



THE LEARNING LINE ACADEMY
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International Bank guarantee-application and Regulations in Bangladesh



ICMAB

THE INSTITUTE OF COST AND MANAGEMENT
ACCOUNTANTS OF BANGLADESH

(A statutory body under the Ministry of Commerce)



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Overview on International Bank Guarantee

Definition

An international bank guarantee is a commitment issued by a bank on behalf of a client (the applicant) to a beneficiary in another country. It ensures that the bank will fulfill the applicant's contractual obligations if the applicant fails to do so. This financial instrument provides security and trust in international trade and business transactions.

Purpose:

Demonstrates the ability to perform contractual duties. Minimizes losses if the counter-party fails to fulfill their roles.

Application:

Both parties (buyer and supplier) can apply for bank guarantees.

Process:

If one party fails, the other party can invoke the bank guarantee. The claimant files a claim with the bank. The bank pays the guaranteed amount.



Parties to International Bank Guarantees

Applicant:

The party requesting the guarantee, usually the buyer or contractor.

Beneficiary:

The party in favor of whom the guarantee is issued, typically the seller or client.

Issuing Bank:

The bank that issues the guarantee on behalf of the applicant.

Advising Bank:

The bank in the beneficiary's country that advises on the guarantee (if required).



Comparison & Bank Guarantee

Aspect	Letter of Credit (LC)	Bank Guarantee (BG)
Definition	A contract via a bank guaranteeing the payment to a supplier if conditions are met.	A bank's promise to cover a loss if a party fails to fulfill contractual obligations.
Purpose	Ensures supplier payment upon meeting specified conditions.	Minimizes losses if a counter-party fails to perform their duties.
Participants	Buyer (importer), supplier (exporter), issuing bank, advising bank.	Any two trade parties (buyer/supplier) and the guarantor bank.
Process	<ul style="list-style-type: none"> - Buyer and seller agree on a sales contract. - Buyer applies for LC from issuing bank. - Issuing bank sends LC to advising bank. - Supplier delivers goods per LC conditions and sends documents to advising bank. - Advising bank forwards documents to issuing bank. 	<ul style="list-style-type: none"> - Either party can apply for a bank guarantee. - Bank guarantees to pay if the counter-party defaults. - The beneficiary can claim the guaranteed amount if there's a failure to perform. - Performance-based: Covers non-performance of contract terms. - Financial-based: Covers non-payment by the buyer.



Types of Bank Guarantee

Bid Bond

- A bid bond is a type of surety bond that provides a guarantee that the bidder will honor their bid and sign the contract if awarded. It protects the project owner by ensuring that the bidder will not withdraw or fail to enter into a contract.
- Example: If a construction company bids on a government project to build a bridge, they might need to provide a bid bond. If they win the bid but then decide not to take the project, the bid bond ensures the government is compensated for any additional costs incurred in finding another contractor.

Performance Bond:

- A performance bond is a surety bond issued to guarantee the satisfactory completion of a project by a contractor. If the contractor fails to complete the project as per the terms of the contract, the bond ensures that the project owner will be compensated or that another contractor will be hired to complete the project.
- Example: A city contracts a company to build a new library. The contractor must provide a performance bond. If the contractor fails to complete the library, the bond ensures the city can hire another contractor to finish the work without incurring additional costs.



Types of Bank Guarantee

Advance Payment Guarantee

- An advance payment guarantee is a type of bond provided by a contractor or supplier to guarantee the repayment of any advance payments made by the project owner if the contractor fails to fulfill their obligations.
- Example: A manufacturer receives an advance payment to deliver machinery to a factory. They provide an advance payment guarantee. If the manufacturer fails to deliver the machinery, the guarantee ensures the factory owner can recover the advance payment..

Payment Guarantee

- A payment guarantee is a promise from a bank or financial institution ensuring that a buyer will pay the seller for goods or services received. It mitigates the risk for the seller by providing assurance of payment.
- Example: A supplier agrees to deliver raw materials to a manufacturer on credit. The manufacturer provides a payment guarantee from their bank. If the manufacturer fails to pay, the bank will cover the payment to the supplier.



Types of Bank Guarantee

Warranty Guarantee

- A warranty guarantee is a surety bond that guarantees the workmanship and materials used in a project for a specified period. It ensures that any defects discovered within the warranty period will be repaired or compensated.
- Example: A contractor builds a new office building and provides a warranty guarantee for five years. If there are structural issues or defects within five years, the guarantee ensures the contractor will fix the issues or compensate the building owner.



