

## New York Reevaluates the "Main Purpose" Exception to the Statute of Frauds: Capital Knitting Mills, Inc. v. Duofold, Inc.

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# NEW YORK REEVALUATES THE “MAIN PURPOSE” EXCEPTION TO THE STATUTE OF FRAUDS: *CAPITAL KNITTING MILLS, INC. v. DUOFOLD, INC.*

The Statute of Frauds (the “Statute”),<sup>1</sup> which requires that

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<sup>1</sup> See generally 2 A. CORBIN, CORBIN ON CONTRACTS §§ 275-81 (1950) (history and application of Statute of Frauds). The Statute of Frauds (the “Statute”) became law in the United States through state legislative enactments. See Morris, *The Leading Purpose Doctrine as Applied to the Statute of Frauds*, 62 W. VA. L. REV. 339, 339 (1960). The American version of the Statute was based on the English version. See *id.*

The English Statute of Frauds, originally known as “An Act for Prevention of Frauds and Perjuries,” was enacted by Parliament in 1677. See Costigan, *The Date and Authorship of the Statute of Frauds*, 26 HARV. L. REV. 329, 336-37 (1913). See generally 6 W. HOLDSWORTH, HISTORY OF ENGLISH LAW 379-97 (1924) (discussing English historical background of Statute); Rabel, *The Statute of Frauds and Comparative Legal History*, 63 LAW Q. REV. 174, 174-78 (1947) (discussing European precursors of Statute). The Statute was adopted at a time when the absence of procedural safeguards encouraged plaintiffs to support their contract claims with false testimony. See E. FARNSWORTH, CONTRACTS § 6.1, at 370 (1982). Sections 4 and 17 required that certain types of oral promises be written to be enforceable. See 2 A. CORBIN, *supra*, § 275, at 2-3; Perillo, *The Statute of Frauds in the Light of the Functions and Dysfunction of Form*, 43 FORDHAM L. REV. 39, 39 (1974). Section 4 of the English Statute provided in pertinent part:

[N]o action shall be brought whereby to charge any executor or administrator upon any special promise, to answer damages out of his own estate; (2) or whereby to charge the defendant upon any special promise to answer for the debt, default or miscarriages of another person; (3) or to charge any person upon any agreement made upon consideration of marriage; (4) or upon any contract [f]or sale of lands, tenements or hereditaments, or any interest in or concerning them; (5) or upon any agreement that is not to be performed within the space of one year from the making thereof; (6) unless the agreement upon which such action shall be brought, or some memorandum or note thereof, shall be in writing, and signed by the party to be charged therewith, or some other person thereunto by him lawfully authorized.

An Act for Prevention of Frauds and Perjuries, 29 Car. 2, ch. 3, § 4 (1677), reprinted in Perillo, *supra*, at 39 n.2. For an actual transcript of the original Statute, see Hening, *The Original Drafts of the Statute of Frauds (29 Car. II c.3) and their Authors*, 61 U. PA. L. REV. 283, 285-316 (1913).

The New York Statute of Frauds is contained in the General Obligations Law. See N.Y. GEN. OBLIG. LAW § 5-701 (McKinney Supp. 1988). Section 5-701 provides in pertinent part:

a. Every agreement, promise or undertaking is void, unless it or some note or memorandum thereof be in writing, and subscribed by the party to be charged therewith, or by his lawful agent, if such agreement, promise or undertaking:

1. By its terms is not to be performed within one year from the making thereof or the performance of which is not to be completed before the end of a lifetime;

certain promises be in writing in order to be enforceable,<sup>2</sup> was adopted to address both evidentiary and cautionary concerns. A written agreement will provide physical evidence that the alleged promise was actually made and impress upon the parties the significance of their acts, thereby preventing impulsive promises.<sup>3</sup> Since the Statute often enables a promisor to escape performance of an actual oral promise, courts have interpreted it narrowly, creating case law exceptions in situations where the Statute's original purposes were not served.<sup>4</sup> Covenants to answer for the debt, de-

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2. Is a special promise to answer for the debt, default or miscarriage of another person;

3. Is made in consideration of marriage, except mutual promises to marry;

....

5. Is a subsequent or new promise to pay a debt discharged in bankruptcy;

....

10. Is a contract to pay compensation for services rendered in negotiating a loan, or in negotiating the purchase, sale, exchange, renting or leasing of any real estate or interest therein . . . .

*Id.*

<sup>2</sup> Compare the first clause of section 4 of the English Statute, *see* Perillo, *supra* note 1, at 39 n.2, with the language of the New York Statute, N.Y. GEN. OBLIG. LAW § 5-701 (McKinney Supp. 1988). Although the wording is different, these sections have been interpreted as imposing similar consequences for noncompliance. *See* E. FARNSWORTH, *supra* note 1, § 6.10, at 425. New York courts have interpreted "void" to mean merely voidable. *See* Holender v. Fred Cammann Prods., Inc., 78 App. Div. 2d 233, 235-36, 434 N.Y.S.2d 226, 228-29 (1st Dep't 1980). Unless the party against whom contract enforcement is sought raises the Statute's defense, it is deemed waived. *See* Reich v. Knopf, 65 App. Div. 2d 618, 619, 409 N.Y.S.2d 539, 541 (2d Dep't 1978)(mem.). In addition, a party is "not precluded from asserting defenses based on the terms of the contract, even though he could not have enforced the contract himself." *See* E. FARNSWORTH, *supra* note 1, § 6.10, at 426.

<sup>3</sup> *See* *Recent Statute—Statute of Frauds—Part of English Act Repealed*, 68 HARV. L. REV. 383, 384 (1954) [hereinafter *Recent Statute*]. The primary function of the contractual writing formality is to supply and preserve evidence of the contract. *See* Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799, 800 (1941); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 112 comment a (1981) [hereinafter RESTATEMENT] (primary purpose of Statute assumed to be evidentiary). "The purpose of [the Statute] was to prevent the foisting of an obligation of specified classes by perjury upon one who had never assented to assume it." 2 A. CORBIN, *supra* note 1, § 275, at 3.

Since the promise to pay the debt of another is often gratuitously motivated, the requirement of a writing gives the proposed surety the opportunity to pause and consider the nature and terms of the obligation. *See* Note, *Contracts: Statute of Frauds: Law Reform (Enforcement of Contracts) Act, 1954, 2 & 3 Eliz. 2, c. 34*, 40 CORNELL L.Q. 581, 588 (1955).

