BETTER SECURED IN DOMESTIC AND FOREIGN BUSINESS.

The bank guarantee.

Bank Austria
Corporate Banking

Member of UniCredit Group

SAFEGUARDING PERFORMANCE AND PAYMENT OBLIGATIONS WITH A BANK GUARANTEE.

For domestic and cross-border transactions.

Today's business environment is unthinkable without the bank guarantee, a security instrument which is used in both domestic and cross-border transactions.

Whenever there is a need to secure a transaction within a legal framework, a bank guarantee may be used.

Bank Austria offers you a professional service which is essential in this field, which has exacting legal requirements.

What is a bank guarantee?

A bank guarantee is the irrevocable, autonomous obligation of a bank (= guarantor) towards a specified beneficiary, to vouch for the failure of an agreed performance of its client (= instructing party) by means of transfer of a stipulated sum to the beneficiary on his written demand (= claim for payment).

The characteristics of a bank guarantee.

- Irrevocability.
  A bank guarantee which has already been issued cannot be revoked; further, an amendment of the guarantee conditions is only possible with the consent of all parties to the guarantee.
- Abstract/Non accessory.
  This means that a guarantee is completely autonomous from the underlying contract/business.
  Objections from the underlying transaction (for instance in case of a claim for payment) may therefore not be raised.

Why a bank guarantee?

When partners conclude a contract, it may be difficult for them to assess whether the other party is able or willing to meet its contractual obligations. Such a risk of non-performance may be safeguarded by a bank guarantee.

What does the bank do?

It issues on behalf of its client (= the party whose contractual obligations are to be ensured) its guarantee in favour of the beneficiary (= the party who wants to be protected).

In case the latter demands the payment of the guarantee amount (which requires strict compliance with the terms and conditions of the guarantee) the bank is obliged to effect payment.

Who may be a beneficiary?

The bank may issue guarantees in favour of

- domestic beneficiaries (-> domestic guarantee)
  or
- foreign beneficiaries (-> foreign guarantee).

Direct/indirect guarantees.

A **"direct"** guarantee is issued by the instructing party's bank direct to the beneficiary. Therefore a direct legal relationship is formed between that bank and the beneficiary. For the instructing party the advantage of this arrangement lies in lower costs as well as in the fact that the guarantee (if established by an Austrian bank) is governed by Austrian law.

One cannot, however, always choose a direct guarantee, since beneficiaries occasionally prefer guarantees from a local bank. Moreover, existing customs or legal regulations in some countries allow only the acceptance of guarantees issued by local banks. Therefore the instructing party's bank has to ask the local bank in the beneficiary's country to issue the guarantee. This is known as an **indirect guarantee,** in which there is no direct legal relationship between the instructing party's bank and the beneficiary. This guarantee is governed by the laws of the country of the bank issuing the guarantee. Commission and charges of both banks are borne by the instructing party.

Advised guarantee.

That is a guarantee issued by another bank in favour of one of our clients, which we pass on to the latter without any obligation on our part.

A practical example:

Messrs Vidonni Gmbh (Vienna) as sellers concluded a contract with Messrs Smaller Business Gmbh (Munich, buyer). Under this contract Messrs Vidonni Gmbh undertook to supply 3 machines to their German customer by May 2 and to effect repairs which might become necessary during the warranty period. This transaction is the first one between the two parties, so that the German buyer cannot be sure whether the Austrian firm is willing and able to fulfill its maintenance obligations.
The buyer is also aware of the fact that it may become difficult and tedious either to prompt Messrs Vidonni to meet their contractual obligations, or – if he does not succeed – to achieve appropriate compensation by taking legal action.
Therefore the buyer insists on a condition in the contract according to which Messrs Vidonni have to have a bank guarantee issued in his favour. This enables him to demand payment under the bank guarantee in the event of Messrs Vidonni's not fulfilling their contractual obligations.

Types of guarantee.

The name of a guarantee is deduced from the nature of the obligations to be secured by it. In principle it is possible to issue guarantees in connection with every kind of transaction that does not contravene law.
The most common bank guarantees are:

If the instructing party is supplier:

- **Bid bond (tender guarantee).**
  Mostly to be issued within the framework of (public) invitations to tender. It covers the successful tenderer's obligation to sign the contract and to have further guarantees issued which may be required (e.g. down payment guarantee, performance guarantee, ...).
  Guarantee amount: 1–5% of the tendered value.
- **Warranty guarantee.**
  Safeguards the supplier's contractual warranty obligations.
  Guarantee amount: 5–10% of the contract value.
- **Down/advance payment guarantee.**
  This guarantee serves to secure the repayment of the effected down/advance payment in case the contractual delivery/performance obligations are not met.
  Guarantee amount: the same as the down/advance payment.
- **Retention money guarantee.**
  By means of this guarantee the buyer is assured of the repayment of a part of the contract price transferred by him ahead of schedule in case damages occur during delivery/performance within the (warranty) period agreed upon.
  Guarantee amount: 3–10% of the contract value.
- **Delivery guarantee.**
  Secures the fulfilment of the contractually agreed delivery/performance obligations by the seller.
  Guarantee amount: starting from 10% of the contract value.
- **Performance guarantee.**
  This guarantee ensures that all the supplier's agreed-upon contractual obligations are covered.
  Guarantee amount: 5–10% of the contract value.