Role of International Bank Guarantee

- Facilitates Trust Between International Trading Partners**
 - Builds Credibility:**
 - Bank guarantees assure both parties of commitment and reliability.
 - Reduces Hesitation:**
 - Encourages companies to engage in international transactions with new or less-known partners.
 - Strengthens Relationships:**
 - Consistent use of bank guarantees fosters long-term business relationships.

- Mitigates Risks Associated with Non-Payment or Non-Performance**
 - Protection for Exporters:**
 - Ensures exporters receive payment even if the importer defaults.
 - Assurance for Importers:**
 - Guarantees importers receive products or services as per the contract.
 - Risk Management:**
 - Minimizes financial risks and uncertainties in international trade.



Role of International Bank Guarantee

- Provides Financial Security and Assurance**
 - Guaranteed Compensation:**
 - Ensures financial compensation in case of breach or non-compliance.**
 - Support for Credit Arrangements:**
 - Facilitates easier access to credit and financing from banks and financial institutions.**
 - Market Stability:**
 - Contributes to overall stability and predictability in international markets.**



Key risks in International Bank Guarantee

Credit Risk

- The risk that the counterparty will default on their financial obligations.
- Example: An exporter receives a bank guarantee from a foreign bank. If the foreign bank defaults, the exporter may not receive the payment guaranteed for the delivered goods.

Operational Risk

- The risk of loss due to failed internal processes, systems, or human errors.
- Example: A bank mistakenly issues a guarantee with incorrect terms due to a clerical error, leading to disputes and financial losses when the guarantee is called upon.

Legal Risk

- The risk of legal action due to non-compliance with laws, regulations, or contractual terms.
- Example: A company issues a guarantee without ensuring it meets all local legal requirements, resulting in the guarantee being unenforceable in a foreign jurisdiction.



Key risks in International Bank Guarantee

Market Risk

- The risk of losses due to changes in market conditions affecting the value of the guarantee.
- Example: Fluctuations in exchange rates impact the value of a bank guarantee issued in a foreign currency, potentially reducing its effectiveness in covering the guaranteed amount.

Country Risk

- The risk associated with political, economic, or social instability in a country that could affect the fulfillment of the guarantee.
- Example: Political turmoil in a country leads to a government-imposed freeze on international payments, preventing the honoring of a bank guarantee issued by a bank in that country.



Domestic Regulation on Guarantee



Loans or Overdrafts Against Overseas Guarantees or Collaterals

- Rule:**To get a Taka loan or overdraft using a guarantee or collateral outside Bangladesh, you need prior approval from Bangladesh Bank. This applies to everyone and for non-commercial purposes.
- Procedure:**Fill out Form L (Appendix 5/94).Submit it to Bangladesh Bank for approval.
- Example:Scenario:**John in Bangladesh wants a personal loan to renovate his house. His uncle in the USA offers his US bank account as collateral.
- Steps:**
 - Fill Form L:**
 - John completes Form L with loan details.
 - Submit for Approval:**
 - John sends Form L to Bangladesh Bank for approval.
 - Wait for Approval:**
 - John must wait for approval before getting the loan.



Guarantees

RESIDENT TO NON-RESIDENT



Guarantees- from Resident to Non-Resident

Bank Guarantee: Bid Bond/Performance Bond

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission
Resident	Local Supplier	Authorised Dealer	Non-Resident	International Tender Inviting agency	Bid bond/Performace bond	Not required



Guarantees- from Resident to Non-Resident

Minor Bank Guarantees

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission
Resident	Exporter	Authorised Dealer	Non-Resident	Buyers	Export related minor activities	Not required

Missing documents,

To Banks
abroad

Authentication of
signature,

To Freight
Forwarder

Release of goods on Trust
Receipts and

Carrier

defects in documents
negotiated under LC or
otherwise.

To Banks



Guarantees- from Resident to Non-Resident

Export Performance-Bank Guarantees

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission
Resident	Exporter	Authorised Dealer	Non-Resident	Buyers	Performance bond	Not required

Conditions

- The tender floated by the foreign buyer calls for bank guarantee/performance bond
- The tenderer is a bonafide importer/user/trader of the commodity/product concerned
- There is no export ban in Bangladesh on the commodity/product to be supplied
- The past performance of the exporter is considered satisfactory by the AD.
- The remittance, if any, to the beneficiary as a result of invocation of the bond or guarantee can be made subject to report to the Bangladesh Bank.



