Using DFI and ECA guarantees and indemnities as credit risk mitigants

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What are MDBs, DFIs and ECAs doing?

- *"… The financial system does not reduce risk; it merely diverts it from person to person …"*
  - *Prudential Insurance Co v Inland Revenue Commissioners* [1904]
- We are seeing MDBs, DFIs and ECAs being more active and absorbing more risks globally and more active risk takers
- But - different credit risk mitigants have different rules
- MDBs, DFIs and ECAs although doing similar things as risk takers differ amongst themselves
- The CRMs that they offer differ amongst themselves

What are MDBs, DFIs and ECAs doing? *(continued)*

- Partly the reason why the products they offer differ is that historically the financial markets were segregated into industry sectors with the business of each sector being conducted by different institutions
- One of the things that we will suggest that there needs to be a more integrated approach to what MDBs/DFIs/ECAs do and what they offer to maximise efficiencies and to minimise legal risks

What do we mean by “legal risk”

- Legal risk is the risk of loss to an institution which is primarily caused by:
  - a defective transaction; or
  - a claim (including a defence to a claim or a counterclaim) being made or some other event occurring which results in a liability for the institution or other loss (for example, as a result of the termination of a contract) or;
  - failing to take appropriate measures to protect assets (for example, intellectual property) owned by the institution; or
  - change in law.

What do we mean by "defective transactions" in the context of legal risk

- Entering into a transaction which does not allocate rights and obligations and associated risks in the manner intended;
- Entering into a transaction which is or may be determined to be void or unenforceable in whole or with respect to a material part;
- Entering into a transaction on the basis of representations or investigations which are shown to be misleading or false or which fail to disclose material facts or circumstances;

What do we mean by "defective transactions" in the context of legal risk *(continued)*

- Misunderstanding the effect of one or more transactions (for example, believing that a right of set-off exists when it does not or that certain rights will be available on the insolvency of a party when they will not);
- Entering into a contract which does not, or may not, have an effective or fair dispute resolution procedure (or procedures for enforcement of judgements/arbitral decisions) applicable to it;
- Entering into a contract inadvertently;
- Security arrangements that are, or may be, defective (for whatever reason).

The Challenge

"… analysis of multilateral institutions indicates that guarantees represent approximately only 5% of their commitments but generate approximately 45% of their private-sector mobilization. Many of the factors limiting the utilization of these tools stem from the misalignment of the global regulatory architecture for financial institutions and the incentives underpinning development organizations. In particular, development guarantees do not always closely align with the policies and regulations that govern financial institutions, such as obligations prescribed by the Basel accords. Unless corrected, our ability to achieve the SDGs may be limited …"

Clearing a Path for Global Development Finance:
Enabling Basel and Development Guarantees to Deliver on Sustainable Development Goals

The challenge

Complexity in structuring guarantees and the need for expertise

Guarantees are complex instruments to structure, … . Currently, the lack of standardisation among guarantee products across development finance providers can lead to more time being spent on negotiations by the parties involved in a deal, as well as high transaction costs (e.g. legal costs) (GIIN, 2017[24]). The complexity of guarantees has implications for the skill-set needed within development organisations who want to develop and issue guarantees. According to (Lee, Betru and Horrocks, 2018[4]), many development organisations lack the operational capabilities to provide guarantees at scale. Commercial skill sets and financial backgrounds are exceptions rather than the rule in many development organisations, and building such capabilities in order to deliver best practices requires proper training and incentives for development institution personnel.

The role of guarantees in blended finance Working paper
OECD Development Co-operation Working Papers
1 June 2021

The Challenge

- *"... The OECD defines guarantees as "a type of insurance policy protecting banks and investors from the risks of non-payment ..."*
- *"... Deploying guarantees requires specific financial and risk-management expertise, which may not be readily available ..."*
  - The Role of Guarantees in Blended Finance – OECD Working Paper 97

The CRR perspective

- CRR treatment
- Eligible providers of unfunded credit protection include:
  - Central governments and central banks
  - Regional governments or local authorities
  - Multilateral development banks
  - Insurance and reinsurance undertakings and export credit agencies
- How do they differ from each other?
- Sovereign versus multi-laterals

Types of CRM

- Direct – Guarantees, insurance
- Indirect – Counter guarantees
- Synthethic – Derivatives – recent BIS announcement into synthethic CRM
- However as seen in many export credit insurance cases the terms "insurance" and "guarantee" are often used interchangeably by the ECA
  - In *Lucas ltd V ECGD* the court confirmed that ECGD issued a policy of insurance although being described as a "guarantee"
  - In *Lonrho Exports v ECGD* the court confirmed ECGD issued two standard formcontracts of insurance called "external trade guarantee" and "comprehensive short-term guarantee"
  - *In Morgan Grenfell & Co Limited v SACE the term "guarantee" was used throughout the policy instead of "insurance" and even the bank was referred to as "the guaranteed party" under the policy, but the court observed that the contract was in essence an insurance policy …*

What do MDBs, DFIs and ECAs provide?

