



Branch of Activity
USA CAPITAL EURO LLC

USA CAPITAL EURO LLC

826 Frederick Reid St.E, Fort Myers, Lehigh Acres FL33974

UNITED STATES OF AMERICA

Tel: +1.239.258.9891 Fax: +1.239.264.9804

e-mail: usakapital@yahoo.com

Bank Guarantees

10th revised edition, 2013

Published in German, English and French

© CREDIT SUISSE (copy)

Bank Guarantees as Protection against Non-performance and Non-payment

In their trade dealings, buyers and sellers often face similar problems. A seller might find it difficult to assess the buyer's willingness and ability to pay, while the buyer might not be sure that the seller genuinely intends to perform its side of the contract or has the necessary financial and technical resources to do so. Just as the buyer needs protection against non-performance, so the seller will want to minimize or insure against the risk of non-payment. Documentary credits are generally used in such cases.

Further information on this type of payment instrument can be found in our brochure titled "Documentary Credits – Documentary Collections, Greater Security in International Trading." Yet

various other forms of bank guarantees are available. The term "bank guarantee" has no precise definition, particularly in international law. Some use the term exclusively to describe a transaction in which one party makes an independent guarantee commitment in respect of another party's liabilities, regardless of the latter's form and enforceability. Others describe as guarantees all transactions in which security is offered – from letters of comfort (which often are morally binding at most) to surety bonds and abstract payment undertakings. The custom in international trade is to have undertakings that are payable on first demand and that are legally separate from the underlying transaction.

The common element in all these arrangements is that the guarantor undertakes to be answerable for the payment of a debt or the fulfillment of an obligation in the event of default by the party that is primarily responsible for it. Thus the basic function of a bank guarantee is to provide security.

The main difference between a bank guarantee and a documentary credit is that the latter also functions as a means of payment.

Bank guarantees are governed almost exclusively by the law of the country of domicile of the bank that issues the guarantee to the

A. Overview and Basis in Law

In practice, we distinguish between the following different forms of bank guarantee (also referred to as "sureties"):

Accessorial obligations ■ surety bonds (governed by the Swiss Code of Obligations [SCO]) – simple suretyship (SCO 495) – joint and several suretyship (SCO 496).

Nonaccessorial (abstract) obligations ■ guarantees ■ promise to pay (conditional or unconditional order confirmations) ■ standby letters of credit, according to the rules laid down in – International Standby Practices (ISP98), or – Uniform Customs and Practice for Documentary Credits (UCP).

All of these forms may be used as protection against either nonperformance or nonpayment. While the specific structure of surety bonds and order confirmations under Swiss law means that they can hardly ever be used internationally, the other instruments can be used around the world, subject to country-specific customs.

Where a guarantee beneficiary is unable to accept the guarantee liability in its favor from what it considers to be a foreign bank, the common international device of an indirect guarantee can be used instead. As a rule, the confirmation or countersignature of a guarantee by another bank should be avoided.

Banks around the world tend to stipulate their own wording in accordance with local practices and the local legal background. In 1992, the International Chamber of Commerce (ICC) in Paris issued new regulations titled "ICC Uniform Rules for Demand Guarantees" (URDG) in an attempt to harmonize these different wordings and customs (see Section 3 below and Appendix).

Standby letters of credit were created in response to banking legislation in the US. Where used, they qualify as a guarantee.

1

beneficiary. This means that the legal position must be studied in each case. Specialists at Swiss banks keep themselves informed of developments in the countries served by Swiss exporters and will be happy to provide information on specific problems. The following presentation is based primarily on Swiss law and practice.

Every declaration that is designated a "bank guarantee" must be examined carefully to ascertain its legal significance and implications. A particularly clear distinction must be made between a surety bond and an abstract payment undertaking.

The specialists at the CREDIT SUISSE AG Trade Finance Service Center will be pleased to advise you about how the various instruments can be used, as well as the benefits they offer your business.

