ICC PORTUGAL
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New Tools for International Trade

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Key Issues on Demand Guarantees / Analysis and Discussion

Agenda

International Practice and perspectives – URDG 2010 Revision

Different aspects and perspectives: issuing banks, customers and applicability by courts/legal aspects

The bank guarantee and how it works within the volatility of current international climate.

Introduction

In today's globalized economy, it's hard to imagine any business around the world without a guarantee.

We estimate the aggregate value of guarantees in the range of 100s of billions of USD, covering the obligations in all sectors of trade and industry including construction, commercial lending, corporate restructuring or structured finance all around the world.

A need for guarantee rules ?

Introduction

A French bank issues a guarantee to Cameroun with an expiry date October 30th, 2011 (Sunday)

When is the actual expiry i.e. latest day for presenting a claim, supposed the guarantee is subject to

- ☞ **Local law**
- ☞ **URDG 458**
- ☞ **URDG 758**

?

Introduction

☞ **local law**

open questions:

- which law is to be considered ?
- French Law or Cameroun Law or is the guarantee subject to a third law ?

☞ **URDG 458**

remain silent

☞ **URDG 758**

Article 25d:

next business day, Monday 31st October 2011

History

1978 URCG 325 were ICC‘s first attempt to standardize international guarantee practice

1992 URDG 458 as the second set of guarantee-rules are one of the most important instruments ever published by the ICC

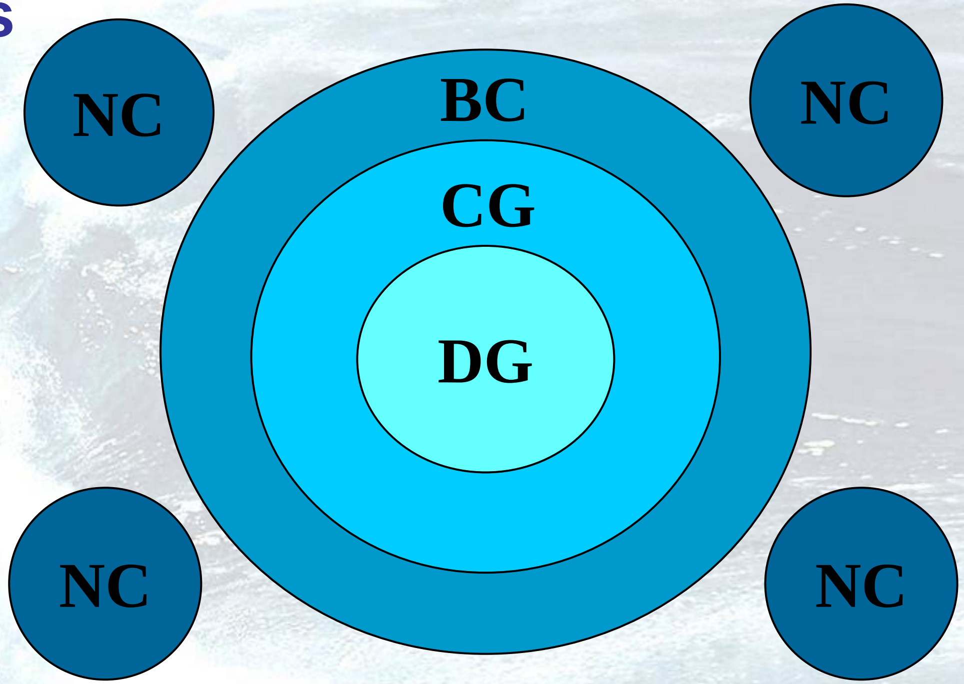
1994 ready-to-use model forms for most common types of guarantees published by ICC

2010 URDG 758 bringing the codified guarantee practice into the 21st century

The Road to URDG 758 - the Revision Process

Structure of the Revision

- Drafting Group
- Consulting Group (Guarantee Task Force)
- ICC Banking Commission
- National Committees