<sup>4</sup> *See* H. ARANT, HANDBOOK OF THE LAW OF SURETYSHIP AND GUARANTY § 31, at 86-87 (1931). The Statute is sometimes used by dishonest parties to invalidate agreements made in good faith contracts. *See* 3 S. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 448, at 343-47 (1960). Consequently, courts have developed devices to take contracts outside the purview of the Statute, and have developed legal and equitable remedies to grant relief to

fault or miscarriage of another—known as “suretyship” promises<sup>5</sup>—must be in writing under the Statute. However, this requirement is limited by the “main purpose” rule,<sup>6</sup> which provides that an oral suretyship promise is enforceable if the promisor’s main purpose is to secure a direct benefit for himself and the third

parties that have performed oral agreements. See J. CALAMARI & J. PERILLO, *THE LAW OF CONTRACTS* § 16-8, at 671 (3d ed. 1987).

Some commentators have called for a total or partial abolition of the Statute in the United States, since the original reasons for its passage are no longer compelling. See, e.g., Cunningham, *The Case for Repealing the Statute of Frauds*, 86 CASE & COMMENT, July-Aug. 1981, at 43-47 (Statute’s provision for sales of goods no longer serves useful purpose); Willis, *The Statute of Frauds—A Legal Anachronism*, 3 IND. L.J. 427, 541 (1928); see also *Recent Statute*, *supra* note 3, at 384 (“[d]issatisfaction with the Statute of Frauds in the United States has resulted . . . in movements for revision rather than repeal”). However, other commentators have argued that even if the original reasons for the Statute’s enactment are no longer persuasive, there are additional grounds for a writing requirement. See Vold, *The Application of the Statute of Frauds under the Uniform Sales Act*, 15 MINN. L. REV. 391, 393-95 (1931). For example, the writing requirement prevents innocent misunderstanding of the actual terms of complex modern contracts, thereby avoiding litigation. See *id.*

The English Parliament in the Law Reform (Enforcement of Contracts) Act of 1954, 2 & 3 Eliz. 2, ch. 34, § 1, has repealed all but two of the original Statute’s provisions: the promise to answer for the debt of another, and contracts for the sale of interests in land. See Grunfeld, *Statutes and Reports of Committees - Law Reform (Enforcement of Contracts) Act, 1954*, 17 MOD. L. REV. 451, 451 (1954). A writing requirement for real property transactions remains necessary because of their relatively complicated nature, while the suretyship provision is intended to impress upon the inexperienced promisor the seriousness of his undertaking. See *id.* at 451-52. The English Law Revision Commission had recommended repeal of the Statute because it was passed under conditions which no longer existed. See LAW REFORM COMMITTEE, FIRST REPORT, 1953, CMND. SER. 4, No. 8809; LAW REVISION COMMITTEE, SIXTH INTERIM REPORT, 1937, CMND. SER., No. 5449 [hereinafter SIXTH INTERIM REPORT], reprinted in 15 CANADIAN B. REV. 585-619 (1937). In addition, the Statute was accused of promoting more fraud than it prevented and applying to only arbitrarily selected types of contracts. See SIXTH INTERIM REPORT, *supra*, reprinted in 15 CANADIAN B. REV., *supra*, at 589.

<sup>5</sup> See N.Y. GEN. OBLIG. LAW § 5-701(2) (McKinney Supp. 1988). For a promise to answer for the debt of another to be within this provision, a principal obligation must be owed by the promisee to someone other than the promisor, and the promisee must know or have reason to know of the suretyship relation. See RESTATEMENT, *supra* note 3, § 112 comments b, c & d. The principal debtor’s duty may be conditional, voidable or unenforceable as long as it actually exists. *Id.*; see also W. CLARK, *HANDBOOK OF THE LAW OF CONTRACTS* § 41, at 90-96 (4th ed. 1931) (promise contemplated by Statute is contract of guaranty or suretyship).

<sup>6</sup> See H. ARANT, *supra* note 4, § 36, at 111-12. “Where the surety-promisor’s main purpose is his own pecuniary or business advantage, the gratuitous or sentimental element often present in suretyship is eliminated, the likelihood of disproportion in the values exchanged between promisor and promisee is reduced, and the commercial context commonly provides evidentiary safeguards.” RESTATEMENT, *supra* note 3, § 116 comment a. See also *Hurst Hardware Co. v. Goodman*, 68 W. Va. 462, 469, 69 S.E. 898, 901 (1910) (promisor’s economic benefit goal substantiated existence of oral agreement).

party remains the primary debtor.<sup>7</sup> New York has not adopted this approach, requiring instead that the oral promise to answer for the debt of another be supported by beneficial consideration and that the promisor become the principal debtor.<sup>8</sup> Recently, however, in *Capital Knitting Mills, Inc. v. Duofold, Inc.*,<sup>9</sup> the New York Appellate Division, First Department, while reluctantly applying the New York rule, called upon the New York Court of Appeals to join the majority of states in adopting the "main purpose" exception to the Statute.<sup>10</sup>

In *Capital Knitting*, the defendant, Duofold, Inc. ("Duofold"), a clothing manufacturer, ordered fabrics for its new line from the plaintiff, Capital Knitting Mills, Inc. ("Capital").<sup>11</sup> Duofold instructed the plaintiff to ship the goods to Holtz and Company ("Holtz"), who was going to manufacture the goods for Duofold.<sup>12</sup> Subsequently, Holtz sent a purchase order to Capital, but Capital refused to deliver fabric to Holtz because of Holtz's poor credit rating.<sup>13</sup> Duofold then orally promised to be responsible for Holtz's

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<sup>7</sup> See RESTATEMENT, *supra* note 3, § 116. For an early statement of the main purpose rule, see *Nelson v. Boynton*, 44 Mass. (3 Met.) 396 (1841). "[The] cases are not considered as coming within the statute, when the party promising has for his object a benefit which he did not before enjoy, accruing immediately to himself." *Id.* at 402. This "benefit" has been construed to mean more than mere "adequate" consideration; the consideration must be clearly beneficial to the promisor. See 3 S. WILLISTON, *supra* note 4, § 472, at 431-32. This approach has been adopted by the United States Supreme Court. See, e.g., *Davis v. Patrick*, 141 U.S. 479, 488 (1891) (Statute inapplicable when promisor has "personal, immediate and pecuniary interest in the transaction"); *Emerson v. Slater*, 63 U.S. (22 How.) 28, 45 (1859) (oral agreement made primarily to promote promisor's individual interest is enforceable).