Guarantees- from Resident to Non-Resident

Umrah Hajj-Bank Guarantees

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission	Guarantee Amount
Resident	Approved Umrah Hajj Agent	Authorised Dealer	Non-Resident	Official Umrah service agents/providers of Kingdom of Saudi Arabia (KSA)	Performance bond	Not required	Up to 2.00 Lac Saudi Riyal

Licensing Conditions	<ul style="list-style-type: none"> ✓ Must have an up-to-date license from the Ministry of Religious Affairs as Umrah agents. ✓ Must have a valid license from the Ministry of Civil Aviation and Tourism as travel agents. ✓ Must have a valid Accreditation Certificate from the International Air Transport Association (IATA).
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Other Conditions	<ul style="list-style-type: none"> <input type="checkbox"/> Agreement Submission: Authorized Dealers (ADs) must obtain agreements signed between Bangladeshi Umrah agents and official Umrah service agents in Saudi Arabia. <input type="checkbox"/> Performance Review: ADs must consider the past performance of the applicant agents to be satisfactory. <input type="checkbox"/> Remittance Conditions: Any remittance to the beneficiary due to the invocation of a bank guarantee or performance bond must be reported to Bangladesh Bank with detailed reasons for the invocation.
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Guarantees- from Resident to Non-Resident

Bank Guarantees against the suppliers credit

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission	Guarantee Amount
Resident	Import-Industrial Concern under Public/Private sector	Authorised Dealer	Suppliers	International suppliers	Repayment Guarantee	Required	Any Amount

- If the credit is from the Islamic Trade Finance Corporation(ITFC)
- The loan shall be up to 180 days period.
- Even if BIDA approved loan,prior BB permission required for issuing bank guarantee if the borrowing from the international lender other than ITFC.

Exception



Guarantees- from Resident to Non-Resident

Non Bank Led Guarantees against the suppliers credit

- Corporate Guarantee
- Personal Guarantee
- Third Party Guarantees

Non-Bank Led Guarantee

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission	Guarantee Amount
Resident	Import-Industrial Concern under Public/Private sector	Corporation/Persons/and other entity	Suppliers	International suppliers	Repayment Guarantee	Not Required	Any Amount

- Loan shall be approved by the BIDA

Condition:



Guarantees

NON-RESIDENT TO RESIDENT



Guarantees- from Non-Resident to Resident

Bank Guarantees against the alternative of earnest money deposit

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission	Guarantee Amount
Non-Resident	foreign or foreign controlled companies/firms operating in Bangladesh	Authorised Dealer	Local Entity inviting tender	Resident in Bangladesh	Alternative of earnest money deposit	Not Required	Any Amount

- The guarantee can be issued if the full amount is deposited in cash.

Against 100% Cash Deposit:

- The guarantee can be submitted with tender documents instead of an earnest money deposit.
- The validity of this guarantee will be limited to the period during which the tender decision (acceptance or rejection) is made.

In Lieu of Earnest Money Deposit:

- The guarantee can be issued by adjusting the amount from the company's or firm's existing overdraft limit, if applicable.

Against Overdraft Limit:

- The guarantee must be issued in local currency (Taka).

Currency:



Guarantees- from Non-Resident to Resident

Bank Guarantees against the Performance

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission	Guarantee Amount
Non-Resident	Non_resident firms and Companies	Authorised Dealer	Resident	local tender Inviting entity	Bid Bond/Performance bond	Not Required	Any Amount

Conditions

- **Guarantee may be issued both in local or foreign currency.**
- **The AD must have a back-to-back guarantee covering the guaranteed amount from an overseas correspondent or another bank abroad.**
- **The AD must verify the authenticity and validity of the overseas guarantee before issuing its own guarantee, bid bond, or performance bond.**



Guarantees

RESIDENT TO RESIDENT



Guarantees- Resident to Resident

Bank Guarantees against the bidding/Performance

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission	Guarantee Amount
Resident	Local suppliers	Authorised Dealer	Resident	local tender Inviting entity	Bid Bond/Performance bond	Not Required	Any Amount

Conditions

- **Guarantee may be issued in local and foreign currency**
- **In case of foreign currency guarantee, the guarantee beneficiary is to be financed by the International donors/Government.**
- **Guarantee invocation shall be in Taka.**



Guarantees NON-RESIDENT TO NON-RESIDENT



Guarantees: Non-Resident to Non-Resident

Bank Guarantees against the bidding/Performance

Applicant		Guarantee Issuer	Guarantee Beneficiary		Purpose	Prior Permission	Guarantee Amount
Non-Resident	Non-Resident contractors	Authorised Dealer	Non-Resident	Non-Resident International agencies financing the project	Supply of materials/down payment	Not Required	Any Amount

Condition

100% bank guarantee

100% cash in FC brought from abroad and deposited with guarantee issuing Bank.



