Date Introduced: 16 August 1978
House: House of Representatives
Presented by: Rt. Hon. J.D. Anthony, Minister for Trade and Resources

Purpose

To allow the Export Finance and Insurance Corporation (EFIC) to provide indemnities to private financial corporations which issue tender, performance and related guarantees.

Background

EFIC was established by the Export Finance and Insurance Corporation Act 1974 and was designed to replace the Export Payments Insurance Corporation. It is run as a commercial operation with the objective of encouraging exports by providing finance and insurance facilities to exporters in situations where such services are difficult to obtain from private financial institutions. However, there are no provisions in the Act that allow EFIC to provide performance guarantees for exporters. The Bill will rectify this situation.

Performance guarantees are a means of ensuring that compensation is paid to buyers in the event of suppliers failing to complete a contract. They apply primarily to consultancy and construction contracts although in some circumstances they affect other goods and services.

The mechanism by which they work is as follows. Firstly when a buyer calls for tenders for a project one of the conditions may be that the successful supplier puts up a bond that is repaid on completion of the contract. If, however, the supplier fails to complete the project the bond is kept by the buyer. Bond size is typically a percentage of the contract price and may be as much as 20% to 25% for Middle East countries. Firms tendering for contracts often have insufficient capital to provide such a bond. Buyers realise that this situation may arise and are therefore usually prepared to accept a guarantee of payment, by a bank or other financial institution, instead of a bond.
Financial institutions make this guarantee in return for some premium paid by the supplier. The capital assets of the supplier are used as security in the event that non-compliance with the contract forces payment of the guaranteed sum by the financial institution. If a supplier's capital assets are so small that the guarantor could not expect to recover its payments in the event of non-compliance with the contract or if the contract appears unduly risky, no private institution will act as guarantor. In such circumstances the contract will probably be lost to another country.

The decision to introduce legislation that would reduce Australia's loss of worthwhile contracts was first announced on 27 February 1978 by the Minister. The Bill itself allows EFIC to indemnify some percentage of the private financial institution's total guarantee. The intention behind this procedure for obtaining EFIC assistance is that EFIC supplements, rather than supplants, existing private sector facilities.

The scheme should be financially self-sufficient as EFIC will charge premiums and investigate each contract to ensure that provision of a guarantee is commercially acceptable. In view of the risks, however, the Minister stated in his Second Reading Speech that an initial limit of $30 million will be placed on the level of contingent liability in respect of performance guarantees provided at any one time.

Main Provisions

Clause 4 of the Bill provides for the addition to the Principal Act of sections 35A to 35D, which relate to performance guarantees. Proposed subsection 35B(1) enables EFIC to indemnify part of an "approved guarantor's" liability with respect to performance guarantees.

"Approved guarantor" is defined in proposed s.35A to include banks or other financial institutions or insurers declared by the Minister to be approved guarantors.

Proposed s.35C enables the Minister to approve, in circumstances beyond EFIC's normal authority, a contract of indemnity if he considers that it is in the national interest.

In order to maintain private sector participation EFIC may not provide a guarantee or indemnity unless the approved guarantor bears part of the liability (proposed s.35D). The Minister, in his Second Reading Speech, stated that a minimum private sector participation of 5% would be required.
Other clauses in the Bill are designed to bring various provisions of the Act into line with recent comparable Statutory Authority legislation, or repeal provisions that have been made redundant by subsequent legislation.

Finance, Industries, Trade & Development Group

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