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NOTARY BONDS AND INSURANCE: INCREASING THE PROTECTION FOR CONSUMERS AND NOTARIES

MICHAEL J. OSTY*

*He that is a surety for a stranger shall smart for it: and he that hateth suretyship is sure.*¹

INTRODUCTION

This Article discusses the form and function of bonds and the effectiveness of their protection. The bonds discussed here are not those among family, friends, and neighbors. Rather, the bonds and surety relationships discussed in this Article are of a commercial nature. More often than not, the relationships are between unacquainted parties, with the bond serving the purpose of preventing loss.

Suretyship and bonding will be discussed in detail, with particular emphasis placed on notary bonds. The basics of bonding are reviewed, in order to acquaint those unfamiliar with bond terminology, function, and practice. With respect to the notary bond, this Article specifically addresses the form, function and effectiveness of current bonding practices and law. The Article concludes with recommendations and suggestions for additional methods of protecting both the public and the notary from financial loss.

I. OVERVIEW OF SURETYSHIP & BONDING

To gain a thorough understanding of the notary bond and its level of effectiveness, it is essential to understand the fundamental purpose and function of suretyship. This section begins by discussing the purpose of suretyship and the bond. It will then review bond terminology, provide definitions of terms applicable to bonds

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1. 11 PROVERBS 15.

and suretyship, identify the parties involved in a typical surety relationship, and conclude by providing sample bonding language.

A. *Suretyship, Bonding and Commerce*

In every commercial transaction there is an opportunity for gain, but the potential risk of loss. That loss can be in the form of a dishonest employee stealing from the company till, or a debtor's default on a loan. In either case, even the most careful and prudent businessperson may not be able to prevent the loss from occurring. In the public sector, officials are entrusted with power and responsibility to serve the good of society. If this trust is misplaced and the official commits a wrong while in *colore officii*, the public can suffer substantial harm.

The role of the surety is to prevent that harm from occurring under circumstances where the average businessperson or citizen exercising reasonable care would not be saved.² The surety enters into the relationship expecting that the businessperson or citizen will continue to use common sense and prevent loss to themselves. However, in those undertakings where loss could not be avoided, the surety will pay the protected party. The symbol of this protection is the bond. With the bond in place, parties are more willing to take on the role of creditor and the public is more willing to trust that their officials will perform faithfully.

Suretyship existed a thousand years before the birth of Christ.³ Since that time, the role of the parties and terminology have changed little. A review of these general concepts and terms is helpful to fully appreciate the form and function of the notary bond.

B. *Terminology*

The bond terminology in this section is used in any discussion or procedure related to the commercial or legal instrument known as the "bond." The American Heritage Dictionary defines a bond as a "[a]n insurance contract in which an agency guarantees payment to an employer in the event of unforeseen financial loss through the actions of an employee."⁴ Black's legal dictionary defines suretyship as "[t]he relationship among three parties whereby one person (the surety) guarantees payment of a debtor's debt owed to a creditor . . ."⁵ The role of the surety should not be

2. LAURENCE P. SIMPSON, HANDBOOK ON THE LAW OF SURETYSHIP 3 (1950). For the sake of convenience, "surety," "surety company" and "bonding company" will be used interchangeably throughout this paper. So too will the terms "notary" and "notary public" be used interchangeably.

3. *Id.* at 2.

4. THE AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE 215 (3d. ed. 1992).

5. BLACK'S LAW DICTIONARY 1006 (6th ed. 1990).

confused with that of an insurer, as that role is commonly understood. The following technical terms will explain the role of the surety and other parties in the bonding relationship and further define their obligations:

PRINCIPAL: The person who owes a duty, debt or obligation to another is the Principal.⁶ The Principal is primarily liable for the performance of that duty to the intended party.⁷ Sometimes referred to as the "Obligor" or "Debtor," the Principal is considered to have the "principal obligation" to the party to whom the duty is owed.⁸

BENEFICIARY: The Beneficiary is the party to whom the Principal owes the duty, debt or obligation.⁹ Sometimes referred to as the "Obligee" or "Creditor," the Beneficiary is secure in the knowledge that if the Principal does not perform, he may require the Surety to pay.¹⁰

SURETY: The Surety is the third party in the bonding relationship.¹¹ Usually a corporation, it agrees to be under the same duty to the Beneficiary as the Principal.¹² The Surety's liability is also primary and is conditioned only on the Principal's lack of performance of the duty.¹³ If the Principal fails to perform, the Beneficiary may require the Surety to pay.¹⁴ The Surety will thereafter seek reimbursement from the Principal.¹⁵

BOND: A guaranty given by the Surety to the Beneficiary that the Principal will perform his or her duty in the manner intended.¹⁶ Should the Principal default on his obligation, the Surety will pay the Beneficiary for the damages caused, up to the Bond Limit pro-

6. SIMPSON, *supra* note 2, at 13.

7. A distinction in law is made between parties who are primarily liable and those who are secondarily liable. SIMPSON, *supra* note 2, at 5. The term "primary obligation" indicates that the promisor's undertaking is not conditioned upon the failure of another person to perform, but is a direct, absolute promise himself to perform. *Id.* The term "secondary obligation" indicates that the promisor has undertaken to perform only in the event that another person has failed to perform his duty. *Id.* All contracts of suretyship are primary obligations; whereas contracts of guaranty are secondary obligations. *Id.*

8. *Id.* at 4. "The term 'principal obligation' suggests that its performance is secured by another promise, the latter being called an accessorial promise. *Id.* The accessorial promisor expects the principal obligor sought to perform that the obligee may not call on him for performance." SIMPSON, *supra* note 2, at 5.