<sup>8</sup> See *Martin Roofing, Inc. v. Goldstein*, 60 N.Y.2d 262, 267, 457 N.E.2d 700, 703, 469 N.Y.S.2d 595, 597 (1983), *cert. denied*, 466 U.S. 905 (1984); see also Calamari, *The Suretyship Statute of Frauds*, 27 FORDHAM L. REV. 332, 341-50 (1958) (analysis of New York rule); Conway, *Subsequent Oral Promise to Perform Another's Duty and the New York Statute of Frauds*, 22 FORDHAM L. REV. 119, 153-54 (1953) (New York Court of Appeals decisions indicate public policy against adoption of main purpose rule). See generally W. HAGENORN, *THE LAW OF SURETYSHIP AND GUARANTY* § 47 (1950) (general discussion and interpretation of New York Statute).

<sup>9</sup> 131 App. Div. 2d 87, 519 N.Y.S.2d 968 (1st Dep't 1987).

<sup>10</sup> See *id.* at 91-95, 519 N.Y.S.2d at 970-73.

<sup>11</sup> See *id.* at 88, 519 N.Y.S.2d at 968. Duofold, an underwear manufacturer and seller, needed special stripe colored fabric for a new line of products it sought to develop, and Capital ordered yarns from its suppliers in reliance upon the order. See *id.*

<sup>12</sup> See *id.* at 88-89, 519 N.Y.S.2d at 969. A Duofold representative also told Capital that they should expect to receive a purchase order from Holtz that would include the fabrics previously ordered. See *id.* at 89, 519 N.Y.S.2d at 969.

<sup>13</sup> See *id.* An insurance company had informed Capital that they could not give credit approval because they did not have a current financial statement for Holtz, Holtz's condition was unbalanced, and sales had been declining. *Id.*

obligations in return for Capital's promise to sell the goods to Holtz.<sup>14</sup> Thereafter, Capital sent invoices to Holtz, billing them for the fabrics.<sup>15</sup> Learning that Holtz had filed a petition in bankruptcy, Capital brought an action against Duofold for payment.<sup>16</sup> The New York Supreme Court denied the defendant's motion for summary judgment, finding that there were factual issues presented regarding the Statute.<sup>17</sup> The Appellate Division reversed.<sup>18</sup>

Writing for a unanimous court, Justice Sandler applied the traditional New York rule: an oral promise to pay the debt of another is enforceable only if the plaintiff proves that it was supported by new beneficial consideration and that the promisor had become the principal debtor.<sup>19</sup> Since Duofold's main purpose in promising to pay Holtz's debt was to secure an economic advantage for itself with its new clothing line, the court found sufficient beneficial consideration.<sup>20</sup> However, Capital did not fulfill the second part of the test.<sup>21</sup> Despite Duofold's promises to be responsible, the court found that Capital continued to consider Holtz the primary debtor, as evidenced by its acceptance of the order from

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<sup>14</sup> See *id.* After hearing that Capital refused to sell to Holtz, Duofold's representative told Capital not to be concerned because Duofold was the responsible party. *Id.* Duofold supervised the entire transaction, controlled the quantity of material manufactured, and changed garment specifications. *Id.* at 89-90, 519 N.Y.S.2d at 969. Duofold later requested that both Capital and Holtz reduce their output, and promised Capital that they would assume responsibility for excess goods. *Id.* at 90, 519 N.Y.S.2d at 969. Subsequently, Holtz fell behind in its payments. *Id.*

<sup>15</sup> See *id.* at 90, 519 N.Y.S.2d at 969-70.

<sup>16</sup> See *id.* at 90, 519 N.Y.S.2d at 970.

<sup>17</sup> See *id.* The lower court premised its denial of the motion on the Statute's provision in U.C.C. § 2-201(1), which provides that contracts for the sale of goods over \$500 must be in writing. See *id.* at 90-91, 519 N.Y.S.2d at 970. The court found that there were factual issues presented regarding whether the contract fell within the U.C.C. § 2-201(3) exception for specially manufactured goods that are not suitable for sale to others in the seller's ordinary course of business. See *id.* at 91, 519 N.Y.S.2d at 970.

<sup>18</sup> See *id.* at 95, 519 N.Y.S.2d at 973. The Appellate Division addressed an issue which was not directly considered by the lower court: whether the first cause of action was void because the oral promise was made to answer for the debt of another. See *id.* at 91, 519 N.Y.S.2d at 970.

<sup>19</sup> See *id.* at 93, 519 N.Y.S.2d at 971.

<sup>20</sup> See *id.* "The New York approach" has been interpreted by the courts to require a finding of beneficial consideration before they will consider the primary obligation issue. See *id.*; *Martin Roofing, Inc., v. Goldstein*, 60 N.Y.2d 262, 266, 457 N.E.2d 700, 702, 469 N.Y.S.2d 595, 597 (1983), *cert. denied*, 466 U.S. 905 (1984); see also *Richardson Press v. Albright*, 224 N.Y. 497, 501, 121 N.E. 362, 364 (1918) (requiring promisor to be independently liable after finding of beneficial consideration).

<sup>21</sup> See *Capital Knitting*, 131 App. Div. 2d at 93, 519 N.Y.S.2d at 971.

Holtz and its submission of invoices to them.<sup>22</sup> Although the court might have properly concluded its decision at this point, it further discussed the "main purpose" rule.<sup>23</sup>

Justice Sandler noted that the rule has been adopted by a majority of jurisdictions, and accepted by leading contract law scholars.<sup>24</sup> In advocating the rule's adoption in New York, the court argued that no prior New York case had explicitly rejected the "main purpose" rule or articulated a reason for departing from it.<sup>25</sup> Moreover, the evidentiary and cautionary concerns addressed by the Statute had not been present in cases arising under this rule.<sup>26</sup> Justice Sandler concluded that the facts in the *Capital Knitting* would provide the New York Court of Appeals with an opportunity to reconsider adoption of the "main purpose" rule.<sup>27</sup>

While *Capital Knitting* argued cogently for reevaluation of the "main purpose" rule, it is submitted that more compelling reasons than those articulated by the court exist in favor of the rule's adoption. By comparing the "main purpose" rule with the tradi-

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<sup>22</sup> See *id.* "[N]otwithstanding Duofold's promise to be responsible, Capital understood, as evidenced by its acceptance of the order from Holtz and its submission of invoices to Holtz, that Holtz was, at least in the first instance, the party from whom payment was to be secured." *Id.* at 91, 519 N.Y.S.2d at 970. Capital did not claim that it relied upon Duofold's most recent oral promise, nor was there any indication that the new promise was intended to extinguish Holtz's liability. See *id.* at 93, 519 N.Y.S.2d at 971.