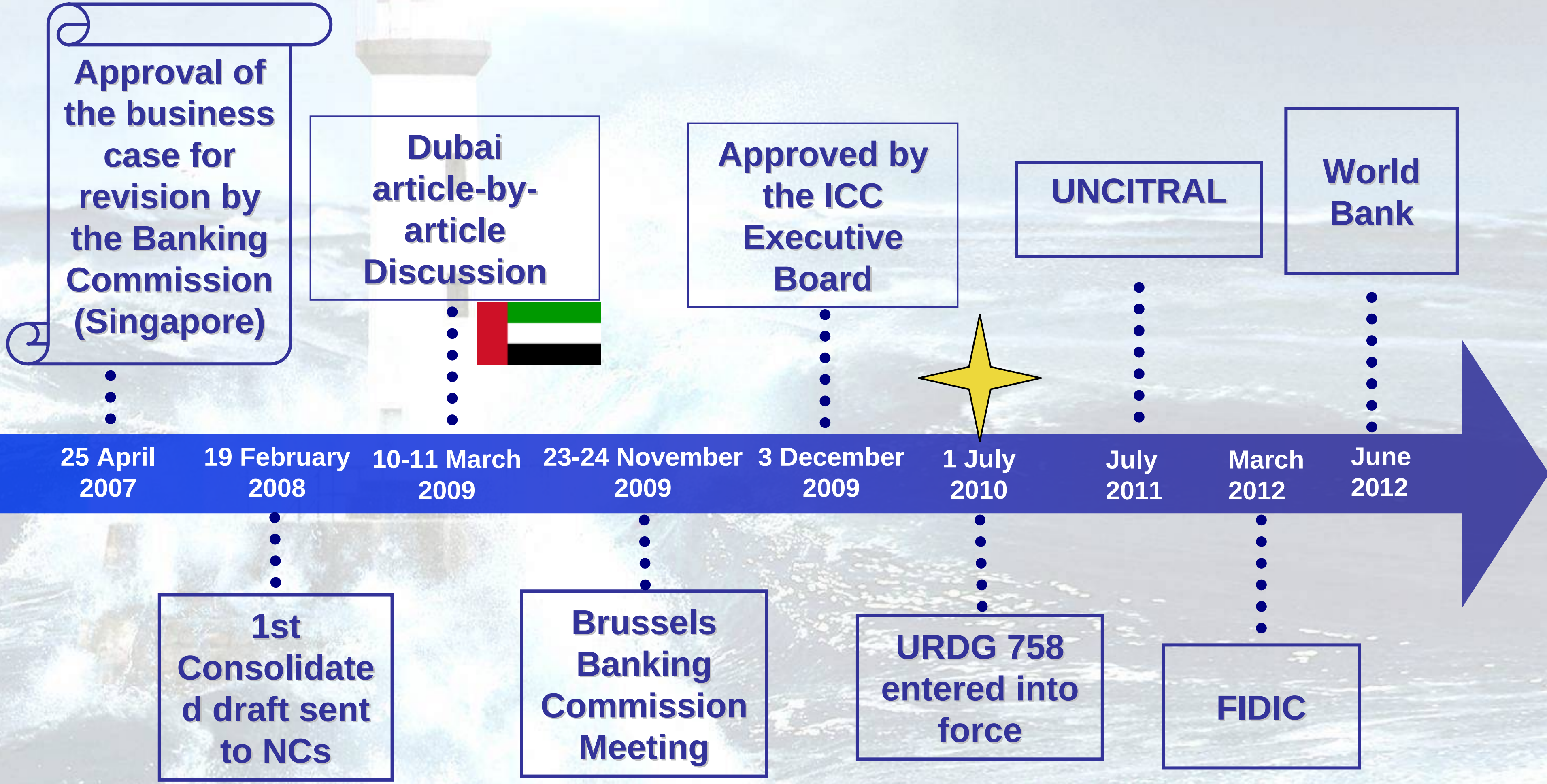
The new URDG : an overview

- **Methodology of the revision:**
  - **Revision time (processing of comments, discussion, drafting, compilation):**
    - **48 meeting days,**
    - **24 hours of confcalls,**
    - **25 working days (and nights !) of compilation of comments,**
    - **800 pages of compiled comments representing approx. 5,000 comments, each of which was thoroughly examined.**

Article by Article Discussion of the URDG 758 in Dubai, 10th and 11th of March 2009