9. *Id.* at 13.

10. *Id.*

11. *Id.* at 7.

12. *Id.* at 6.

13. *Id.* at 7.

14. SIMPSON, *supra* note 2, at 13.

15. *Id.* at 7.

16. BLACK'S LAW DICTIONARY 181 (6th ed. 1990).

claimed on the Bond.¹⁷

BOND LIMIT: The monetary amount fixed on a Bond up to which the Surety may be held liable to the Beneficiary.¹⁸ This amount is sometimes referred to as the Penal Sum or Penalty of the Bond.¹⁹ The Surety's obligation cannot exceed this amount.²⁰

CLAIM: A written statement made by the Beneficiary of the Bond, given to the Surety company, describing the losses sustained which are covered under the Bond.²¹

The surety bond is not insurance and can be distinguished in several ways. First, the bond is more like a form of credit, secured for the benefit of those who would suffer a loss if a duty was breached. The principal need only pay the premium required to obtain this credit. Second, unlike an insurance policy, no probability of loss is calculated, nor a premium charged, based upon the level of risk. Rather, the cost of the surety's guarantee is based upon the cost of administering the bond. Third, where an insurance company would be ultimately responsible for any payout on a policy claim, the surety is able to recover from the principal, any payments made under the bond. The language of the bond determines the events requiring a surety to pay.

C. Typical Bond Language

There are many different types of bonds available, depending upon the industry or field and the exigencies of the circumstances. In addition to the notary bond, surety or insurance companies may offer the following bonds: license and permit; public official; fidelity; fiduciary; judicial; lost instrument; and bail. Regardless of the type of bond, the basic parties, the Principal, Surety and Beneficiary and their relationship, remain the same. The language of the bond, however, will differ depending upon the intention of the

17. SIMPSON, *supra* note 2, at 13.

18. *Id.*

19. *Id.*

20. However, the surety can be held liable for amounts in excess of the bond limit where that amount is for interest or costs incurred as a result of the surety's detaining payment. *Harris v. Northwestern Nat'l Ins. Co.*, 6 Cal. App. 4th 1061, 1065 (1992). It is usually for fees and costs incurred by the beneficiary a result of the surety's denial of a claim. *Id.* In *Harris*, the surety, Northwestern, denied liability for damages suffered by the Plaintiffs. *Id.* at 1063. The notary was found negligent for failing to obtain adequate identification and keep accurate records. *Id.* An award was entered against the notary individually and against the surety. *Id.* at 1064. The surety appealed the finding on behalf of the notary and itself. *Id.* The court found that the surety, as appellant, was responsible as a losing party litigant for costs incurred in addition to the amount of the bond. *Id.* at 1068.

21. William Peterson, *Why Notary Public Bonds?*, AM. NOTARY MAG., Nov.-Dec. 1995, at 4.

parties.

The language of the bond expresses the conditions of the relationship and the circumstances under which the surety must pay. By using a performance or completion bond, a homeowner can protect themselves from unscrupulous builders. The bond, entered into for the benefit of a homeowner, usually states that the construction contractor, as principal, along with the surety, guarantee that if the contractor fails to complete the intended work, the homeowner can make a claim against the bond to pay for completion of the work.

The notary bond contains the same basic parties, the principal, surety and beneficiary. The bonding company signs as surety and the notary as principal. The party who would request the notarial act is the beneficiary. The following language, taken from the Illinois notary bond, is typical of bond agreements:

KNOW ALL BY THESE PRESENT, That we (the notary) as principal and (insurance company, as surety) are held and firmly bound unto the People of the State of Illinois, in the penal sum of FIVE THOUSAND DOLLARS, for the payment of which, well and truly made, we bind ourselves, our heirs, executors, administrators and assigns jointly and severally, firmly by these presents.

THE CONDITION OF THE ABOVE OBLIGATION IS SUCH THAT, whereas, the above bound principal has applied for appointment by the Secretary of State of the State of Illinois as a Notary Public for a four year term.

Now, if the said principal shall truly and faithfully perform and discharge the duties of said office of Notary Public, in all things according to law, then the above obligation is null and void, otherwise to remain in full force and virtue in law. The term of this bond is four years and commences on the effective date of the principal's commission.²²

The language of the bond identifies the parties, dictates their obligations and provides for a remedy if those obligations are not met. If the beneficiary believes that the principal has defaulted on his or her obligation under the bond, the right of recovery is built into the language of the bond and specifies the maximum amount recoverable against the bond.

However, what the notary bond fails to describe in plain English, are those elements of greatest concern to any beneficiary. First and foremost, the ordinary citizen without some training in the law would have no idea that they can pursue a claim against the surety without ever bothering with the notary. This right is identified by the language "jointly and severally." Another concern of any would be claimant, is under what circumstances the notary

22. Taken from the Illinois Bond.

is in default. According to the bond, the principal's duty is to "[t]ruly and faithfully perform and discharge the duties of the office . . ." ²³ This language was chosen purposefully, to provide a remedy for both negligent and intentional misconduct. The claimant is protected whether the notary fails to act in a reasonable manner or willfully commits a wrong under color of office.