<sup>23</sup> See *id.* at 91-93, 519 N.Y.S.2d at 970-71. The court stated that Duofold's oral promise to pay for Holtz's debt would have been enforceable under the "main purpose" exception to the Statute. See *id.* at 92, 519 N.Y.S.2d at 971. For a discussion of the substantive elements of the main purpose rule, see *infra* notes 43-51 and accompanying text.

<sup>24</sup> See *Capital Knitting*, 131 App. Div. 2d at 94, 519 N.Y.S. 2d at 972. The court noted Professor Corbin's strong support for the main purpose rule and the rule's recent adoption by Texas, a state that had previously rejected the rule. See *id.* at 92, 95, 519 N.Y.S.2d at 971-72.

<sup>25</sup> See *id.* at 93-94, 519 N.Y.S.2d at 972. The *Capital Knitting* court stated that "in none of the four opinions that . . . came to be interpreted as establishing the New York rule does there appear an explicit rejection of the main purpose rule. Nor do any of these decisions set forth a reasoned explanation for departing from a doctrine . . . supported by impressive judicial authority." *Id.* (citations omitted). In the only case of the four which referred directly to the main purpose rule, *White v. Rintoul*, 108 N.Y. 222, 15 N.E. 318 (1888), the court of appeals had concluded that the promisor was not primarily motivated by an economic benefit. *Id.* at 230-31, 15 N.E. at 322.

<sup>26</sup> See *Capital Knitting*, 131 App. Div. 2d at 92, 519 N.Y.S.2d at 970-71.

<sup>27</sup> See *id.* at 95, 519 N.Y.S.2d at 973. In *Martin Roofing v. Goldstein*, 60 N.Y.2d 262, 457 N.E.2d 700, 469 N.Y.S.2d 595 (1983), *cert. denied*, 466 U.S. 905 (1984), the court of appeals stated that the main purpose rule was not the law in New York and would have been inapplicable in any event under the facts of that case. *Id.* at 269, 457 N.E.2d at 704, 469 N.Y.S.2d at 598. The Appellate Division interpreted this as a description of the current state of the law, not as approval of the correctness of this rule. See *Capital Knitting*, 131 App. Div. 2d at 95, 519 N.Y.S.2d at 973.

tional New York approach, this Comment will examine the considerations which require that suretyship promises be in writing. It will also discuss the concerns, such as the Statute's harsh effect and the presence of extrinsic indicia of a promise's genuineness, that have led courts to develop exceptions to the Statute. This Comment will then argue that such concerns are inadequately addressed by the current New York approach and will propose that adoption of the "main purpose" rule is consistent with the policies behind inclusion of suretyship promises within the Statute's coverage and exceptions to the Statute previously developed by the New York courts.

### SURETYSHIP AND THE STATUTE OF FRAUDS

The suretyship provision of the Statute applies to agreements under which a party conditionally promises a creditor to answer for the debt of another, the principal debtor.<sup>28</sup> Courts examine the intentions of the surety and the creditor to determine whether the surety has assumed secondary, conditional liability.<sup>29</sup> Thus, in

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<sup>28</sup> See N.Y. GEN. OBLIG. LAW § 5-701(a)(2) (McKinney Supp. 1988); RESTATEMENT, *supra* note 3, § 112. See also *Continental Casualty Co. v. Associated Pipe & Supply Co.*, 447 F.2d 1041, 1057 (5th Cir. 1971) ("promises to pay the debts of third parties are in the nature of suretyship and . . . unenforceable" unless written). A Texas court has stated:

In determining whether a promise to pay the debt of another is within or without the Statute of Frauds, one test devised by the courts is whether the promisor, by his promise, is a *surety* and is therefore secondarily liable, or whether he has accepted *primary responsibility* for the debt of another. By this test if an oral promise creates the relationship of surety and principal between the promisor and the original debtor, and if the fact is known to the creditor-promisee, it is within the Statute and is therefore unenforceable.

*Gulf Liquid Fertilizer Co. v. Titus*, 163 Tex. 260, 269, 354 S.W.2d 378, 382 (1962). The term "surety" is used within the context of the Statute as a synonym for "guaranty." See E. FARNSWORTH, *supra* note 1, § 6.3, at 379 n.5. A guarantor promises to pay another's debt, with nonperformance by the other as a condition precedent to the duty to pay. See L. SIMPSON, *HANDBOOK ON THE LAW OF SURETYSHIP* 10 (1950).

<sup>29</sup> See, e.g., *Rowan v. Brady*, 98 App. Div. 2d 638, 639, 469 N.Y.S.2d 711, 713 (1st Dep't 1983) (intention of parties determines whether conditional liability exists). An agreement comes under the Statute only when the promisor agrees to pay another's debt if that other does not, not if the promisor agrees to become independently, primarily, unconditionally liable. See E. FARNSWORTH, *supra* note 1, § 6.3, at 379-80. The courts look to the language used, the situation of the parties, and the circumstances surrounding the agreement between the creditor and the promisor to determine their intent as to whom the creditor will hold primarily liable. See, e.g., *O'Hair v. Kounalis*, 23 Utah 2d 355, 358, 463 P.2d 799, 801 (1970) (in determining whether promise is within Statute, intention of parties is most often fact question).