possible, by other expeditious means.		The ICC … is of the view that further clarity or total removal of some vague wordings would be required in the document. For instance in Articles 9, 10E, 11A and 23D, the word 'expeditious means' was used and this may be misinterpreted.
b. The guarantee cannot be amended without the agreement of the beneficiary		264-273 There are no same sub-articles to cover counter guarantee amendments and counter guarantor liability for issued amendments and guarantor's rights to accept or rejects counter guarantee amendments.
		Line 264 The ….. NC once more suggests to exclude simple extensions or increase in amounts from the necessity of beneficiary's consent. So we suggest to add in
		Lines 264/265 Without the explanatory notes there may arise some misunderstanding to the meaning of " . . *except where the guarantee otherwise provides* . . "; the wording of subpara b) should clearly reflect the intention to cover automatic amendments already fixed in the original guarantee wording and not the possibility to deprive the beneficiary of his right to agree to/refuse an amendment We suggest a wording like: „….except where the **original** guarantee otherwise provides…"
		Line 264 We are of the opinion that it would add much more meaning to the article and help the banker if you added after **cannot be amended** additional two words **nor cancelled.**
except where the guarantee otherwise provides. Nevertheless the guarantor is		line 265: " *This agreement resp. consent by the beneficiary is not required in case a simple extension or an increase in amount is advised by the guarantor*." This would put an unnecessary burden of work on the banks and many beneficiaries just would refuse to react on an agreed and long expected amendment in their advantage. Also this is clearly against current market practice (international standard demand guarantee practice !) and the new URDG should reflect the actual market practice
		Lines 265 and 269 We suggest to write as follows: "guarantee or previous accepted amendments". This will avoid disputes when the related provision has not been stated in the guarantee but in an amendment.
		Line 265: Delete "except where the guarantee otherwise provides" as this is already covered by sub-article 1 (a).
		Lines 265 and 269: The phrase until the period of line 265 and the entire line 269 seem useless as they refer to a condition already provided under art. 1. **To be omitted**.
irrevocably bound by an amendment as from the time it issues the amendment		
and unless and until the beneficiary rejects the amendment.		
		Line 268: Proposal: "....by an amendment as from the time it leaves the control of the guarantor….." (pls see line 149)
c. Except where made in accordance with the terms of the guarantee, an		Line 269 The granting to the beneficiary of an unlimited period of time to decide whether he will accept the amendment or not puts the bank as well as the applicant/instructing party into a too long period of uncertainty concerning the exact status of the guarantee. Example: the guarantee is amended from a defined expiry to an unlimited validity: how long do the bank (and applicant/instructing party) have to wait until the liability may be booked off ?
		2. Lines 269-273 – we strongly believe that unlike in L/C which is often issued for a short term and usually is utilized, a beneficiary of a demand guarantee must notify whether he accepts or rejects an amendment. Let's take as an example an amendment which decreases the amount of the guarantee and in the same time extends its expiry date. In such case if no notification is made, the guarantor does not know whether the guarantee is valid after the original expiry date.
		Lines 269-273 Please substitute sub-article 11 (c) by: "The beneficiary under a guarantee or the guarantor under a counter-guarantee should give written notification of acceptance or rejection of an amendment to the guarantor or counter-guarantor, respectively, without delay." This provision mirroring sentence 2 of sub-article 10 (c) UCP 600 appears to be the best which one can do in guarantee business to achieve the desired clarity, unless one wants to imply, in the absence of any timely rejection, that any extension of the expiry or augmentation of amount will be deemed to have been accepted, which would, however, lead to unreasonable results and may legally not be upheld in many jurisdictions.

URDG Revision Roadmap



The Big Change

What makes life different when using the new Uniform Rules for Demand Guarantees URDG 758 ?

Can we really achieve major changes in the international guarantee practice or is it just another set of rules?

©Yes, we can !

Fundamental Changes
&
Key Provisions

URDG 758

The key issues:

- Definitions brought together in 1 article
- Bank vs party
- Presentation/demand
- Examination of documents
- Time limit – sanction clause
- Duty to inform
- Applicant/instructing party
- Guarantee/counter-guarantee /asymmetrical guarantees

URDG 758

The key issues II:

- Amendments
- Electronic presentation
- Extend or pay
- Force majeure
- Incomplete demand – partial demand – multiple
- demands
- No must (shall - should – may – recommended)
- Automatic termination
- Change of currency
- Art 33 transfer

URDG 758

Due to the limited time let me pick up the most important innovations/changes for the guarantee business compared to the former times prior to URDG 758

- Examination of documents - time limit - preclusion clause
- Applicant vs. Instructing party, bank vs. party
- Guarantee vs. counterguarantee
- (electronic) Presentation vs. Demand
- Extend or pay
- Force Majeure
- incomplete demand
- Automatic termination
- Change of currency
- Transfer vs. assignment

Examination of Documents – Time limits – Preclusion clause

Relevant Articles:

- **Article 19**
- **Article 20**
- **Article 24**

- **Article 19** contains – for the 1st time ever – standards how to deal with documents under a guarantee. Up to now the only set of rules giving instructions how to examine documents were the UCP.