From the economic standpoint of recovery, the bond fails to advise the beneficiary whether attorney's fees or costs, incurred as a result of the claim, are reimbursed from bond funds. How to proceed on a claim against the notary bond and whether the claim can be barred after a certain time is not explained. This information is critical, and could be written in plain English on the face of the bond. Even if it were, most assuredly, very few, if any notaries do or would present the conditions of their notarial obligation to potential signatories.

A curious or concerned signatory could always call a bonding company for further explanation of the bond's purpose. Unfortunately, depending upon the company called, the signatory could become further confused or completely misinformed. While conducting research for this article, the author called several bonding companies to find out exactly how the bond worked and how one proceeded with a claim. Upon asking "who is protected by the bond," the author was advised that the "bond was intended to protect the Secretary of State." If someone sued the State because it commissioned a notary who committed bad acts, the bond would reimburse the State for its costs. ²⁴ (The explanation of the recovery procedures was only somewhat more informed).

D. Recovery Under the Bond

In order for a beneficiary to recover any amount under a bond, one must make a claim. The claim can be made by a formal demand against the surety or through filing a civil suit. It is not necessary to file suit in order to recover on a bond. In fact, one intended benefit of having a bond is to provide a fast, low cost way by which an aggrieved party can recover damages. Moreover, if a beneficiary does file suit, usually jointly against the principal and surety, attorney's fees are not recoverable against the surety unless they are provided for by the terms of the bond or by statute. ²⁵ Neither are the notary's legal fees covered by the bond, should one

23. *Id.*

24. Telephone Interview with a bonding company (January 20, 1998). The author does not wish to identify the particular bonding company for fear of jeopardizing the careers of its misinformed, yet well meaning employees. The supervisor was only too eager to call back and confirm that the state was indeed the intended beneficiary of the notary bond.

25. See *supra* note 20 and accompanying text for a discussion of exceeding the bond limit.

seek counsel.

The terms of the bond and the intentions of the parties determine whether the surety is liable for the principal's default. Generally, the liability of the surety accrues upon the default of the principal's obligation under the bond. In addition to showing default, the beneficiary must also allege that the injuries incurred are a proximate result of that default. It is not uncommon for a surety to deny a claim based on the defense that the principal did not breach the conditions of the bond or that the beneficiary was not injured due to the proximate cause of the breach.²⁶

Once the claim is proved to the satisfaction of the surety, or a judgment is entered against the principal, the surety will pay the damages caused, up to the penal sum of the bond. In general, the amount of the surety's liability for the claim is set by the penalty of the bond and cannot exceed that amount.²⁷ However, if the surety appeals a judgment of liability, it may be found liable for costs. Moreover, when liability on the bond is established, by judgment or otherwise, it becomes a debt due. Thereafter, any interest accrued will become an additional liability of the surety, even if that amount is in excess of the penal sum of the bond.²⁸

What may seem a precarious position for the surety, in fact, is not. The surety has the right to immediate recovery from the principal of any amounts disbursed under the bond on the principal's behalf. This right of reimbursement is an established rule of law, and exists regardless of whether it is stated in the contract between the principal and surety.²⁹ Therefore, unlike an insurance policy, the principal (notary) has ultimate personal responsibility for any loss incurred by a breach. Unlike the beneficiary, even with the bond in place, the notary has no protection from personal financial loss.

II. THE NOTARY BOND

In order to protect the public from damage caused by the official misconduct of a notary, thirty states currently require notaries to be bonded.³⁰ The amounts range from as low as \$500 to a

26. MICHAEL L. CLOSEN ET AL., NOTARY LAW AND PRACTICE: CASES AND MATERIALS 277 (1997). See also *State v. Maryland Cas. Co. of Baltimore*, 344 S.W.2d 55, 59 (Mo. 1961) (stating that the surety was unsuccessful in arguing that the fraudulent act of the notary was not the proximate cause of the plaintiff injury).

27. See *supra* note 20 for a discussion on the notary exceeding the bond limit. See also *Great Am. Indem. Co. v. State*, 32 Del. Ch. 562, 567 (1952).

28. *Illinois Surety Co. v. John Davis Co.*, 244 U.S. 376, 381 (1917).

29. *Pearlman v. Reliance Ins. Co.*, 371 U.S. 132, 137 (1962).

30. Bond amounts vary state by state, see ALA CODE. § 36-20-3 (1991) (\$10,000); ALASKA STAT. § 44.50.120 (Michie 1989) (\$1,000); ARIZ. REV. STAT. § 41-315 (1992 & Supp. 1995) (\$5,000); ARK. CODE ANN. § 21-14-101(d)(1) (Michie 1996) (\$4,000); CAL GOV'T CODE. § 8212 (West 1992 & Supp. 1996)

maximum of \$15,000. Historically, these bonds provided a reliable method for injured parties to recover a significant amount of money damages. However, the notary bond limit has failed to keep pace with inflation and dramatically increasing consumer prices, thereby trivializing the protection it was originally meant to provide.

A. Protection of the Notary Bond

A public or quasi-public official, the notary holds a unique and important position in the flow of commerce in the United States.³¹ The notary serves the critical purpose of preventing fraud and forgery on a large scale. Acting as an unbiased witness to the identity of a person who comes before him or her, the notary's seal indicates authenticity and imbues trust in the document presented. For these reasons, the notary holds a great deal of responsibility to the citizens and is therefore held to a certain standard of care. If the notary fails to meet that standard, the damage can be severe.

