GUIDING PRINCIPLES FOR BANK GUARANTEES

I. Introduction

1.1 On January 12, 2000, the Board of Directors approved a General Authority on the Bank’s Financial Products and Services (ADB/BD/WP/99/164) that provides for the issuance of guarantees as one of the Bank’s core financial products. As a follow up to the General Authority, this document has been prepared to outline a set of interim principles and modalities that will be used to guide the issuance of Bank guarantees during a two-year pilot period. Based on the Bank’s experience during this pilot phase, a more comprehensive policy on Bank guarantees will be developed for the Board’s consideration.

II. Rationale and Limitations for Guarantees

2.1 Under the guarantee, the Bank agrees to fulfill the payment obligations of a borrower to a third party lender in the event the borrower fails to meet its guaranteed obligations to the lender. As with loans, the Bank may offer guarantees to public sector entities, private sector institutions, or to enclave projects.

2.2 In offering guarantees, the Bank seeks to enable its borrowers to obtain debt financing from lenders and to gain experience in raising funds through the international capital markets. The nature and scope of the undertakings that the Bank may guarantee will depend on the specific operation, sector, and country circumstances. The Bank will not offer guarantees for equity instruments.

2.3 In issuing guarantees, the Bank aims to maximize the risk sharing between interested parties by minimizing the coverage of its guarantee. Although the Bank may provide a full risk guarantee, the coverage of the Bank’s guarantee shall normally be set, on a case by case basis, at the minimum level necessary to mobilize funding for the project.

2.4 In issuing guarantees, the Bank will continue to place paramount importance on the necessity to preserve its operational and financial integrity as a development finance institution.

III. Eligibility for Guarantees

3.1 The Bank will apply the same criteria to determine eligibility for guarantees as it applies for loans to public sector entities, private sector institutions, or enclave projects.

3.2 The Bank will ensure that all operations supported by its guarantees are consistent with the development objectives of the country and the Bank's
operational strategies as outlined in the Bank’s Country Strategy Paper. Operations that benefit from a Bank guarantee must comply with all of the policies that would normally apply for Bank loans.

IV. **Modalities for Issuing Guarantees**

4.1 As specified in the General Authority on the Bank’s Financial Products and Services, the introduction of all new financial products will be preceded by the formulation and approval of the relevant operational guidelines. Key aspects of the guidelines for guarantees include:

**Counter-Guarantee for Public Sector Guarantees**

4.2 In accordance with the provisions of Article (18.3.b) of the Agreement Establishing the Bank, for Public Sector operations, the Bank may require a counter guarantee from the member country in whose territory the project is located. Under a counter-guarantee, the Bank has the right to demand immediate repayment of any amount paid by it pursuant to a guarantee call. If the government fails to repay the Bank as per the agreed terms, the Bank will have the option to apply the same remedies as in the other defaults, such as those applicable under its arrears policy.

**Exposure Policies**

4.3 In accordance with the Bank’s policy on Capital Adequacy and Exposure Management (AB/BD/WP/2000/29), the exposures created by Bank guarantees shall be aggregated with the exposures of Bank loans on a loan equivalent basis. The addition of a guarantee and any other form of Bank assistance shall not exceed the limits applicable to a Bank loan to a project or country, unless otherwise specifically approved by the Board.

**Compensation**

4.4 In accordance with the provisions of Article (17.1.k) of the Agreement Establishing the Bank, the Bank shall receive suitable compensation for its risks. Accordingly, for public sector, private sector and enclave project guarantees, the Bank will seek appropriate compensation consistent with the respective policies for the pricing of loans. This may include a front-end fee, a commitment fee, a guarantee fee, and other charges incurred in the process of providing the guarantee.

**Settlement Resolution**

4.5 To minimize the Bank’s exposure to legal disputes related to a call on a Bank guarantee, the Bank will seek to include provisions for settlement/arbitration in the guarantee agreement. On a case by case basis, the Bank may reach agreement on the terms of dispute settlement/arbitration with the lenders.
Processing of Guarantees

4.6 Guarantees shall be appraised and supervised in accordance with the Bank’s relevant operational procedures for public sector, private sector, or enclave project loans.

Environmental Policies

4.7 All operations that benefit from a Bank guarantee must comply with the Bank’s policies for environment and sustainable development.

Procurement Policies

4.8 All operations that benefit from a Bank guarantee must comply with the Bank rules and procedures for procurement of goods and services.

V. Development of a Guarantee Policy

5.1 The principal objective of the proposed guarantee pilot program is to gain experience in the application and modalities of issuing guarantees. In view of this objective, Management is proposing to structure the pilot program for Bank guarantees with an initial life of 2 years and a total loan equivalent amount of up to UA 750 million.

5.2 At the conclusion of the pilot program, Management will prepare a report on the lessons learned to serve as a basis for the policy proposal that will be subsequently submitted for the Board’s consideration.

VI. Recommendation

The Board is invited to:

(i) Take note of the Bank’s guarantee guiding principles outlined in this document; and,

(ii) Approve the two-year pilot program with a planned guarantee ceiling of UA 750 million.