- Guarantees
- Insurance
- Derivatives
- Standby credits
- Performance bonds

Some differences (Lin, Cheng. Law of Export Credit Insurance and Guarantees. Taylor & Francis.)

- A surety under a guarantee is “a person who answers for the default of another”
- An insurer is “a person who guarantees against loss by an event”
- A contract of guarantee must be in written form
- A contract of nonmarine insurance can be made orally
- A contract of guarantee is accessory to the underlying contract
- A contract of insurance is independent of the underlying contract – the contract conumdrum
- The obligation of the insurer is direct
- The obligation of a guarantor is accessory
- A contract of insurance based upon utmost good faith subject to the duty of fair presentation under the IA 2015
- The duty of fair representation does not apply to guarantees and the duty of disclosure is limited

Risks

- Going off-cover
- The ECA will impose various obligations on the beneficiary bank(s)
- English law is protective of guarantors (considerations for English law governed ECA guarantees)
- Care therefore needs to be taken to ensure that bank lenders understand the scope of the guarantee (i.e. what is being guaranteed) or how and when the ECA might be discharged as guarantor (whether by the terms of the guarantee or at law)- e.g. amendments/changes to the guaranteed project/transaction

Risks

- Whilst commercial guarantees typically include waiver of defences provisions, ECA guarantees do not include these provisions
- As a result, a bank must have in place adequate risk management processes to ensure that it does not discharge the ECA and leave itself uncovered (or “off cover”) – e.g. Facility Agent invalidation of cover; amendments without ECA consent (all within bank’s control)
- Time to execute
- Greater due diligence and ongoing deliverables and monitoring
- Confidentiality vs transparency rules

Re-characterisation risk

- *"… If the transaction is a cow and has cloven hooves, the parties cannot turn it into a horse by using quine terminology or saying it is a horse …"*
  - *Re New Bullas Trading Ltd [1993]*
- "… The manufacture of a five-pronged implement for manual digging results in a fork even if the manufacturer, unfamiliar with the English language insists that he intended to make a spade …"
  - *Street v Mountfound [1985]*
- In characterizing a transaction the court looks to the legal substance and not the form
  - *Welsh Development Agency [1992]*
- Characterization involves construction and then legal characterization
- The court found that a "letter of comfort" was a legally binding document that constituted both a guarantee and an indemnity
  - *IDBI Bank Ltd v Axcel Sunshine Ltd & Anor [2025] EWHC 442 (Comm).*

Who bears documentation risk?

- In addition to general exclusions on particular perils documentation risk may (or may not) be excluded
- What do we mean by “documentation risk”?
- The risk that the bank cannot receive payment because of the
  - Invailidity
  - Illegality
  - Unenforcability

  of the loan agreement with the buyer/borrower

Who bears the burden of ESG due diligence?

- A sense that environmental and social due diligence is becoming too much of a burden

Understanding the claim process

- How long is the waiting period?
- Is interest paid during the waiting period?
- Can you accelerate?
- ECAs and DFIs take different approaches
- Approach of the courts?
- English courts in *AB SEK v New Hampshire Insurance [1988]* held that in the context of ECI the assured should be compensated by the insurer the default interest "for being kept out of the money"
- What constitutes a "valid claim"
- Does an exclusion apply?

Disclosure and fair presentation

- Under English law thre is a significant difference between the disclosure obligations under export credit guarantees and insurance

Disclosure - Guarantees

- Beneficiary under a Guarantee is generally under no duty to disclose material facts to the Guarantor
- A contract of guarantee, unlike a contract of insurance, is not contract of the utmost good faith (ubberimae fidei)
- The policy underlying this general rule is that a Guarantor is expected to look after himself
- Whilst there is no general duty of disclosure there is a limited principle of disclosure of unusual features

Disclosure – Guarantees *(continued)*

- Court of Appeal has held that there is no duty to disclose facts or matters which are not unusual features of the contractual relationship between the creditor and the debtor, or between the creditor and other creditors of the debtor.
- It is always open to the parties to agree that certain specific matters should be disclosed to the Guarantor.
- Guarantors can import similar duties of "fair presentation"

The legal framework of insurance policies

- Whist insurance contracts are subject to general English contract law principles they are also governed by a set of specific rules and principles peculiar to insurance
- Falling foul of these rules can render the insurance effectively worthless
- Understanding the legal framework in which insurance policies operate is vital for ensuring that the risk transfer relied on by the financer is as robust as possible
- Insurance Act 2015 (IA 2015) reformed the law in a number of key areas:
  - pre-contract disclosure of information
  - warranties
  - fraudulent claims