The standard of care for notaries, no matter in what state, is one of objective reasonable care.³² This means that the notary must act as any other reasonably prudent notary would act in similar circumstances.³³ The notary will be held personally liable if he or she fails to exercise reasonable care in the performance of

(\$15,000); D.C. CODE ANN. § 1-803 (1992) (\$2,000); FLA. STAT. ANN. § 117.01(4) (West 1996) (\$5,000); HAW. REV. STAT. § 456-5 (1995) (\$1,000); IDAHO CODE § 51-105(2) (1994) (\$10,000); 5 ILCS 312/2-105 (West 1993 & Supp. 1996) (\$5,000); IND. CODE ANN. § 33-16-2-1(c) (West 1992 & Supp. 1996) (\$5,000); KAN. STAT. ANN. § 53-102 (West 1983) (\$7,500); KY. REV. STAT. ANN. §§ 423.010 - .990 (Michie 1992) (ranging usually from \$500 to \$1,000 depending upon the county); LA. REV. STAT. ANN. § 35:1 (West 1985 & Supp. 1996) (\$5,000); MICH. COMP. LAWS ANN. § 55-110 (West 1991) (\$10,000); MISS. CODE ANN. § 25-33-1 (1991) (\$5,000); MO. ANN. STAT. § 486-235 (West & Supp. 1996) (\$10,000); MONT. CODE ANN. § 1-5-405 (1995) (\$5,000); NEB. REV. STAT. § 64-102 (1990) (\$10,000); NEV. REV. STAT. ANN. § 240.030 (Michie 1996) (\$10,000); N.M. STAT. ANN. § 14-12-3 (Michie 1995) (\$500); N.D. CENT. CODE § 44-06-03 (1993) (\$7,500); OKLA. STAT. ANN. TIT. 49, § 2 (West 1988 & Supp. 1996) (\$1,000); 57 PA. CONS. STAT. ANN. § 154 (1996) (\$3,000); S.D. CODIFIED LAWS § 18-1-2 (Michie 1995) (\$500); TENN. CODE ANN. § 8-16-104 (1993) (\$10,000); TEX. GOV'T CODE § 406.010 (1990) (\$2,500); UTAH CODE ANN. § 46-1-4 (1993) (\$5,000); WASH. REV. CODE ANN. § 42.44.020 (West 1991) (\$10,000); WIS. STAT. ANN. § 137.01 (West 1989) (\$500); WYO. STAT. ANN. § 32-1-104 (Michie 1996) (\$500). Vincent Gnoffo, Comment, *Notary Law and Practice for the 21st Century: Suggested Modification for the Model Notary Act*, 30 J. MARSHALL L. REV. 1063, 1073 n.70 (1997).

31. See *Commercial Bank of Ky. v. Varnum*, 49 N.Y. 269, 270 (1870) (declaring a notary is a "public officer"); *May v. Jones*, 14 S.E. 552, 553 (Ga. 1891) (holding that a notary is a public official); *Simon v. Peoples Bank & Trust Co.*, 180 A. 682, 682 (N.J. 1935) (holding that a notary is a quasi-public official).

32. *City Consumer Serv., Inc. v. Metcalf*, 775 P.2d 1065, 1069 (Ariz 1989).

33. *Id.* at 1068.

duty.³⁴ Negligent, reckless or willful misconduct by the notary in *colore officii* will invariably result in the notary being held liable for damages.³⁵

The burden is on the injured party to show that the notary committed official misconduct.³⁶ The plaintiff must prove that the damages suffered were a proximate result of the improper notarization.³⁷ The notary's official misconduct does not have to be the sole cause of the damages.³⁸ If damages are proved, the notary has personal liability for all damages proximately caused by the act.³⁹ This liability can be both civil and criminal.⁴⁰

To serve as a source for payment of these damages, most states have required that notaries be bonded.⁴¹ In order to receive a commission in these states, the notary applicant must first be bonded.⁴² Surety companies often serve as a "one-stop shop," providing the application for commission and, on the reverse side of the application, the statutory form of the bond. Upon payment to the surety of the state notary and bond fee, the surety will forward the completed application and evidence of bond to the appropriate state agency. For an additional fee, the company can also provide the notarial seal (which may or may not be required).⁴³

As stated above, bond limits range between \$500 and \$15,000. The average cost of a four year bond for \$10,000 ranges from \$50 to \$75. In many cases, the notary's employer pays for both the costs of the notary application and bond. Nevertheless, both the commission and the bond are personal to the notary. A notary's commission belongs to the notary, and the seal and journal are "adjuncts of the public office of Notary . . . regardless who paid for them."⁴⁴

An employer is also liable for the misconduct of a notary if the notary public was acting within the scope of employment at the time the notary committed the official misconduct, and the em-

34. *Id.* at 1069.

35. *Id.*

36. *McDonald v. Plumb*, 90 Cal. Rptr. 822, 824 (Cal. App. 2d 1970).

37. *Id.*

38. *See generally id.*; *Commonwealth v. American Surety Co. of N.Y.*, 149 A.2d 515 (Pa. Super. Ct. 1959); *Iselin-Jefferson Fin. v. United Cal. Bank*, 549 P.2d 142 (Cal. 1976) (holding that notaries are liable for the injury to the plaintiff in spite of other negligent actors or tortfeasors).