"The application of the statute should not be made to depend upon the form of words used by the promisor." 2 A. CORBIN, *supra* note 1, § 358, at 247. The fact that the promisor's

*Capital Knitting*, Holtz became the principal debtor by ordering the fabric from Capital, the creditor, and Duofold subsequently became the surety by promising to pay Holtz's debt.<sup>30</sup> Capital looked to Holtz first for payment, demonstrating the parties' intent that Duofold only assume secondary liability.<sup>31</sup>

The suretyship provision was included in the Statute as an evidentiary measure to avoid perjury.<sup>32</sup> In most contracts, the promisor has received something for his promise and the circumstances indicate probable liability of the parties, whereas in a suretyship agreement such a benefit is not usually apparent.<sup>33</sup> Consequently, it was easier for creditors to make false claims and to exaggerate the scope and nature of their promises.<sup>34</sup> The formalities associated with requiring a written suretyship agreement should emphasize to the surety the significance of the promise, which is often

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promise is alleged to have been absolute in form, "I will pay P's debt," is not enough for it to be taken outside the Statute. *See Kossick v. United Fruit Co.*, 166 F. Supp. 571, 576 (S.D.N.Y. 1958), *aff'd*, 275 F.2d 500 (2d Cir. 1960), *rev'd on other grounds*, 365 U.S. 731 (1961). The promise in substance must be to answer for the debt of another, "I will pay P's debt if P does not." *See id.* "The ancient purpose of the statute of frauds was to require satisfactory evidence of a promise to answer for the debt of another person, and its efficacy should not be wasted by unsubstantial verbal distinctions." *Id.* *See also Symons v. Burton*, 83 Ind. App. 631, 635, 149 N.E. 460, 461 (1925) (difficult to determine from mere words whether promise was undertaken to incur independent liability).

<sup>30</sup> *See Capital Knitting*, 131 App. Div. 2d at 88-90, 519 N.Y.S.2d at 968-70.

<sup>31</sup> *See id.* at 91, 519 N.Y.S.2d at 970.

<sup>32</sup> *See* RESTATEMENT, *supra* note 3, at 286 statutory note. "In general the primary purpose of the Statute of Frauds is assumed to be evidentiary, to provide reliable evidence of the existence and terms of the contract . . . [T]he Statute serves [a cautionary] purpose . . . in the cases covered by the suretyship . . . provision[]." *Id.* The suretyship provision was designed to prevent false and fictitious claims; it requires a writing to establish liability in circumstances under which the creditor seeks to recover against a mere voluntary surety or guaranty of another. *See Howell v. Harvey*, 65 W. Va. 310, 313, 64 S.E. 249, 251 (1909).

<sup>33</sup> *See Martin Roofing, Inc. v. Goldstein*, 60 N.Y.2d 262, 265, 457 N.E.2d 700, 701, 469 N.Y.S.2d 595, 596 (1983), *cert. denied*, 406 U.S. 905 (1984). The surety must receive consideration for his promise to render the agreement valid. *Id.* Often, however, the consideration for a surety's promise to pay for the debt of another is simply an extension of credit or services to the principal debtor. *See, e.g., Romney Produce Co. v. Edwards*, 9 Ariz. App. 258, 261, 451 P.2d 338, 339-40 (1969) (father's oral assurance to stand behind son's account unenforceable); *Ginger v. Zisman*, 366 Mich. 697, 699, 116 N.W.2d 56, 57 (1962) (attorney's oral promise to pay for services rendered to his client by another attorney unenforceable).

<sup>34</sup> *See* 3 S. WILLISTON, *supra* note 4, § 452, at 357. Where the promisor has not received an apparent benefit from the transaction, the likelihood of perjury is greater "because while in the case of one who has received something the circumstances themselves which are capable of proof show probable liability, in the case of a guaranty nothing but the promise is of evidentiary value." *Id.* at 357-58 (footnote omitted). If the original debtor is unable to pay, a creditor may be tempted to enlarge the scope of the promise or exaggerate words of encouragement to imply an absolute promise. *See Davis v. Patrick*, 141 U.S. 479, 487 (1891).

made under circumstances in which the surety's motives are gratuitous and the possibility of obligation seems remote.<sup>35</sup>

Because the Statute may render a valid oral agreement unenforceable, the courts have carved out exceptions where the aforementioned concerns are absent.<sup>36</sup> Oral agreements which are not promises to answer for the debt of another are enforceable.<sup>37</sup> Thus, an oral promise to pay, irrespective of the liability of the original debtor, is not within the Statute.<sup>38</sup> Similarly, an oral novation—a promise to pay which is accepted by the creditor in immediate discharge of the principal debtor's obligation—is enforceable.<sup>39</sup> The

<sup>35</sup> See RESTATEMENT, *supra* note 3, § 112 comment a. "In the case of suretyship contracts . . . the Statute . . . serves the cautionary function of guarding the promisor against ill-considered action." *Id.* See SIXTH INTERIM REPORT, *supra* note 4, reprinted in 15 CANADIAN B. REV., *supra* note 4, at 617. Several committee members had recommended that the suretyship provision of the English Statute of Frauds should not be repealed since the necessity of a writing would give the proposed surety the opportunity to pause and consider the nature and terms of the obligation. *See id.*

<sup>36</sup> See 2 A. CORBIN, *supra* note 1, § 275, at 3. As Professor Corbin has stated:

Such gain in the prevention of fraud as is attained by the statute is attained at the expense of permitting persons who have in fact made oral promises to break those promises with impunity and to cause disappointment and loss to honest men. It is this fact that has caused the courts to interpret the statute so narrowly as to exclude many promises from its operation . . . The courts cannot bear to permit the dishonest breaking of a promise when they are convinced that the promise was in fact made. The statute of frauds is regarded as a technical defense that often goes counter to the merits.

*Id.* See also Morris, *supra* note 1, at 340 (courts have acted wisely in not applying Statute in contexts where it may be invoked to escape liability).

<sup>37</sup> See H. ARANT, *supra* note 4, § 35, at 99. The Statute does not apply to promises whose form and consideration make the promisor a primary obligor since the promisor is promising to pay his own debt and not the debt of another. *See id.* This is true even though the performance of the promise may effectively discharge the debt of another by fulfilling the original debtor's obligation. *See id.*

<sup>38</sup> See *Habeeb v. Mamary*, 103 Misc. 503, 505, 170 N.Y.S. 468, 470 (Sup. Ct. App. T. 1st Dep't 1918). An oral promise to pay one's own debt, creating independent unconditional liability, is enforceable. *See, e.g., Huckabee v. Stevens*, 32 Conn. Sup. 511, 513, 338 A.2d 512, 514 (1975) (oral promise to pay one's own obligation is not within Statute of Frauds); *Crawler Parts, Inc. v. Hill*, 441 So. 2d 1357, 1358 (Miss. 1983) (Statute not violated where party contracted on his own behalf to have his son's machine repaired); *Hansen v. G.G.F. Holdings, Inc.*, 376 N.W.2d 341, 343-44 (S.D. 1985) (exception to Statute where circumstances render promisor primarily liable depends on whether creditor relied on promise). The initial determination asks whether the promisor was independent and absolute. *See Habeeb*, 103 Misc. at 503, 170 N.Y.S. at 468.