2

Contents A. Overview and Basis in Law 51. Surety Bonds 52. Guarantees 63. ICC Uniform Rules for Demand Guarantees 84. Conditional and Unconditional Order Confirmations ("Promise to Pay") 85. Standby Letters of Credit 9 B. Effects of Bank Guarantees 10 C. Issuance of a Bank Guarantee 11 D. Content of a Bank Guarantee Payable on Demand 14 E. Claiming under a Bank Guarantee 151. Justified Claims 152. Unjustified Claims 15 F. Main Types of Guarantees 161. Tender Bond (Bid Bond) 162. Performance and Warranty Bonds 183. Advance Payment Guarantee 21 G. Other Types of Guarantees 23 H. Consortium Operations 25 I. International Standby Practices (ISP98) 27 K. Costs 29 L. Glossary 31 Appendix 37 ■ The International Standby Practices – ISP98 39 ■ Index 48 ■ The Uniform Rules for Demand Guarantees (Attachment) 5 Overview and Basis in Law

They were originally governed only by UCP, but the new ISP98 guidelines issued by the ICC specifically for standby letters of credit have been used increasingly since January 1, 1999 (see Section 5 below and Appendix).

1. Surety Bonds

Surety bonds are governed in law by Art. 492 et seq. of the SCO. They establish an accessorial obligation to the creditor, i.e. one that relies on the existence of the primary debtor's obligation and is limited to the substance and scope of that obligation. As such, the bond becomes void if the underlying debt is extinguished for any reason (e.g. through payment). In the event of a claim, the guarantor must use all of the defenses against the creditor that are available to the primary debtor, provided they do not relate to the latter's insolvency (Art. 502, para. 1 SCO).

In practice, Swiss legislation means that a bank acting as a guarantor will generally meet a claim from the creditor only if expressly authorized to do so by the principal.

In the case of "simple suretyship" (Art. 495 SCO), the guarantor is obliged to make payment only if the primary debtor becomes insolvent or has been granted a period of time in which to restructure their debts (the law also lists a number of less important cases). In practice, simple suretyship is rare. Only in the case of "joint and several suretyship" can the guarantor be claimed against prior to the primary debtor (Art. 496 SCO).

Surety bonds are used almost exclusively for securing the claims of domestic creditors (see Figure 2, page 7). 6 Overview and Basis in Law

2. Guarantees

Guarantees (see Figure 1) create a nonaccessorial, abstract obligation to the beneficiary. Unlike suretyship, they are not governed by explicit provisions in law. According to current opinion and practice, guarantees are rooted in the following legal provisions: ■ contract against a third party (Art. 111 SCO) ■ an assumed order (Art. 466 et seq. SCO).

The distinction between a surety bond and a guarantee depends on whether or not the obligation is accessorial. If it is, it constitutes a surety bond; otherwise it is a guarantee (see ruling by the Swiss Federal Supreme Court [Bundesgerichtsentscheid, BGE] 113 II 437 [1987]).

The guarantor remains liable even if the underlying obligation is extinguished for any reason. The guarantor must pay upon demand, without making any objection or invoking any defense. On receiving a claim, the guarantor can therefore merely check that it has been validly made, i.e. that the formal conditions laid down in the wording of the guarantee have been met. The guarantor will not examine the material justification for the claim. If the formal conditions as set out in the guarantee are satisfied, the guarantor is obliged to make payment, regardless of whether or not the principal believes the payment is due.

This form of guarantee places the beneficiary in a very strong legal position. The beneficiary can demand immediate payment, and the guarantor and principal have no right to raise any objections or present any defense on the strength of the underlying transaction. Thus the beneficiary is relieved not only of the risk of the principal becoming insolvent but also of the risk of having to enforce a claim through the courts. As in the case of documentary credits, the rule is “pay first, sue later.”

The extract in Figure 1 clearly shows that when a claim is made under this type of guarantee, the principal is powerless to obstruct it.