39. *McDonald*, 90 Cal. Rptr. at 824.

40. *Johnson v. State*, 238 N.E.2d 651, 654 (Ind. 1968).

41. *Comparison of State Notary Provisions*, NAT'L NOTARY ASS'N, May 1997, at 24.

42. *Id.*

43. Not all states require a notary seal. *Id.* Connecticut, Iowa, Kentucky, Louisiana, Maine, Massachusetts, Michigan, New Jersey, New York, Rhode Island, South Carolina, Vermont and Virginia do not require any seal whatsoever. *Id.*

44. *101 Useful Notary Tips*, NAT'L NOTARY ASS'N, May 1995, at 18.

ployer consented to the misconduct.⁴⁵ However, since the employer is not a party to the notary bond, a claimant cannot seek damages against the employer under the bond. The claimant must pursue a separate action against the employer under the theory of vicarious liability.

B. Effectiveness of the Notary Bond's Protection

The notary bond is intended to "serve as a guarantee to consumers that they will be protected if wronged by the act of a notary."⁴⁶ Unfortunately, the general public probably does not even realize that notaries are bonded.⁴⁷ And even if the public is aware of the bond, the limits are so low that the bond is "useless, wasteful, and misleading."⁴⁸

In the 1800s, when notary bonds were first introduced, the bond limits were typically \$500 to \$5,000. At the time, this was a substantial amount of coverage for a wrongful notarial act. Through the years, the number of notaries and notarizations grew, carriages turned into Cadillacs, and the price of consumer goods skyrocketed. Yet, the notary bond has failed to mirror the economic changes.

The Illinois notary bond is a prime example of that failure. In 1913, the Illinois notary bond was \$1,000. Between 1913 and 1997, the cost of consumer goods rose dramatically. If in 1913 you bought goods or services priced at \$1,000, those same goods or services would cost you \$16,260, in 1997.⁴⁹ However, Illinois, like all other states mandating a bond, failed to match the protection of the bond with escalating consumer prices. In 1986, Illinois raised the bond limit to where it currently stands at \$5,000. This \$5,000 limit was hardly a significant amount at that time, and eleven

45. See generally *Commercial Union Ins. Co. v. Burt Thomas-Aitken Constr. Co.*, 230 A.2d 498 (N.J. 1967); *Transamerica Ins. Co. v. Valley Nat'l Bank*, 462 P.2d 814 (Ariz. Ct. App. 1969); *Garton v. Title Ins. & Trust Co.*, 106 Cal. App. 3d 365 (1980) (describing instances where courts were forced to consider whether employers were vicariously liable for the negligent actions of its employee notaries).

46. Peterson, *supra* note 21, at 4.

47. See Letter from Eugene Hines, past President of the National Notary Association to Vincent Gnoffo, John Marshall Law School student (Jan. 23, 1998) (on file with author) (expressing his serious doubt that many people are aware that notaries are bonded).

48. Michael L. Closen & Michael J. Osty, *The Illinois Notary Bond Deception*, ILL. POL., Mar. 1995, at 13.

49. This figure is based on the change in the Consumer Price Index (CPI) between the years given. See *CPI Calculation Machine* (visited Jan. 6, 1998) <<http://woodrow.mpls.frb.fed.us/economy/calc/cpihome.html>>. The base year is chained; 1982-1984= 100. *Id.* "The [CPI] is that ratio of the value of a basket of goods in the current year to the value of that same basket of goods in an earlier year. It measures the average level of prices of the goods and services typically consumed by an urban American Family." *Id.*

years later, it constitutes a completely irrelevant sum in light of the above analysis.

One need only examine the relevant case law for further evidence that current bond amounts are trivial and useless. Courts, in the last twenty years have held notaries and their employers liable for amounts exceeding their surety bond. For instance, in the 1994 Illinois case of *CNB National Bank v. Spiwak*, the court held the notary personally liable for more than \$23,000 although the notary's bond amount was only \$5,000.⁵⁰ In another case, *City Consumer Services v. Metcalf*, an Arizona court held a notary accountable for \$60,000 while the required bond amount for the notary was merely \$5,000.⁵¹ A Louisiana court, in *Webb v. Pioneer Bank & Trust Co.*, found a notary liable for \$20,000 yet Louisiana only required a \$5,000 surety bond for the notary.⁵² Similarly, in the 1976 case of *Iselin-Jefferson Financial Co. v. United California Bank*, the court held that the notary caused over \$70,000 [damages] to the plaintiff, however, the notary's bond only covered up to \$5,000 in damages.⁵³ Finally, in a 1969 Arizona case, *Transamerica Ins. Co. v. Valley Nat'l Bank*,⁵⁴ the court found a notary liable for over \$84,000 in damages although the state-required surety bond was only \$5,000.⁵⁵

Without fail in these cases, the damages claimed, and awarded, far exceeded the value of the bonds! In a recent article, the claims attorney of a bonding company provided a further example of the ineffectiveness of the bond.⁵⁶ The article, in *American Notary*, used the "real life" case of two parties damaged in the amount of \$72,000.⁵⁷ "Since the notary bond was much less than the amount of the claims made by the [parties] . . . (the bond was \$5,000), both parties reached an agreement whereby one party received \$3,000 and the other \$2,000."⁵⁸ Despite the knowledge of this gross disparity between the value of today's transactions and applicable bond coverage, states and surety companies do not seem to be taking much action.