<sup>39</sup> See E. FARNSWORTH, *supra* note 1, § 6.3, at 383. A novation is "a substituted contract that discharges a duty by adding a" new debtor. *Id.* § 4.24, at 284. The consideration for the promisor's promise to pay another's debt is the creditor's promise to release the original debtor. *See RESTATEMENT, supra* note 3, § 280 comment d. A promisor's promise to pay the debt of another is not a novation if the original debtor remains liable and the new promisor's performance of actual payment later discharges the original debtor's obligation. *See*

cautionary policy concerns behind the Statute are not present in either case, as no contingency exists when promisors agree to pay their own debts.<sup>40</sup> Additionally, some promises do not fall within the Statute despite the existence of a suretyship relationship.<sup>41</sup> Promises made directly to the debtor are not covered because creditors are generally the parties who falsely claim that others agreed to pay debts owed them, thereby implicating the evidentiary concerns addressed by the Statute.<sup>42</sup>

### THE "MAIN PURPOSE" RULE

The "main purpose" rule is an additional exception to the Statute's requirement that suretyship promises be in writing.<sup>43</sup> If the promisor's primary objective is to secure some benefit or further some purpose of his own, the oral promise is enforceable.<sup>44</sup>

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*id.*; see also *State Highway Dep't v. Eagle Constr. Co.*, 125 Ga. App. 678, 680, 188 S.E.2d 810, 811-12 (1972) (Statute does not include promise under which promisor substitutes himself as party to perform and releases original promisor); *F.I. Somers & Sons, Inc. v. LeClerc*, 110 Vt. 408, 413, 8 A.2d 663, 665 (1939) (novation is never presumed, clear intention must be shown that novation is essence of agreement).

<sup>40</sup> See 3 S. WILLISTON, *supra* note 4, at 455.

<sup>41</sup> See E. FARNSWORTH, *supra* note 1, § 6.3, at 383. Contracts which are not covered by the Statute fall into two categories. See Falconbridge, *Guarantees and the Statute of Frauds*, 68 U. PA. L. REV. 1, 2 (1919-20). First, there are those contracts which do give rise to suretyship conditional liability but have been held to fall within special exceptions to the statute. *Id.* Second, there are agreements which give rise to independent liability and therefore are not surety contracts, although they are often mischaracterized as such. *Id.*

<sup>42</sup> See H. ARANT, *supra* note 4, § 32, at 88. It is generally agreed that a promise is not within the Statute unless it is made to the creditor. *Id.* A promise to the debtor is not within the language of the Statute and does not implicate its dangers. See L. SIMPSON, *supra* note 28, at 119.

<sup>43</sup> See *Kline v. Lightman*, 243 Md. 460, 221 A.2d 675 (1966).

[W]henver the main purpose of the promisor is to subserve some pecuniary or business purpose . . . , [the] promise is not within the Statute, although it may be in form a promise to pay the debt of another, and although the performance of it may incidentally have the effect of extinguishing that liability.

*Id.* at 473, 221 A.2d at 683 (quoting *Crown Realty Corp. v. Weinstein*, 177 Md. 260, 263, 9 A.2d 602, 603 (1939)).

<sup>44</sup> See *Yarbro v. Neil B. McGinnis Equip. Co.*, 101 Ariz. 378, 381, 420 P.2d 163, 165 (1966). The courts have applied the "main purpose rule" in various situations. A typical situation involves a subcontractor who refuses to work because the contractor has defaulted in payment, and a building owner who agrees to take care of the payment if the contractor does not. See *Otto Contracting Co. v. S. Schinella & Son Inc.*, 179 Conn. 704, 427 A.2d 856 (1980). Here, the courts have determined that the building owner's main purpose was to secure an immediate benefit. See *id.* at 711, 427 A.2d at 859.

Another common situation involves a sole or controlling stockowner of a corporation who guarantees the corporation's debt. See, e.g., *Stuart Studio, Inc. v. National School of Heavy Equip. Inc.*, 25 N.C. App. 544, 547, 214 S.E.2d 192, 194 (1975). In this scenario, a

Originally, the existence of a pecuniary benefit to the promisor evidenced the promisor's intent to incur an independent obligation.<sup>45</sup> However, the courts have expanded the rule to include promises that benefit the promisor in cases where he only intends to incur secondary conditional liability.<sup>46</sup> As the *Capital Knitting* court stated, "[w]here the surety-promisor's main purpose is his own pecuniary or business advantage, the gratuitous . . . element often present in suretyship is eliminated, the likelihood of disproportion in the values exchanged . . . is reduced, and the commercial context commonly provides evidentiary safeguards."<sup>47</sup> Thus, *both* the evidentiary and cautionary policy concerns addressed by the Statute are absent.<sup>48</sup>

The "main purpose" rule has been criticized as inherently difficult to employ.<sup>49</sup> By premising the Statute's applicability to a promise on the promisor's primary motivation, the rule assumes that one of the promisor's purposes predominates and that it is possible to make an objective determination of that motivation.<sup>50</sup> In addition, the "personal benefit" requirement has been inconsistently utilized by the courts; some jurisdictions mandate that the benefit be pecuniary, others only require that the benefit be "busi-

promise to pay the corporation's debt is made principally to advance the stockholder's own interests. *See id.*

<sup>45</sup> *See* L. SIMPSON, *supra* note 28, at 138. Under this view, the main purpose rule applies if the promisor's primary motivation was to secure a benefit, that is, answer for his own debt. *See id.*; *see also* *Hurst Hardware Co. v. Goodman*, 68 W. Va. 462, 468, 69 S.E. 898, 899 (1910) (true test under main purpose exception is whether debt is promisor's or that of another); Simpson, *A Suggested Test for Application of the Main Purpose Rule Under the Statute of Frauds*, 36 CALIF. L. REV. 405, 405-06 (1948) (promise to pay one's own debt, shown by direct beneficial consideration to promisor, not covered by Statute).