Key elements of the duty of fair presentation under the IA 2015

- Some of the key elements of the duty of fair presentation include:
  - Fair presentation
  - Manner of disclosure
  - Materiality
- Fair presentation:
  - The duty of fair presentation requires the insured to disclose every material circumstance which the insured knows or ought to know (s.3(4)(a))
  - The insured may discharge its duty if it discloses sufficient information to place the insurer on notice that further enquiries are needed (s.3(4)(b))
  - There are certain circumstances which the insured is not required to disclose, for example, circumstances which diminish the risk or which the insurer knows (s.3(5))

Insurer's remedies for breach of duty of fair presentation

- It would not have written the policy at all
  - the insurer may avoid the policy, refuse all claims but must return the premium
- It would have written the policy on different terms
  - the policy will be interpreted as if those terms had been incorporated
- It would have written the policy but charged a higher premium
  - the claim amount will be reduced proportionately
- If the insurer can show that the breach was deliberate or reckless
  - it may avoid the contract
  - refuse all claims
  - retain the premium

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Mark's practice covers project and export credit finance, asset finance, structured trade and commodity finance, debt restructurings, acquisition finance and corporate advisory work.

He represents financial institutions, export credit agencies, corporates, boards, and national and supranational sovereign organizations in relation to finance transactions throughout Western, Central and Eastern Europe, Africa and the Middle East. Mark has extensive sector experience in infrastructure financing across Africa including off-grid power, healthcare and transportation. He also advises on ESG financings including hospitals, clean energy and transportation.

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Daniela advises on trade and commodity finance structures, acting for banks and non-bank financial institutions, development finance institutions and multilateral organizations as well as borrowers. She has significant knowledge of supply chain finance techniques, blended finance and export financing across the globe with a focus on emerging markets.

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Awards & Recognition

The Legal 500 UK, 2025
Sullivan ranked in Tier 1 for Trade Finance by *The Legal 500 UK, 2025* for the 11th year running
Partners Geoffrey Wynne and Simon Cook are recognised in the “Hall of Fame”
Partners Mark Norris and Sam Fowler-Holmes are recognised as Leading Individuals
Partner Marian Boyle, Counsel Daniela Barrdear, and Associate Luna Owen are recognised as key members of the practice

Chambers UK, 2025
Chambers UK, 2025 ranked Sullivan in Tier 1 for Commodities: Trade Finance (UK-wide)
Geoffrey Wynne and Simon Cook are both ranked in Tier 1
Mark Norris and Sam Fowler-Holmes are both ranked in Tier 3

Chambers Global, 2025
Chambers Global, 2025 ranked Sullivan as a Spotlight Firm in its 2025 Africa-wide Banking & Finance table
Simon Cook and Mark Norris are included as Leading Lawyers

The Best Lawyers in the United Kingdom®, 2025
Best Lawyers included five London partners — Marian Boyle, Simon Cook, Sam Fowler-Holmes, Mark Norris and Geoffrey Wynne — in the 2025 edition of *The Best Lawyers in the United Kingdom®*

IFLR1000, 2024
Sullivan recognised for Banking Lending - Lender Side in the United Kingdom by the *IFLR1000, 2024*
Partner Geoffrey Wynne is recognised as a Leading Lawyer – Highly Regarded in the United Kingdom

Receivables Finance International (RFIx) Annual Awards
Partner Geoffrey Wynne presented with the “Lifetime Achievement Award” at the Receivables Finance International (RFIx) Annual Awards, 2024
Geoffrey Wynne named “Industry Ambassador of the Year” at the RFIx Annual Awards, 2023

***Global Trade Review (GTR)* “Best Export Finance Law Firm”, 2023**
GTR named Sullivan “Best Export Finance Law Firm” at the GTR Leaders in Trade Awards, 2023

***Trade Finance Global* “Legal Innovation in Trade” 2023**
Sullivan recognised for “Legal Innovation in Trade" 2023 by *Trade Finance Global* (in connection with BAFT) at its Trade, Treasury and Payment Awards 2023

***Trade Finance Global* “Best Trade Finance Law Firm” 2022**
Sullivan named “Best Trade Finance Law Firm” 2022 by *Trade Finance Global* (in connection with BAFT) at its International Trade Awards, 2022

In 2022, 2021, 2020 and 2019, GTR recognised Sullivan
The firm was named “Best Trade or Supply Chain Finance Law Firm” at the 2022 *GTR* Leaders in Trade Awards, “Law Firm of the Year” in the category “Leaders in Trade for Innovation” at the 2021 *GTR* Leaders in Trade Awards and “Best Trade Finance Law Firm” at the GTR Leaders in Trade Awards in 2020 and 2019

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