Maintaining a low bond limit is to the advantage of surety companies. Under the current limits, parties are more reluctant to pursue the notary for the small amount the bond provides. Since the notary is only peripherally involved in the transaction, another party will likely face a claim for damages. This party will more of-

50. No. 89-L-13696 (Cir. Ct. of Cook County tried April 20, 1994).

51. 775 P.2d 1065, 1066 (Ariz. 1989).

52. 530 So.2d 115, 118 (La. Ct. App. 1988).

53. 549 P.2d 142, 143 (Cal. 1976).

54. 462 P.2d 814, 815 (Ariz. Ct. App. 1969).

55. Gnoffo, *supra* note 30, at 1086-87.

56. Brent Beaty, *Claims Against Notary Public Bonds*, AM. NOTARY MAG., January-February 1996, at 7.

57. *Id.*

58. *Id.*

ten be the one with "deep pockets." Even if a claim is pursued against the notary, because the amount of the bond is so small, the bonding company stands a fair chance of recouping its disbursement. Therefore, a lower bond limit means fewer claims and a reduced risk of unrecoverable outlays.

Conversely, if higher bond limits were imposed, say \$100,000, the bonding companies would likely see a marked increase in claims and administrative costs with an equal, if not greater rise in unrecoverable disbursements. Unless a notary had significant personal assets to repay the bonding company (how many people have \$100,000 handy), the notary would be judgment proof, and the bonding company would be unable to recover. Taking a closer look at the statistics of the notary bonding industry, one can see why bonding companies might want to maintain the status quo.

In 1997, there were over 2.3 million notaries in states requiring a notary bond. With the average premium for a four year bond being about \$75, the money collected for these bonds is significant. The profit earned from notaries by surety companies is by no means small either. Consider the following table of statistics provided by the *Surety Association of America*:

USA	DIRECT PREMIUMS EARNED	DIRECT LOSSES INCURRED	LOSS RATIO
1993	17,233,640	376,711	2.2%
1994	16,740,980	516,940	3.1%
1995	16,899,337	503,195	3.0%
1996	22,327,884	826,535	3.7%

("The "earned premiums" figures represent only the premiums properly allocated to each year. For example: If a four-year bond was sold in a particular year, only one-fourth of the premium is shown for that year. The figures shown are prior to deduction for sales commissions.")⁵⁹

Surety companies certainly would want to continue making a 97% profit margin on notary bonds. But increasing the bond amount may lead to an increase in the "Direct Losses Incurred," and thereby decreasing the profit margin. As one bonding company representative told the author, "I am not certain how the bonding procedure works, since we have not paid on a notary bond in ten years."⁶⁰ With a track record that good, there is no incentive for bonding companies to raise bond amounts and expose themselves to increased administrative costs and greater risk of loss on

59. ALFRED E. PIOMBINO, NOTARY PUBLIC HANDBOOK, PRINCIPLES, PRACTICES & CASES 16 (Nat'l ed. 1996).

60. Telephone Interview, *supra* note 24.

claims. Therefore, unless states act to mandate higher bond limits, bond amounts will remain low and the protection will continue to be minimal, with the bonding companies themselves reaping the greatest benefit.

Further studies support the position that, under the current system, bonding companies are the only real winners. In 1987, the Minnesota Department of Commerce conducted a study of claims brought statewide against notary bonds.⁶¹ The study focused on claims submitted to surety companies, two in particular, against notary bonds issued to persons commissioned as notaries in Minnesota.⁶² The results showed that, over a four year period, the two bonding companies collected over \$970,000 in premiums. During that same period, the companies disbursed only \$2,277.50 in claims that they could not recoup from the notaries.⁶³

Colorado also performed a study of the usefulness and necessity of the notary bond.⁶⁴ It found that the small bond limit, compared with the typical cost of consumer goods and real estate, "offers little recovery if a consumer is harmed by the action of a notary."⁶⁵ An injured party will choose to sue the "deepest pocket" instead of the notary.

If the public is not making claims against the notary, then the "hundreds of thousands" of dollars being spent on the bonds are not benefiting the public.

The resolution to the current notary bonding problems is not to eliminate the bond requirement altogether, as Minnesota and Colorado did. Instead, notary bonds should be mandatory and the bond limits should be increased dramatically, to match the rate of inflation and the increasing costs of consumer goods and real estate. Additional measures should also be taken to strengthen and improve all available means of preventing fraud and loss caused by improper notarizations.

III. IMPROVING PROTECTION AGAINST FRAUD AND FINANCIAL DISASTER

A. *Errors and Omissions Insurance*

The answer to the notary bond dilemma is relatively simple.

61. MINNESOTA DEP'T OF COMMERCE, STUDY OF CLAIMS BROUGHT AGAINST NOTARY BONDS 12 (Oct. 1987).

62. *Id.*

63. *Id.* The period studied was from 1983 to 1987. *Id.* During that period, Western Surety wrote 16,038 bonds. *Id.* "During this same period, however, only ten claims (with no paid claims) against the bonds were closed by Western Surety." *Id.* at 14-16.