Figure 1

We, CREDIT SUISSE AG, CH-8070 Zurich, Switzerland, hereby irrevocably guarantee that we shall pay you, upon first request, irrespective of the validity and legal effect of the aforementioned agreement and waiving any objections or defense arising from the same, any amount up to a maximum of CHF 50,000.00 (fifty thousand Swiss francs)

The following section describes only the various forms of bank guarantees that dominate transactions with foreign countries.⁷ Overview and Basis in Law Surety bond The guarantor's obligation goes only as far as that of the principal debtor. As a rule, the guarantor does not make payment unless proof is provided that the principal debtor has failed to fulfill the terms of the contract with the creditor. The process for a surety bond to ensure performance: Guarantee The guarantor's obligation is independent of the existence or continuation of a contractual relationship between the principal and the beneficiary. The process for a guarantee to ensure performance: Surety bond Creditor (buyer) Guarantor Principal debtor (seller) Contract Beneficiary (importer, buyer) Guarantor Principal (exporter, seller) Contract Guarantee Surety Bond/Guarantee (Figure 2) 8 Overview and Basis in Law

3. ICC Uniform Rules for Demand Guarantees

In 1992, the International Chamber of Commerce (ICC) in Paris issued a new set of regulations titled “ICC Uniform Rules for Demand Guarantees” (ICC Publication no. 458). The new rules are the product of a joint working group of representatives of the Commission on International Commercial Practice and the Commission on Banking Technique and Practice. The rules cover all types of guarantees and other payment undertakings under the terms of which the guarantor is obliged to make payment on presentation of a written demand and any other documents specified in the guarantee. While still applicable, the previous “ICC Uniform Rules for Contract Guarantees” (ICC Publication no. 325) published in 1978 failed to gain general acceptance owing to confusion about the scope of their application. The regulations issued in 1992 largely correspond to current international practice and also take appropriate account of the interests of the various parties involved.

Demand guarantees may be subjected to the new rules by including a simple statement to this effect in the guarantee agreement. To qualify as a demand guarantee, the guarantee document must not stipulate any conditions for payment other than the presentation of a written demand and any other specified documents. In particular, the guarantor must not be required to decide whether or not the beneficiary and principal have fulfilled their contractual obligations. Restrictions on entry into force – such as the receipt of a down payment – may nonetheless be imposed.

The rules are intended to balance the interests of the beneficiary with the principal's wish for protection against unjustified claims. The beneficiary wishes to protect itself against the risk that the principal will not fulfill its contractual obligations. A demand guarantee provides quick, easy access to a guaranteed sum of money if these obligations are not met. However, for the sake of equity and fair dealing, the rules contain a provision to the effect that any demand should be accompanied by a statement by the beneficiary explaining in what respect the principal is in default. This is intended as a safeguard against unfair calling. It should be emphasized that the rules do not in any way prejudice national legislation with respect to fraudulent claims.

The rules are currently being revised. URDG 458 and our sample text based on the rules are provided in the Appendix.

4. Conditional and Unconditional Order Confirmations (“Promise to Pay”)

As is the case with a documentary credit or a demand guarantee, under Art. 468 SCO an order confirmation constitutes a nonaccessorial payment undertaking. A client (“instructing party”) issues an order to a bank (“instructed party”) either to pay a fixed sum to a beneficiary (“recipient”) on a certain date (unconditional order) or to make a payment to the beneficiary after certain conditions have been fulfilled (conditional order). Examples of such conditions include the submission of documents or declarations by the beneficiary or by third parties. Similar to a documentary credit, an order is therefore an indirect form of payment.

However, the order does not place the bank under any obligation until it has declared to the beneficiary that it accepts the order without reservation. Once this declaration of acceptance has been made, the undertaking may not be further changed or canceled without the consent of the beneficiary. 9 Overview and Basis in Law

5. Standby Letters of Credit

Standby letters of credit originated in the U.S., where old banking legislation forbade commercial banks to issue contingent liabilities in the form of guarantees (bonds) from the late 1930s onward. Documentary credits were therefore used for this purpose. Subject to the Uniform Customs and Practice for Documentary Credits (UCP), they were then modified into standby letters of credit. Standby letters of credit are guarantee-like instruments to secure a claim and may, in principle, apply anywhere that a guarantee would be used. For example, they may be used to guarantee the following types of performance and payment: ■ payment of term bills of exchange ■ repayment of bank loans and advance payments ■ payment for goods delivered ■ contract fulfillment of all types, etc.