- Local law as well as the old 458 remain silent to that question causing great uncertainty in the market

URDG 758

- **Article 20** limits the playing field for the guarantor by fixing the time limit for checking a demand under a guarantee to 5 business days following the day of presentation.

- Furthermore this article clearly and without any doubt states, that the guarantor has to effect payment when he determines that the demand is complying.

- **Article 24** contains a preclusion (sanction clause) for any guarantor not obeying to the rules by precluding this guarantor from refusing a demand as non complying.

Applicant - Instructing Party
Bank - Party

Relevant Articles: Article 2 (Definitions)

URDG 758 follows market practice and for the first time recognizes, that applicant and instructing party may be different entities.

applicant means the party indicated in the guarantee as having its obligation under the underlying relationship supported by the guarantee. The applicant may or may not be the instructing party;

instructing party means the party, ... who gives instructions to issue a guarantee . . . . and is responsible for indemnifying the guarantor . . . The instructing party may or may not be the applicant;

The Drafting Group did not want to limit the use of the URDG to bank guarantees only. URDG 758 are applicable to all sort of guarantees by using the neutral term “party” instead of “bank”

Guarantee vs. Counterguarantee
Asymmetrical Guarantees

Relevant Articles: Article 1, 2, 3, 5

Article 1 b) **deals with the so called asymmetrical guarantees:**

Where, at the request of a counter-guarantor, a demand guarantee is issued subject to the URDG, the counter-guarantee shall also be subject to the URDG, unless the counter-guarantee excludes the URDG. However, a demand guarantee does not become subject to the URDG merely because the counter-guarantee is subject to the URDG.

Article 2 **states, that the counterguarantor is not defined as instructing party !**

- instructing party means the party, other than the counter-guarantor, who gives instructions . . . . .

Guarantee vs. Counterguarantee Asymmetrical Guarantees

Article 3b)

- **brings the discussion about guarantee/counterguarantee to an end as one criticisms voiced (unfairly) against URDG 458 was that some of their provisions referred only to guarantees, but not to counterguarantees, leading to the impression that a number of rules seems to cover only guarantees but not counter-guarantees.**

- **Except where the context otherwise requires, a guarantee includes a counter-guarantee and any amendment to either, a guarantor includes a counter-guarantor, and a beneficiary includes the party in whose favour a counter-guarantee is issued.**

Guarantee vs. Counterguarantee Asymmetrical Guarantees

Article 5

- A counter-guarantee is by its nature independent of the guarantee, the underlying relationship, the application and any other counter-guarantee to which it relates, ...
  A reference in the counter-guarantee to the underlying relationship for the purpose of identifying it does not change the independent nature of the counter-guarantee. The undertaking of a counter-guarantor . . . . is not subject to claims or defences arising from any relationship other than a relationship between the counter-guarantor and the guarantor or other counter-guarantor to whom the counter-guarantee is issued.

(electronic) presentation vs. demand

Relevant Articles

- Article 2
- Article 14
- Article 15

For the first time, URDG 758 distinguish between a presentation and a demand

Article 2

- **presentation means the delivery of a document under a guarantee to the guarantor or the document so delivered. It includes a presentation other than for a demand, f. ex., a presentation for the purpose of triggering the expiry of the guarantee or a variation of its amount;**
- **demand means a signed document by the beneficiary demanding payment under a guarantee;**

(electronic) presentation vs. demand

Article 14 c)

- **Deals with the conditions of an electronic presentation**

Article 14 d)

- **Deals with the mode of transport in case of a paper presentation**

Article 14 e)

- **Contains a fall back rule in case the guarantee remains silent about electronic/paper presentation**

(electronic) presentation vs. demand

Article 15 a)

- stresses the necessity of the statement of breach to be presented under a guarantee and terminates the doubtful situation under 458 of the separateness of this statement or not

Article 15 b)

- regulates the statement of breach under a counterguarantee and contains similar conditions for the separateness of the statement as under 15 a)

Article 15 c)

- The statement of breach (art 15 a and b) can only by excluded by explicit wording, not by different conditions in the guarantee

Extend or pay

Relevant Articles: **Article 23**

- **Everyone dealing with guarantees, has to face - at least once – an extend or pay demand.**

- **Everybody knows about it and everybody feels uncomfortable with it due to a lack of regulation how to deal with such a request.**

- **In URDG 758 Article 23 there is now a clear and defined procedure to be followed in case of an extend or pay demand to reduce uncertainty in the market and stop misuse**

Force Majeure

<u>Relevant Article :</u> Article 26

- Local laws deal with Force Majeure quite differently, leaving the international community unsure of how to proceed in case of Force Majeure events.
- Most of the International Rules have put the burden of Force Majeure on the beneficiary, even in case the FM event happened with the bank or the counterpart.
- The URDG Drafting Group felt it was time for a fair balance of the risk of FM among all the parties involved in a guarantee transaction.
- Article 26 defines 6 situations, when FM may happen under a guarantee and provides a clear solution how to proceed in such a situation and spreads the risk of FM according to the different stages in the guarantee.