64. COLO. DEP'T OF REGULATORY AGENCIES, SUNSET REVIEW OF NOTARIES PUBLIC ACT 5 (June 1991).

65. *Id.* at 7.

States should require more substantial notary bonds and mandate Errors and Omissions Insurance (E&O). As previously noted, the notary bond is intended to protect the public from injury due to improper notarization. The bond does nothing to protect the notary, who will ultimately be responsible for reimbursing the surety. Unlike the notary bond, E&O is true insurance. The E&O policy is there to protect the notary, as well as the public. Just as auto insurance protects the negligent driver from financial ruin, by paying for the damage done to himself or the victim, so too does the E&O policy protect the notary and the victim of the notary's misconduct.

An action against the notary for misconduct triggers the claims procedure. If a notary is found liable for negligence, the E&O policy will cover the damages up to the limit on the policy.⁶⁶ Unlike the low and practically useless limits of the notary bond, an E&O policy can have a substantially higher limit, even exceeding \$250,000.

A further benefit of an E&O policy is that it covers the notary's legal fees incurred while defending against the claim. This is true whether or not the claimant recovers. Additionally, if the notary did negligently perform the duties of his or her office, the E&O policy will cover the resulting damages up to the limit of the policy. Though this protection is readily available today, most notaries are unaware that it even exists.

The reasons for this lack of awareness vary, but it likely stems from the failure of notaries to realize that a wrongful notarization, however innocent, could result in personal financial disaster. As was previously discussed, most notaries labor under the misconception that the notary bond protects them. With this misperception in place, notaries do not perceive a need for other or additional protection, like E&O, and therefore do not look for it.

Geographical location may also play a part in the lack of E&O knowledge.⁶⁷ While notaries in urban areas like Chicago, New York or Los Angeles may be concerned about incidents of fraud and deception by document signers, their counterparts in the more rural areas are less likely to share that same suspicion.⁶⁸

Whether a notary performs duties in a corporate environment or at street level, can influence the notary's knowledge of E&O protection. A notary who received a commission at the request

66. Like most malpractice insurance policies, an E&O policy does not cover acts of intentional misconduct of by the notary. In such an instance, the injured party could only claim against the notary bond, thereby making a substantial bond limit even more critical for full recovery of damages.

67. Telephone Interview with Charles N. Faerber, Vice President of the Nat'l Notary Ass'n (Jan. 15, 1998).

68. Gnoffo, *supra* note 30, at 1089 (stating that few states have continuing education programs for notary publics).

and probably expense of the employer, and who performs all or most of the notarial functions in the office, is less likely to perceive the need for E&O. First, the notary notarizes the signature of individuals one interacts with on a daily basis, whose identity and integrity one has little doubt. Second, the notary may believe that the company's umbrella insurance policy covers notarizations in the office. Despite the fact that one notarizes in a seemingly secure environment, this notary can face the danger of an improper notarization and suffer dire financial consequences. Nothing is more illustrative of this point than the following Florida case described in an *American Notary* article by Derrick Huckleberry.⁶⁹

In this 1995 case, the notary was a secretary and her boss asked her to notarize his wife's signature on a document.⁷⁰ She took her boss' word that the signature was genuine, when in fact it was not.⁷¹ The wife denied ever signing the document and the case was settled for \$10,000.⁷² The notary bond in Florida at the time was a mere \$1,000, all of which the notary had to repay to the bonding company.⁷³ And the notary would have been personally liable for the remaining \$9,000 had she not had E&O, which paid the remaining amount for her.⁷⁴ Fortunately, this notary had the foresight to obtain E&O.⁷⁵

The cost of an E&O policy is reasonable and relatively small compared to the amount and duration of the coverage received. E&O notary policy limits now being sold typically range from \$10,000 to \$25,000. A \$15,000 policy can cost between \$45 to \$50 for a three-year term, while a \$25,000 policy can cost between \$55 to \$60 for the same term. The surety companies can further minimize the cost of the policy through the use of risk pools, thereby making a \$250,000 policy affordable. In addition, many employers will pay for the cost of the insurance since they want the benefit of a notary in the office.

The best time to get an E&O policy is at the onset of the notary commission.⁷⁶ Most major insurance companies offer E&O policies, usually through a separate surety company. Often overlooked is the fact that the same notary bonding companies that help notaries obtain their commission, also offer E&O. Unfortunately, they usually recommend E&O only to their commercial cli-

69. Derrick Huckleberry, *Errors and Omissions Insurance: The Ultimate Protection!*, AM. NOTARY MAG., 1st Quarter 1998, at 1.

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.*

75. Huckleberry, *supra* note 69, at 9.

76. It is possible for a notary to get E&O coverage even after their commission begins. The policy can be prorated to cover the remaining years in the notary's term.

ents like banks and currency exchanges. They believe that the higher exposure to the general public, and therefore increased instances of fraud or deception on a daily basis, necessitates the added protection. Nevertheless, even the occasional notary can fall prey to an unscrupulous customer, or worse yet, suffer a lapse in judgment, resulting in an improper notarization and possible financial ruin.

To apprise notaries of the need for E&O and to avoid unexpected financial loss, states should mandate E&O.⁷⁷ By mandating coverage, states will raise awareness that improper notarizations can cause dire financial consequences for notaries and associated parties. But more importantly, states will ensure that there is a mechanism in place to provide substantial recovery for injured parties. The victims of negligence will be protected from either insufficient recovery or wholly unrecoverable loss. An injured party would no longer have to rely on a small or non-existent bond, or expensive litigation, for recovery of damages. Instead, an E&O policy with a significant limit would be available to make the victim whole.