Like guarantees, standby letters of credit are payable on demand and no defense against the claim is permitted. As such, they constitute abstract commitments that are independent of the underlying transaction. To trigger payment, the documents stipulated in the wording of the standby letter of credit must be submitted in accordance with the applicable regulations. Alongside UCP, ISP98 (International Standby Practices) has been in force since January 1, 1999. This set of rules was developed and

approved specifically for standby letters of credit by the International Chamber of Commerce (ICC). In practice, use of ISP98 is now becoming increasingly widespread (see Appendix).¹⁰

Effects of Bank Guarantees

B. Effects of Bank Guarantees

The guarantor bank is not obliged to supply goods or perform work on the principal's behalf. It will not, for instance, build an airport itself if its client fails to do so, neither will it manufacture or supply looms or chemicals if its client falls behind with deliveries. The bank's commitment is solely a financial one, as its obligation as a guarantor is limited to the payment of a sum of money as a substitute for performance that has not been rendered.

How, then, does a bank guarantee provide protection against nonperformance? In three ways:

Legitimation:

A bank guarantee testifies to the principal's ability to carry out the contract. Since the issuance of a guarantee constitutes an irrevocable payment undertaking, a bank will not enter into such a commitment without first thoroughly examining the principal's financial status and technical capability.

Motivation:

The principal stands to lose the guarantee amount if it fails to fulfill the contract terms. This is a strong incentive to complete the contract, even if the transaction has lost its appeal in the meantime.

Compensation:

If the principal fails to fulfill its obligations, the buyer is entitled to demand payment of the guarantee sum, which will compensate fully or partly for the financial consequences of the breach of C.

Issuance of a Bank Guarantee

Bank guarantees are "tailor-made" transactions. A Swiss exporter who is asked to provide a guarantee would therefore be well

The bank will draft the guarantee in such a way as to protect the principal's interests within the framework determined by the wishes of the beneficiary and the relevant regulations in the beneficiary's country. The maximum liability (including principal, interest, charges, etc.) must be stated. It is also very important to specify a precise expiry date. Other provisions cover the procedure for making any claim.

Depending on the instructions communicated by the principal (exporter, seller) at the request of the importer (beneficiary), the Swiss bank will either issue the guarantee itself (direct guarantee) or instruct a correspondent bank in the importer's country to do so on its behalf (indirect guarantee). (See flow chart in Figure 3, page 14.)

A direct guarantee gives the principal more scope to influence the wording of the guarantee in accordance with its particular requirements.

advised to discuss the matter first with a specialist who knows about the various national regulations and practices in different importing countries. In many cases, it is the beneficiary who decides whether the instrument to be used should be a guarantee or a standby letter of credit. The specialist will then draft a guarantee that reflects the particular circumstances of the transaction and submit it to the client for approval. At the same time, the client will be asked to sign a letter of indemnity which states inter alia that the bank may charge the client's account if a claim is made under the guarantee.

Even so, the second approach is more often adopted because many beneficiaries prefer to have an undertaking from a bank in their own country. Claims under the guarantee can then be made to the correspondent bank, and this has a number of practical and legal advantages. For instance, there is less risk of the beneficiary's claim being "lost in the mail," and payment cannot be obstructed by exchange controls or restrictions on the transfer of funds. Moreover, this approach circumvents possible legal uncertainties in the exporter's country with regard to the enforcement of claims under the guarantee.¹² Issuance of a Bank Guarantee Name

CREDIT SUISSE AG
Trade Finance Service Center, Guarantees / Our ref.:

(hereinafter: the "Applicant")

Name of company:
Data of company:
Telephone:
Fax:

contract.11
Issuance of a Bank Guarantee

**For more information contact MGRM, mr. Vladimir Gil
USA CAPITAL EURO LLC ® / Invest, Expo, Broker, Lawyers, Sales, Financial Engineering**

Any information given herewith is obtained from Owner/Dealer or sources we consider reliable.
The information supplied herein is for informational purposes only and shall not constitute a warranty or assurance that said information is correct. NML-41507-B 02/14



e-mail: usakapital@yahoo.com



e-mail: usacapital@investexpo.org



Tel: +1 239 258 98 91 Fax: +1 239 246 98 04 copying is prohibited Skype: expo.invest (copying is prohibited)

