgment is passed against both, there is no substantive law which would enable the guarantor to compel the creditor to execute the judgment first pgainst the debtor. As a matter of fact, a guarantor who remains a defendant is aresumed to have waived his right to invoke the benefit of discussion. . .

CONCLUSION

The point has been made that, more than two decades after the Ethiopian Civil Code came into force, many people, including some judges, still adhere to the old rule that a guarantor cannot be resorted to without the creditor first suing the principal debtor.

But the present law of suretyship, which is largely based on the Civil Code of France, has radically changed that rule. In the words of Planiol, "The surety can be sued first before the debtor." [6]

Yet, the modern laws have not been without their effects. The principles embodied in the *Fetha Negast* - which greatly favoured the guarantor - have been tempered by our procedural laws (which, incidentally, seem to be much more readily absorbed than the substantive laws). Consequently, the current practice is that the creditor invariably joins the pricncipal debtor and the guarantor in the same suit. It has, however, been shown that this practice is tolerated only because the modern law of suretyship is not yet fully understood by many litigants.

After judgment is passed against the co-defendants, it is also current practice that the judgment is first executed against the principal debtor. Once again, this practice finds no support in our law of suretyship.

On the other hand, there is a lot to be said in favour of the present practice As noted earlier, in relation to the Louisiana law of suretyship, it eliminates the possibility of multiple suits,without depriving the guaranty its subsidiary character. To that extent, the practice is more modern than our modern law.

Nevertheless, since the divergence between law and practice cannot be tolerated indefinitely, it should be removed, perhaps by adopting the same approach as that of Louisiana.