It must be said that, in spite of sound and prudent notarial practice, even the most careful notary can be victimized by fraud. In the litigious society we live in, no one, however removed from an action they may be, is safe from a lawsuit. Even if a notary followed all the proper and required procedures and is cleared of wrongdoing, the cost of proving that reasonable behavior alone could reach tens of thousands of dollars. With an E&O policy in place, the innocent notary will not face the unexpected financial drain of defending their actions in court. Even a substantial notary bond would not pay the costs of a legal defense.

Combining a significant notary bond with a large limit E&O policy will provide greater protection to the public for incidents of willful misconduct and negligence. If states raise bond limits to a higher level and mandate E&O coverage, victims of unscrupulous or irresponsible notarizations will have the means available for redress. In addition, innocent notaries will be protected from suffering financial loss due to lawsuits. But whether or not the above mechanisms are in place, notaries should continue to use their best judgment when notarizing, and use all available means to

77. In *Shavers v. Attorney General*, the court upheld the constitutionality of state mandated insurance. 267 N.W.2d 72, 77-79 (Mich. 1978). See generally *Gentile v. Altermatt*, 363 A.2d 1 (Conn. 1975); *Montgomery v. Daniels*, 340 N.E.2d 444 (N.Y. 1975); *Singer v. Shepperd*, 346 A.2d 897 (Pa. 1975); *Lasky v. State Farm Ins. Co.*, 296 So.2d 9 (Fla. 1974); *Opinion of the Justices* May 14, 1973, 304 A.2d 881 (N.H. 1973); *Grace v. Howlett*, 283 N.E.2d 474 (Ill. 1972); *Pinnick v. Cleary*, 271 N.E.2d 592 (Mass. 1971) (discussing the proposition of requiring no-fault automobile liability insurance). See also *Rybeck v. Rybeck*, 358 A.2d 828 (N.J. 1976); *Andrew v. State*, 233 S.E.2d 209 (Ga. 1977) (stating that mandated insurance is not violative of individual rights).

demonstrate that they used reasonable care when notarizing.

B. Maintenance of a Notary Journal

The notary's use of a journal is the best defense against wrongful notarization claims. Notaries must use reasonable care when performing their notarial duties. As discussed, reasonable care is that standard of care that a reasonable notary would use in the same circumstances.⁷⁸ The journal is the most reliable way to demonstrate the use of "reasonable care."

Through the habitual and detailed use of a notary journal, the notary can recall each and every notarial act requested, and exactly which forms of identification were relied upon to prove the identity of each signer. By using the journal each and every time the notary performs a service, the notary thereby creates the best defense against any claim of negligence, the fact that one used "reasonable care."

There is one additional facet to this defense which deserves mention at this time, and that is taking the document signer's thumbprint. The thumbprint is placed in the notary's journal along with the rest of the identification information already requested. Even though the thumbprint has been around since humans began walking the earth, its use by notaries as a tool against document signer fraud is relatively new.⁷⁹ This is unfortunate, as the thumbprint is truly the "ultimate identifier."⁸⁰ As part of the notary's arsenal of defenses against claims of negligence, it is the best evidence that a party personally appeared before the notary to have a document notarized. Should the notary later face an allegation of negligence in performing the notarial act requested, the thumbprint stands as "irrefutable evidence" that the notary used "reasonable care."⁸¹

CONCLUSION

Notary bonding has existed in the United States for almost two hundred years. It was recognized early in this country's history, that notarization was important. So important, that if a no-

78. Gnoffo, *supra* note 30, at 1063.

79. *A Journal Thumbprint: The Ultimate ID*, NAT'L NOTARY MAG., May 1996, at 9. California only as recently as 1996 made the taking of a right thumbprint in notary journals mandatory. CAL. GOV'T CODE, § 8206(a) (West 1992 & Supp. 1997). The wide spread use of the thumbprint as a fraud deterrent has been hampered for several reasons. When legislation was introduced in the late 1980's to make thumbprints in journals mandatory, the ACLU protested that such an act was an invasion of privacy. *A Journal Thumbprint: The Ultimate ID*, *supra*, at 10. Other objections were that taking the print was too messy and too expensive. *Id.*

80. *The Ultimate ID*, *supra* note 79, at 9.

81. *Id.*

tary was negligent or unscrupulous in performing the act, severe damages could result. The way to protect the public from suffering damages was to require that notaries be bonded in significant amounts. However, through the years, states have allowed this necessary coverage to become insignificant, even non-existent.

Efforts should be taken now to strengthen the protection of the notary bond, and further, to mandate substantial E&O to provide additional protection from loss. With this protection in place, the general public will be in a better position to recover damages as a result of an improper notarization, regardless of whether that notarization was willful or negligent. Combined with the use of a notary journal, notaries too will be able to defend themselves from claims of improper notarizations without expending large sums of their personal assets. Increasing bond limits and mandating substantial E&O would once again make notary liability protection effective and ensure that it remains effective as we approach the 21st century. But until these changes are made, and all parties relying on a notarization are truly protected, when it comes to notary bonding, "he that hateth suretyship is sure."