Incomplete Demand/Presentation

<u>Relevant Articles</u>: Article 14, 20

<u>Article 14</u>

- Again, URDG 758 follows actual market practice by accepting that in certain situation beneficiary may not be able to present all the documents together in one lot.
- Under URDG 458 there was only 1 way to handle such a demand: it was to be rejected as non-complying.
- The Drafting Group felt that this was unreasonably punishing the beneficiary and worked out a solution in accordance with the actual daily practice.

<u>Article 20</u>

- deals with the limited period of time for examining a demand in case of an incomplete presentation

Termination

Relevant Article: Article 25

Article 25 b)

- Deals with the necessity of beneficiary‘s explicit action when (partly) releasing a guarantee before the expiry date.

Article 25 c)

- contains an automatic termination clause in case the guarantee states neither an expiry date nor an expiry event.
- This was seen necessary to relieve the burden of the applicants with unreturned guarantees for transactions which have been already fulfilled and closed.

Change of Currency

Relevant Article:

Article 21

- Especially with longlasting guarantees, there might be a situation where payment under the initial currency of the guarantee becomes impossible or illegal.

- There was a need in the market to find a solution for such guarantees and provide a clear regulation how to handle such a payment request.

- It is important to point out, that this only becomes applicable, in case such a situation occurs after the issuance of the guarantee.
  This rule is not be misused by the parties to gain advantages in exchange rates or similar.

Transfer vs. assignment of proceeds

Relevant Article:

Article 33

Before: in many local legislations not regulated/ not possible; URDG 458 only allow assignment of proceeds

-**When starting the revision the market signalized a need for a transfer rule.**

-**Especially in aircraft or ship building contracts, the need for a transfer of rights is demanded quite often.**

-**Article 33 allows the transfer of rights under a guarantee under certain conditions and also deals with the assignment of proceeds**

International Uptake

International Uptake

It would take too much time to talk about countries in detail, so I will only concentrate on the international / supranational organisations.

- UN Endorsement

- World Bank

- FIDIC

UNCITRAL

What is the UNCITRAL ?

The **United Nations Commission on International Trade Law** (UNCITRAL) was established by the United Nations General Assembly by its Resolution 2205 (XXI) of 17 December 1966 "to promote the progressive harmonization and unification of international trade law".

- UNCITRAL carries out its work at annual sessions held alternately in New York City and Vienna.

When world trade began to expand dramatically in the 1960s, national governments began to realize the need for a global set of standards and rules to harmonize national and regional regulations, which until then governed international trade.

UNCITRAL

In UNCITRAL's spring 2011 session the ICC presented the URDG 758 to the plenum and after a short discussion UNCITRAL voted - without a dissenting vote - for the endorsement of the URDG 758.

This achievement was quite exceptional due to 2 reasons:

1) the endorsement was given only 1 year after introduction of the new URDG 758 and

2) the endorsement was given already in the first session UNCITRAL dealt with these rules.

UNCITRAL

249. Taking note of the significant revisions made to the previous version of the Uniform Rules and their usefulness in facilitating international trade, the Commission, at its 937th meeting, on 5 July 2011, agreed to recommend the use of the Uniform Rules in international trade and adopted the following decision:

***The United Nations Commission on International Trade Law*, **

- ***Expressing* its appreciation to the International Chamber of Commerce for transmitting to it the revised text of the Uniform Rules for Demand Guarantees, which was approved by the Executive Board of the International Chamber of Commerce on 3 December 2009, with effect from 1 July 2010,**

- ***Congratulating* the International Chamber of Commerce on having made a further contribution to the facilitation of international trade by making its rules on demand guarantees clearer, more precise and more comprehensive while including innovative features reflecting recent practices, *- Noting* that the Uniform Rules for Demand Guarantees constitute a valuable contribution to the facilitation of international trade,**

- ***Commends* the use of the 2010 revision of the Uniform Rules for Demand Guarantees, as appropriate, in transactions involving demand guarantees.**

WORLD BANK

- Large international organisations like the world bank do not change their standards immediately when an innovation is introduced to the market.
- Georges Affaki has invested much time and did a great job over the past months
- In June 2012 we received the information that the World Bank now adapted their standard documentation to the new URDG 758.
- This is a very important signal to the public sector all around the globe.