Holding collateral in favour of the foreign lender

❑ **Prior Approval Requirement:**

- ❑ Authorized Dealers (ADs) in Bangladesh need prior approval from Bangladesh Bank to provide guarantees or hold collaterals on behalf of overseas bank branches or correspondents. This applies to situations involving credit facilities, guarantees to be extended by these overseas entities, or any other purposes.

❑ **Application Process:**

❑ **Details in Application:**

- ❑ To get approval, ADs must send a letter to Bangladesh Bank detailing the purpose of the guarantee or the collateral deposit.

❑ **Exceptions to the Rule:**

❑ **Funds from Overseas:**

- ❑ **No Prior Approval Needed:** If the ADs are confident that the fixed deposit or other collateral they hold represents funds that have been sent to Bangladesh through the normal banking channels from the borrower's country of residence, they do not need prior approval.
- ❑ **Verification:** ADs must verify that the funds are indeed remitted from abroad through the proper banking channels.

❑ **Industrial Enterprises' External Borrowing:**

- ❑ **No Prior Approval Needed:** ADs can hold collaterals on behalf of overseas bank branches or correspondents without prior approval from Bangladesh Bank for external borrowing by industrial enterprises.
- ❑ **Approval by BIDA/BB:** This is only applicable if the external borrowing has been approved by the Bangladesh Investment Development Authority (BIDA) or Bangladesh Bank (BB).



International Regulation on Guarantee



International Rules governing International Bank guarantees

URDG

URDG: Uniform Rules for Demand Guarantees (2010 Revision) (ICC Publication No. 758) i.e. rules to govern demand Guarantees, effective as of 1 July 2010, replacing ICC's first set of Guarantee rules, URDG 458.

ISP 98

ISP98 International Standby Practices (ISP98): Developed by the Institute of International Banking Law and Practice, and endorsed and published by ICC, they stand as the basic rules for the use of standbys worldwide.

UCP 600

UCP 600: Uniform Customs and Practice for Documentary Credits (2007 Revision) (ICC Publication No. 600). They are universally used for commercial documentary credits but can also be used for standbys



Key rules and potential dispute of URDG

Independence Principle

❑ Independence Principle (Rule 7) Definition:

- ❑ A guarantee is independent of the underlying business contract. Potential Dispute: Misunderstanding this can lead to conflicts by trying to involve the guarantor in disputes over goods, services, or performance.

Complying Presentation

❑ Complying Presentation (Rule 8) Definition:

- ❑ Requires exact submission of specified documents. Potential Dispute: Failure to present documents as stipulated can lead to rejection of the demand and transaction failures.

Expiry event

❑ Expiry Events (Rule 9) Definition:

- ❑ A guarantee expires on the earliest of its expiry date, any extension date, or on the date of payment by the guarantor. Potential Dispute: Misinterpretation of expiry dates can lead to transactional disputes.



Breif overview on ISP98

Origin & Use

- ❑ Standby Letters of Credit (SBLC) originated in the US, widely used where Europeans might use demand guarantees. "Direct pay" standbys, payable without regard to default, have no equivalent in demand guarantees.

Governing Rules

- ❑ Governing Rules In the US, SBLCs can be governed by ISP98 or UCP 600. Demand guarantees are rarely used in the US except in international transactions. In Europe, the preference is often for demand guarantees subject to URDG 758, but SBLCs are used when requested by clients.

Comparing rules

- ❑ UCP 600 is less suitable for demand guarantees or SBLCs due to coverage issues and inadequate handling of extensions, reductions, and transfers.
- ❑ URDG 758 and ISP98 are preferred for more complex security undertakings.
- ❑ URDG 758 benefits from extensive ICC support, training, and publications. ISP98, supported by IIBLP, also has comprehensive resources and educational tools but lacks the same ICC infrastructure.



Brief overview on UCP 600

UCP 600

- ❑ **The Uniform Customs & Practice for Documentary Credits (UCP 600) is a set of rules created by the International Chamber of Commerce (ICC) to regulate the issuance and usage of Letters of Credit.**
- ❑ **Scope: Applies to finance institutions globally, helping standardize international trade and reduce associated risks.**
- ❑ **Coverage: Consists of 39 articles and governs trade in 175 countries, facilitating around \$1 trillion USD in trade annually.**



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THANKS & GOOD BYE

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