If the instructing party is buyer:

- **Payment guarantee.**
  By issuing this guarantee the bank secures the seller's right to receive the contractually stipulated payment from the buyer for his goods/services.
  Guarantee amount: order value.

Examples for other types of guarantee:

- **Facilities guarantee.**
  This guarantee may be required by a lending bank as collateral for the repayment of a loan.
  Guarantee amount: amount of the loan (sometimes plus charges and interest).
- **Customs guarantee.**
  The bank guarantees in favour of the customs authorities that the customs duties arising through the import of goods will be paid. The text is usually stipulated by the customs authorities.
  Guarantee amount: depends on the regulations prevailing in the respective country.

Our service – your benefits.

- **Your guarantee orders are dealt with within 24 hours upon receipt by us, if they are marked “urgent“.**
- **Our guarantees can be issued in any required common foreign language.**
- **You are immediately informed of claims for payment.**
- **We prepare drafts for you (for instance for contract negotiations).**
- **We check drafts submitted by you for passages detrimental to you.**
- **Our guarantee experts are also prepared to advise you on location.**

How guarantees are issued.

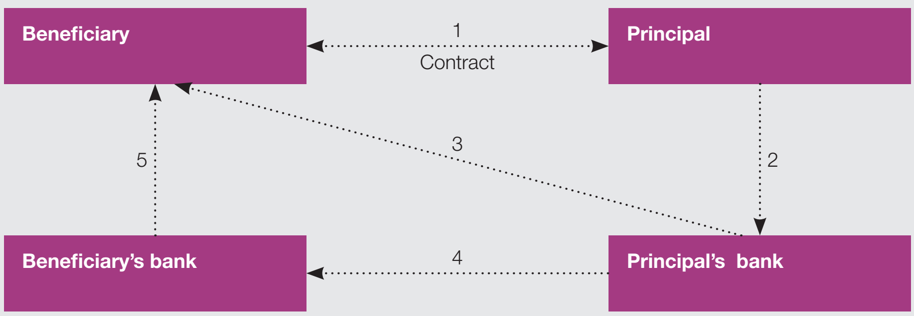
Direct guarantee.

1. Two business partners (the principal and the beneficiary) conclude a contract or the underlying transaction, in which a guarantee is required as security.
2. The principal requests his bank to issue the guarantee.
3. The bank issues the guarantee and sends it directly to the beneficiary.
   Or:
4. The bank issues the guarantee and sends it to an advising bank.
5. The advising bank passes on the guarantee, without any liability on its part, to the beneficiary. (The advising bank examines only the apparent authenticity of the guarantee.)

Indirect guarantee.

1. Two business partners (the principal and the beneficiary) conclude a contract or the underlying transaction, in which the beneficiary requires a security in the form of a guarantee. Either because the beneficiary prefers it that way or because of local regulations, this guarantee has to be issued by a local bank.
2. The principal instructs his bank to have the guarantee issued by one of its correspondent banks in the beneficiary's country.
3. Not applicable.
4. The bank instructs the foreign correspondent bank to issue a guarantee in favour of the beneficiary and provides a counter-guarantee in this regard.
5. The foreign bank issues the guarantee in favour of the beneficiary under the cover of the Austrian bank's counter guarantee. With this type of guarantee construction it is important to note that the guarantee issued by the foreign bank is subject to foreign and not Austrian law. This could result in certain disadvantages for you as principal (especially in case a claim is lodged under the guarantee).

Direct and indirect guarantees.



Some advice for the principal.

Below we would like to make some recommendations to which you, as principal, should pay particular attention.

Order to issue a guarantee.

Prior to sending us your instructions to issue a guarantee, kindly contact your account manager in order to have the necessary credit information processed.

Guarantee wording.

It is extremely important that the guarantee wording is clear and without any legal ambiguity with a view to avoiding risks and disadvantages which might arise out of an ambiguous text for the guaranteeing bank and therefore for you as principal as well. That is why we have already developed standard wordings for the most common types of guarantee, which take these requirements into account.

In the event your contractual partner requests a special guarantee wording which is to become part of the contract please contact us before signing the contract in order to enable us to advise you regarding any amendments to the text which might be necessary to minimise your risks. (We know from experience that as soon as texts have already become part of the contract it is very difficult to amend them.)

Direct/indirect guarantees.

As described above, the issuance of a direct guarantee is more favourable for you as the instructing party. Please bear in mind, however, that such a guarantee is not accepted in all countries (and might not be accepted for all transaction types).

Please contact us, we would be pleased to assist you with information and advice!

Your contacts.

Our experts are available via e-mail and phone: +43 (0) 5 05 05 with the following extensions:

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84900800 XXM/07.10/ST/XX

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