<sup>46</sup> *See* *Davis v. Patrick*, 141 U.S. 479, 488 (1891) (Statute inapplicable if third party is primary obligor and promisor has personal, immediate and pecuniary interest in transaction); *Hudson v. Ashley*, 411 A.2d 963, 967-68 (D.C. 1980) (even if promise found to be conditional, leading object rule may still take promise out of Statute); H. ARANT, *supra* note 4, § 36, at 111-113 (courts have expanded the rule to narrow the "scope of the statute").

<sup>47</sup> *Capital Knitting*, 131 App. Div. 2d at 92, 519 N.Y.S.2d at 970-71 (quoting RESTATEMENT, *supra* note 3, § 116 comment a).

<sup>48</sup> *See, e.g., White Stag Mfg. Co. v. Wind Surfing, Inc.*, 67 Or. App. 459, 679 P.2d 312 (1984). "The [main purpose] doctrine is applied when the pecuniary interests of a promisor in a commercial context replace the gratuitous elements often present in suretyship. It eliminates the need for the evidentiary safeguards provided by the writing requirement of the Statute of Frauds." *Id.* at 464, 679 P.2d at 316.

<sup>49</sup> *See* H. ARANT, *supra* note 4, § 36, at 113; *see also* 1 G. BRANDT, *THE LAW OF SURETYSHIP AND GUARANTEE* § 81, at 174 (3d ed. 1905) ("leading object" standard is unsatisfactory test since "main purpose" is difficult to distinguish); 2 A. CORBIN, *supra* note 1, § 366, at 274-75 (rule involves difficult questions regarding purpose and motive).

<sup>50</sup> *See* L. SIMPSON, *supra* note 28, at 138.

ness related."<sup>51</sup> It is submitted, however, that difficulties in the rule's application do not undercut its rationale. Moreover, in factual circumstances such as those presented in *Capital Knitting*, the chances that the creditor's claim is false are minimal. The promisor, Duofold, clearly had reason to promise to pay Holtz's debt in the event that Holtz did not, since the manufacture of Duofold's new clothing line depended on the extension of credit to Holtz.<sup>52</sup> It is suggested that the "main purpose" rule is especially appropriate to promises arising in arms length business transactions.

### THE "PECULIAR" NEW YORK RULE

The New York courts do not apply the traditional main purpose rule.<sup>53</sup> Under the approach employed by the *Capital Knitting* court, an oral promise to pay the debt of another is enforceable only when the promisor receives direct beneficial consideration and the promisor comes under a duty to pay irrespective of the original debtor's liability.<sup>54</sup> Whether the parties intended that the promisor

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<sup>51</sup> Compare *Jim & Slim's Tool Supply, Inc. v. Metro Communities Corp.*, 328 So. 2d 213, 215 (Fla. Dist. Ct. App. 1976) ("personal benefit" is pecuniary) with *Farr & Stone Ins. Brokers, Inc. v. Lopez*, 61 Cal. App. 3d 618, 622, 132 Cal. Rptr. 641, 643 (1976) (benefit usually is, but need not be, pecuniary). Mere adequate consideration is not enough, however. See *Walton v. Piqua State Bank*, 204 Kan. 741, 752, 466 P.2d 316, 326 (1970).

<sup>52</sup> See *Capital Knitting*, 131 App. Div. 2d at 88-89, 519 N.Y.S.2d at 968-69.

<sup>53</sup> See *J. CALAMARI & J. PERILLO*, *supra* note 4, § 19.8, at 788. At one point, New York adopted the traditional main purpose exception. See *Mallory v. Gillett*, 21 N.Y. 412, 433 (1860). However, subsequent cases added a second requirement to the test. In addition to purposely receiving a personal benefit, the promisor must have become independently liable on the debt. See *Brown v. Weber*, 38 N.Y. 187, 191 (1868).

<sup>54</sup> *Capital Knitting*, 131 App. Div. 2d at 93, 519 N.Y.S.2d at 971 (quoting *Martin Roofing v. Goldstein*, 60 N.Y.2d 262, 269, 457 N.E.2d 700, 701, 469 N.Y.S.2d 595, 596 (1983), *cert. denied*, 466 U.S. 905 (1984)). The "peculiar" New York rule can be stated as follows:

[W]here the primary debt subsists and was antecedently contracted, the promise to pay it is original when it is founded on a new consideration moving to the promisor and beneficial to him, and such that the promisor thereby comes under an independent duty of payment irrespective of the liability of the principal debtor.

*White v. Rintoul*, 108 N.Y. 222, 227, 15 N.E. 318, 320 (1888). This rule has been consistently applied in subsequent cases. See *Bulkley v. Shaw*, 289 N.Y. 133, 137, 44 N.E.2d 398, 400 (1942); *Newton v. VanIngen*, 21 App. Div. 2d 425, 427, 250 N.Y.S.2d 874, 876 (4th Dep't 1964), *aff'd*, 16 N.Y.2d 596, 209 N.E.2d 102, 261 N.Y.S.2d 55 (1965); *Antonio Altamari Inc. v. Hochberg*, 59 Misc. 2d 601, 602, 300 N.Y.S.2d 266, 267 (Dist. Ct. Nassau County 1969).

One commentator has suggested that the "peculiar" New York rule applies only if the promisor has obligated himself after or at the same time as the original debtor. See *Calamari*, *supra* note 8, at 344. In contrast, the majority main purpose rule is utilized if the promise is made before the obligation is incurred by the principal debtor. *Id.* But see *Con-*

assume independent liability is a question of fact.<sup>55</sup>

In *Martin Roofing v. Goldstein*,<sup>56</sup> the New York Court of Appeals recently reaffirmed New York's double requirement and stated that the "main purpose" rule is not the law in New York.<sup>57</sup> The *Martin Roofing* court noted that, under the facts of the case, the "main purpose" exception would have, nonetheless, been inapplicable since the evidence did not establish a benefit to the promisor.<sup>58</sup> The *Capital Knitting* court interpreted this statement to indicate that the court of appeals would reconsider the main purpose rule if presented with a case where facts squarely presented the issue.<sup>59</sup>

### A SUGGESTED APPROACH

New York courts have not articulated a specific reason for rejecting the majority rule. Criticism of the New York rule has focused on the additional requirement that the promisor assume primary liability on the debt.<sup>60</sup> As a result of the additional requirement, New York courts have rarely held an oral, subsequent

way, *supra* note 8, at 141-42 (main purpose rule applicable whether promisor's promise made before, after, or concurrently with original obligor's agreement). Subsequent cases, however, indicate that the New York standard has been applied to promises made both before and after the original promisor has incurred his debt. *See, e.g.,* *Slavenburg Corp. v. Rudes*, 86 App. Div. 2d 517, 518, 445 N.Y.S.2d 759, 761 (1st Dep't 1982) ("no distinction between a case where an antecedent indebtedness existed at the time of the promise and . . . where the indebtedness is created subsequently to the promise").