FIDIC

The acronym FIDIC stands for *Fédération Internationale Des Ingénieurs-Conseils*, French for the *International Federation of Consulting Engineers*. The fact that the organisation has a French title bears testimony to its foundation in 1913 by three countries each wholly or partly francophone. The founding member countries of the FIDIC were Belgium, France and Switzerland.

- Located at the World Trade Center in Geneva, Switzerland, FIDIC aims to represent globally the consulting engineering industry by promoting the business interests of firms supplying technology-based intellectual services for the built and natural environment. Run mostly by volunteers, FIDIC is well known in the consulting engineering industry for its work in defining Conditions of Contract for the Construction Industry worldwide.
- Companies and organizations belonging to FIDIC national member associations are encouraged to announce themselves as FIDIC members and use the FIDIC logo. The use of the logo is strictly controlled, and all FIDIC products and services are protected by the FIDIC trademark.

FIDIC

- had approved the old URDG 458 a couple of years ago and was interested in the progress of the 758 right from the beginning.

- midth of March 2012 FIDIC has now approved the new 758 and has adapted its documentation and model forms to the URDG 758.

International Uptake

An <u>internal</u> survey by the Guarantee Task Force has been started and first results show that

- The number of guarantees issued under 758 has increased significantly compared to former 458 and is still rising.
- There are vast differences among countries, some apply the 758 as a standard, others only upon request by customer, therefore the percentage of 758 guarantee may range from close to 100% down to 15-20%.
- The acceptance of the URDG 758 is very high with private companies, but a bit hesitant till reluctant with state owned enterprises or public authorities.

No Problems so far !

Even as important as the acceptance in the various countries is the fact, that up to now we have not been reported any problem/conflict with local law and we have not been reported any single 758 guarantee brought into court.

This is a clear evidence, that the 758 have reached their goal to be clearer, more precise and more comprehensive than any set of guarantee-rules before.

The bank guarantee and how it works within the volatility of current international climate

Outlook

The bank guarantee is not an innovative instrument, it has been on the market for decades, it is one of the so called traditional banking products.
This is exactly the reason why now - in the time of financial / economic crisis - this instrument is more successful than ever.
Global markets are very nervous and everybody aims at security, even for small amount and short tenor business.
So it is not astonishing, that the number of guarantees issued reach new records every year although in some regions the economy is still in troubles.

Outlook

The number of claims has risen during the first years of the crisis (2009/2010) but are back to normal in most economic regions throughout the world.

Guarantees have been and still are a low-risk instrument, when it comes to terms of actual loss.

According to the figures published in the Trade Default Register the actual loss in guarantees is practically zero (exactly 0,0007 %).

Mistrust is still in the reign in global economy and even after the crisis it will take years until trust will be back in the market, so guarantees will still be very much in demand in the forthcoming years.

Outlook

How can URDG 758 support the recovery of the global economy ?

The Uniform Rules for Demand Guarantees have been developed to level the playing field amongst guarantee parties regardless of the legal, economic or social system in which they operate and ensure a fair balance of interests.
In the wake of the most severe economic crisis that has ever hit trade finance, certainty, predictability and transparency is what the world needs.

The new rules, URDG 758, offer that.

The Future


ICC Uniform Rules for Demand Guarantees
Including Model Forms
2010 REVISION
URDG 758
ICC:s Regler för Demandgarantier
Garanzie a Prima Richiesta
Garantias a Pedido
REVISÃO 2010
ICC Portugal
ICC Uniform Rules for Demand Guarantees URDG 758 Including Model Forms
ICC Einheitliche Richtlinien für auf Anfordern zahlbare Garantien URDG 758
englisch-deutsche Ausgabe
ICC Deutschland
Yhdenmukaiset demand -takuusäännöt
ICC Reglas Uniformes Relativas a las Garantías a Primer Requerimiento
Incluye formularios
REVISIÓN 2010
Гарантии по требованию
infotropic
ICC Jednotná pravidla pro Záruky vyplatitelné na požádání
VČETNĚ VZORŮ
REVIZE 2010
ICC Česká republika

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