

Guarantees

A question of compensation

Doing business with companies abroad is not the same as doing business with Danish companies. Distance alone can make a difference. Both parties can meet with unpleasant surprises, which can lead to the contract they entered into being impossible to uphold.

For this reason, one of the parties will often demand some form of security – e.g. an international guarantee, which ensures you and your trading partner an agreed compensation in the event of a breach of contract.

It is difficult to get out of a contract once it has been signed. Therefore all conditions must be considered and clearly defined before you commit yourself.

Things valid in Denmark are not necessarily valid abroad. For example, in some countries it is quite normal not to respect the expiry date of a guarantee. There may also be a legal requirement that the guarantee must be issued by a local bank, against Danske Bank's counter-guarantee. It is therefore important that you know the situation in the countries you deal with.

We recommend that you ask us for advice.

Negotiating contracts

In our experience, the order of the individual bank transactions is of great importance in projects abroad.

Both exporter and importer want to insure themselves as well as possible.

Example:

The exporter requires the issue of a documentary credit to ensure payment for the goods.

At the same time the importer requires the issue of a bank guarantee to ensure the carrying out of the work/delivery of the goods.

Which should be issued first – documentary credit or guarantee?

A few Danish exporters have experienced that the foreign importer has claimed under the issued bank guarantee before the exporter has even seen the documentary credit.

You can avoid such problems if, for example the guarantee is included as one of the documents required in the documentary credit.

Danske Bank has the expertise

Danske Bank has a lot of experience with international trade, including international guarantees.

We are in daily contact with banks all over the world. Through our global correspondent net we are able to execute guarantees in any country in the world. Therefore Danske Bank has considerable know-how and many years experience in handling guarantee business.

The parties in a guarantee relationship

1. Guarantee applicant - The one who orders the guarantee, is called the guarantee applicant or the applicant
2. Guarantor - The bank, which guarantees that the agreed amount of compensation can be paid out, if the applicant defaults on the agreement, is called the guarantor
3. Guarantee beneficiary - The one, in whose favour the guarantee is issued, is called the guarantee beneficiary or the beneficiary

Types of Guarantee

The most used types of guarantee are as follows:

Bid Bond

A bid bond ensures that the agreed compensation is paid, if the exporter defaults on his tender obligations under an international contract. An exporter's tender will often not even be considered without such a guarantee.

Performance Bond

A performance bond ensures that the agreed compensation will be paid, if the exporter does not fulfil his obligations to the importer. This can be a question of e.g. delivery or functional or quality obligations. This guarantee typically amounts to 10-20% of the contract value.

Advance Payment Bond

An advance payment bond is used primarily in connection with contracts for substantial capital goods, where it is agreed that the importer will pay part of the purchase amount in advance, often between 10 and 30%.

The advance payment bond ensures that the exporter will pay back this advance payment, if he does not fulfil his contractual obligations.

Retention Bond

A retention bond is used where it has been agreed, that the remaining amount, which would be retained during the guarantee period, e.g. 12 months after delivery of the goods, will be paid out immediately.

The retention bond ensures that the exporter will pay back this remaining amount if he does not fulfil his contractual obligations.

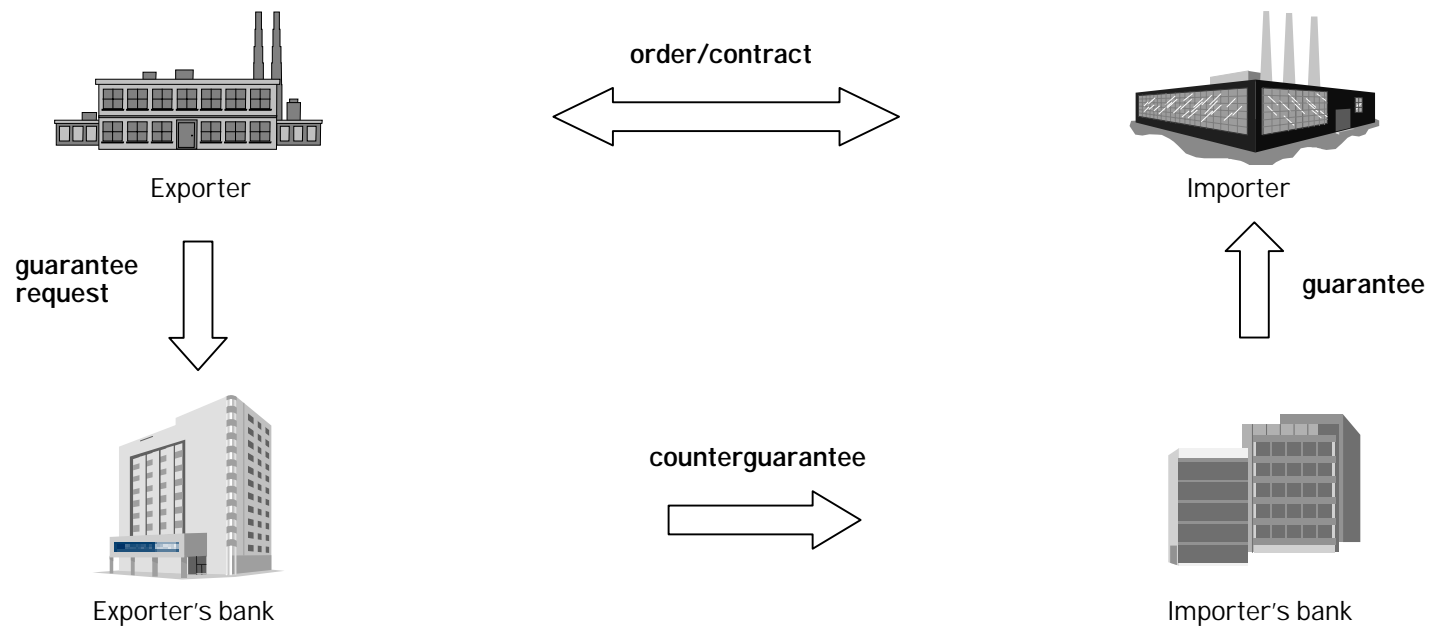
Payment Guarantee

A payment guarantee ensures that the importer fulfils his payment obligations to the exporter.

A payment guarantee can be issued as an endorsement on a Bill of Exchange, a so-called aval endorsement.

Counter guarantees

In certain countries it is a legal requirement that a guarantee must be issued by a local bank against a counter guarantee from Danske Bank. Such a guarantee is always payable on first demand. Below you can see an example of the use of a counter guarantee in export trading.



Payment under guarantees

It is important that you and your trading partner agree on the conditions, under which any claim will be paid.

Must the amount claimed just be paid against a simple declaration of default (demand guarantee) or must the bank wait for an agreement between the parties – alternatively a judicial decision (conditional guarantee)?

It is necessary that this be clearly shown in the guarantee text, so that all parties understand when the claim must be paid.

In our experience, certain countries do not accept conditional guarantees.