<sup>55</sup> *See Rosenkranz v. Schreiber Brewing Co.*, 287 N.Y. 322, 325, 39 N.E.2d 257, 257 (1942); *Trombley & Carrier Co. v. Seligman*, 133 App. Div. 525, 526-27, 117 N.Y.S. 1063, 1063-64 (3d Dep't 1909).

<sup>56</sup> 60 N.Y.2d 262, 457 N.E.2d 700, 469 N.Y.S.2d 595 (1983), *cert. denied*, 466 U.S. 905 (1984).

<sup>57</sup> *See id.* at 267-69, 457 N.E.2d at 703-04, 469 N.Y.S.2d at 597-98. In *Martin Roofing*, a minority stockholder of a corporation allegedly promised a contractor payment of a debt owed by the corporation. *See id.* at 264, 457 N.E.2d at 701, 469 N.Y.S.2d at 596. The New York Court of Appeals, in a unanimous decision, determined that under the New York approach, the stockholder promisor did not receive beneficial consideration. *Id.* at 267, 457 N.E.2d at 703, 469 N.Y.S.2d at 598. Stockholders are not liable for the debts of a corporation and, thus, a promise to answer for the corporation's debts only provided the stockholder with a remote, indirect benefit. *See id.* at 267, 457 N.E.2d at 702, 469 N.Y.S.2d at 597. In dicta, the court also concluded that even if there were beneficial consideration, the stockholder had obligated himself only as a surety, not as an independent obligor; thus, the second part of the test remained unfulfilled. *See id.* at 267-68, 457 N.E.2d at 703, 469 N.Y.S.2d at 598.

<sup>58</sup> *See id.* at 269, 457 N.E.2d at 704, 469 N.Y.S.2d at 598.

<sup>59</sup> *See Capital Knitting*, 131 App. Div. 2d at 93, 519 N.Y.S.2d at 972-73.

<sup>60</sup> *See J. CALAMARI & J. PERILLO, supra* note 4, § 19-9, at 790.

promise to pay the debt of another enforceable.<sup>61</sup> It is suggested that the stringent New York standard is overly cautious, and often operates to prevent enforcement of legitimate oral promises of guaranty. Moreover, New York's rejection of the "main purpose" rule is inconsistent with its adoption of other exceptions to the Statute. New York utilizes the "novation" exception.<sup>62</sup> It also sanctions oral promises not made directly to the creditor.<sup>63</sup> In each exception, *one* of the concerns addressed by the Statute is absent; cautionary in the former, evidentiary in the latter.<sup>64</sup> Thus, enforcement of actual oral agreements is permitted where the concerns addressed by the statute do not exist, and risk of perjury is lessened.<sup>65</sup> The "main purpose" exception has been adopted in other jurisdictions because *both* concerns are absent in situations to which the rule applies.<sup>66</sup> Therefore, virtually no justification for the Statute's requirement of written documentation exists if the promisor's main purpose is to subserve his own interests. It is submitted that adoption of the "main purpose" rule would discourage use of the Statute as a shield from liability on actual oral agreements without abrogating the Statute's fundamental policies of impressing upon individuals the seriousness of contractual obligations, and avoiding uncertainty by reducing agreements to writing.<sup>67</sup>

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<sup>61</sup> See Conway, *supra* note 8, at 130.

<sup>62</sup> See *Town & Country Linoleum & Carpet Co. v. Welch*, 56 App. Div. 2d 708, 708-09, 392 N.Y.S.2d 517, 518-19 (4th Dep't 1977); *Healy v. Brotman*, 96 Misc. 2d 386, 389-90, 409 N.Y.S.2d 72, 73-74 (Sup. Ct. Suffolk County 1978).

<sup>63</sup> See *Zauderer v. Paterno Estates, Inc.*, 25 Misc. 2d 180, 183, 204 N.Y.S.2d 202, 207 (Sup. Ct. Spec. T. N.Y. County 1960); *O'Connor v. Bankers Trust Co.*, 159 Misc. 920, 932, 289 N.Y.S. 252, 269 (Sup. Ct. N.Y. County 1936), *aff'd*, 253 App. Div. 714, 1 N.Y.S.2d 641 (1st Dep't 1937), *aff'd*, 278 N.Y. 649, 16 N.E.2d 302 (1938).

<sup>64</sup> See *supra* notes 39-42 and accompanying text.

<sup>65</sup> See *supra* note 36 and accompanying text.

<sup>66</sup> See *supra* notes 47-48 and accompanying text.

<sup>67</sup> *But see* 2 A. CORBIN, *supra* note 1, at 11. Professor Corbin suggests that the trend under New York law has been to expand the writing requirement policy of the Statute to new classes of cases. See *id.* New York has enacted a statute which provides that a written modification or discharge of an existing contract is enforceable without consideration. See N.Y. GEN. OBLIG. LAW § 15-1103 (McKinney 1978). New York has also adopted a statute which provides that an agreement based upon past consideration is binding if written. See *id.* § 5-1105.

## CONCLUSION

The "suretyship" provision was included in the Statute to avoid imposition of liability on innocent parties by unscrupulous creditors. The Statute, however, also operated to relieve third parties who had actually obligated themselves to others. Consequently, the courts have wisely created exceptions in such situations. Today, under the New York approach, actual oral contracts are needlessly held unenforceable, simply because they have failed to meet the overly stringent double standard required by the New York courts. As New York has adopted exceptions with less compelling rationales, it is suggested that New York judicially or legislatively embrace the "main purpose" exception as an effective tool to prevent use of the Statute of Frauds as a shield from contractual liability.<sup>68</sup>

*Theresa Nick*

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<sup>68</sup> For a listing of states that have codified the main purpose rule, see RESTATEMENT, *supra* note 3, § 116 reporter's note, at 301.