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Danger: “Unlimited” Guaranty Covers Theft Losses Caused By Another

Guarantor was the spouse of a business owner. Spouse’s business opened a deposit account and a disbursement account at Bank 1. Later, Bank1 extended to Spouse’s business a commercial revolving loan with a borrowing limit of \$135,000; that loan provided overdraft protection by funding the disbursement account if the business’ account balance went below zero. To obtain the \$135,000 loan, Spouse and Guarantor executed an *unlimited* commercial guaranty. [1] Bank1 and Spouse executed multiple extensions of both the \$135,000 commercial revolving loan.

Sometime later, Bank 2 made a \$100,000 a commercial revolving loan to Spouse’s business. Once again, Spouse and Guarantor “co-signed a continuing, *unlimited* commercial guaranty in favor of” Bank2. Spouse and Bank2 later refinanced the \$100,000 debt.

In sum, Guarantor executed two “unlimited” guaranty contracts with two different banks securing original loans of \$135,000 and \$100,000.

While maintaining deposit and disbursement accounts at Bank1, Spouse’s business opened a commercial checking account at Bank2. Thus, the business had three accounts at two banks. Later, Bank1 and Bank2 discovered a check kiting scheme in the Spouse’s business’ accounts. Overdrafts from the check kiting scheme exceeded \$1,000,000. Spouse committed suicide shortly after the check kiting discovery. There is no indication that Guarantor participated in, knew about, or benefitted from the check kiting.

Bank1 and Bank2 sued Guarantor for both the outstanding loan balances and the check kiting losses. The banks alleged that the check kiting losses were covered by the “unlimited” guaranty contracts executed by Guarantor as part of the \$135,000 and \$100,000 loan transactions. The trial and appellate courts held that the banks’ \$135,000 and \$100,000 loans were contractual consideration making the guaranty contracts enforceable. Further, the courts stated they were following Ohio law by refusing to inquire as to the adequacy of that consideration to support

Guarantor's liability for the check kiting losses: consideration adequate to induce a party to sign a contract is adequate to require that party to honor that contract.

After a trial related to the banks' alleged negligence, both banks were awarded judgments for the total amounts they sought. The trial court held that Guarantor's unlimited guaranties of Spouse's business' obligations to Bank1 and Bank2 were unambiguous and included Spouse's business' liability to the banks for the banks' check kiting losses. The appellate court affirmed holding that: (i) check kiting is a form of account overdrafts; (ii) account overdrafts are an extension of credit; (iii) the guaranties explicitly covered the extension of additional credit to Spouse's business; and (iv) the guaranty contracts each used the word "unlimited.

Guarantor sought to distinguish between ordinary overdraft "loans" and check kiting which Guarantor described as theft for which Guarantor never agreed to be responsible was rejected. The appellate court rejected that effort saying:

[A]t least one Ohio court has held a debt resulting from check kiting activities creates what may be described as a "subsequent borrowing" or a "claim hereafter arising" under the terms of an unlimited guaranty. *The Central Trust Co. v. Goldbach* (Apr. 18, 1979), Hamilton App. No. 780123. Accordingly, a guaranty which encompasses all indebtedness of a corporate borrower, including future extensions of credit, obligates an officer-guarantor to repay overdrafts resulting from a check kite.

Neither the trial court or the appellate court hinted at Guarantor's involvement in the check kiting scheme. Neither court addressed the actual intent of the Guarantor, Bank1 and Bank2 concerning liability for actions that might be criminal.^[2] Those fairness concerns, however, are not relevant. The signed guaranties were "unlimited" and that is how they were enforced.

The above-discussed case is *MidAm Bank v. Dolin*, 2005 WL 1532622 (Lucas County App. Ct., June 30, 2005).

[1] Guarantor was an officer of Spouse's business but did not have an ownership interest in that business. Equal Credit Opportunity

Act, 15 U.S. C. 1691 *et seq.*, issues apparently were not implicated in the guarantees at issue.

[2] For federal criminal concerns see <https://www.justice.gov/usao-ndoh/pr/three-cleveland-women-indicted-165000-check-kiting-scheme-0> and http://www.fedbar.org/Resources_1/Federal-Lawyer-Magazine/2010/The-Federal-Lawyer-August-2010/After-the-Crash-Banking-and-the-Criminal-Implications-of-Check-Kiting-.aspx?FT=.pdf For Ohio criminal concerns, see O.R.C. Section 2913.11 and related sections.

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