

Newsletter

November 2018

For further information
please contact



Stephen Clugston
Counsel
+81 3 6271 9528
stephen.clugston@bakermckenzie.com



Stephen McCann
Associate
+81 3 6271 9452
stephen.mccann@bakermckenzie.com

Projects perspective: Bid security insecurity in emerging market project tenders

This briefing has been prepared for reference purposes only based on principles of English law. It does not constitute and is not to be relied on as legal advice.

Introduction

As geopolitical uncertainty continues to spread regionally and globally and new, ambitious and intrepid players seek to establish themselves in the project development market, investors and developers are increasingly challenged and under pressure to identify and win unique, innovative and lucrative (or strategic) project opportunities. The result is pressure to look toward markets they would have previously considered to be too risky or unfamiliar.

A bidder competing in a state-run tender process in an emerging market country for the right to invest in or develop an energy or infrastructure project ("**Bidder**") will consider potential risk elements surrounding the procurement process, including local counterparty risk. This is encouraged, especially in frontier markets (i) identified by global risk agencies as being susceptible to political risk; (ii) where there have been reports or allegations of bribery and corruption; (iii) where the Bidder has limited experience with the relevant procuring authority (the "**Procuring Authority**"); and (iv) where a Procuring Authority simply has no or limited track record developing projects with international investors.

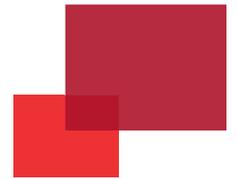
Bidders will or should be aware of the potential importance of bid security in the tender process. Requests for proposals ("**RfPs**") typically set out the requirement for the bid security including governing terms and conditions and in particular, the circumstances under which a Procuring Authority may make a demand for payment from the issuer of the bid security ("**Issuer**").

However, Bidders may also be concerned about the risk of their bid security being unfairly forfeited or called on, especially as they venture into new and riskier markets seeking unique and often politically encouraged opportunities. Such a concern needs to be carefully counterbalanced against the likelihood of disqualification should the Bidder materially deviate from the RfP requirements or choose not to submit bid security. This is not to say that it is impossible for a Bidder to win a project without submitting some form of bid security.

While there are examples of Bidders winning projects without having submitted a compliant form of bid security with their bids, RfPs (on their face) often take an absolute stance, meaning that failure to provide bid security can result in the Bidder's disqualification. Concerned Bidders need to carefully consider form requirements, whether the prescribed form is overly unfavourable to the Bidder, and to what extent they can amend the bid security (including incorporation of governing rules and governing law) to ensure it adequately addresses the risk of unfair draws by the Procuring Authority. This is particularly so given the strict and beneficiary-friendly nature of bid security and the reluctance of courts to intervene in commercial arrangements between parties dealing with bid security (at least under English law).

Why do Procuring Authorities want bid security in competitive tenders?

Procuring Authorities use bid security to ensure Bidders are serious about participating in the tender process on the terms set out in the RfP and prevent abuse of the bid process by ensuring bids are not frivolous. This is arguably more likely for sensitive projects such as large projects involving international investors and multi-sourced financing supported by foreign state-owned or state-funded institutions (and thereby an element of political interest).



It is also used as compensation in the event that a Bidder: either withdraws its bid other than as permitted by the RfP; contravenes a material condition in the RfP; or fails to negotiate and sign the project documents following qualification as preferred Bidder. In such case the Procuring Authority would need to re-tender the contract, resulting in delays and additional procedural costs, which would be covered by the bid security.

Under the RfP, a Procuring Authority is typically entitled to exercise the bid security (i.e. make a demand for payment) upon the occurrence of specific events. Common examples include:

- withdrawal by the Bidder;
- failure by the Bidder to negotiate and execute the contracts enclosed with its bid within the required period if appointed as the qualified Bidder;
- any material changes in financial or technical capabilities of the Bidder; and
- where the Bidder engages in any illegal acts or corrupt or fraudulent practices,

(each a "**Demand Event**").

The form of bid security is usually prescribed in the RfP by the Procuring Authority and commonly required to be a bid bond by way of demand guarantee ("**Bid Bond**") or standby letter of credit ("**Standby LC**"). These forms are generally favourable to the Procuring Authority for the reasons discussed below.

However, every project is unique and carries varying degrees of market and party risk. So too therefore, is the Procuring Authority's risk perception when dealing with international Bidders. Accordingly, one cannot necessarily assume that the Demand Events nor bid security terms will be identical across project RfPs. **Figures 1 through 3** below highlight some of the contrasting Demand Events and other bid security terms across Africa, the Middle East, and APAC regions.

There is always a possibility of a Procuring Authority exercising its rights under the relevant bid security. To a degree however, this is within the control of the Bidder as it is based on the terms of its proposal. However, beyond the form of the bid security, there is also a risk of an unfair or fraudulent demand by the Procuring Authority and Bidders should be familiar with relevant legal elements in the context of the tender process. Just as the procedures in relation to demands very much depend on the terms of the bid security (and by extension, Bidder decisions regarding bid security), insecurity in relation to the perceived risk depends on properly understanding the underlying legal mechanics, legal rights, and options available to the Procuring Authority, the Issuer, and the Bidder.

Fig. 1 - Bid security in Africa

1. Country	2. Bid security	3. Sizing	4. Compliance	5. Form of bid security
South Africa	Bank guarantee.	Sized in local currency by reference to contracted capacity.	Strict. Procuring Authority absolute discretion to disqualify for non-compliance.	Annexed to RfP.
Uganda	Irrevocable and unconditional standby letter of credit.	Fixed USD.	Strict. Procuring Authority absolute discretion to disqualify for non-compliance.	Proposed form attached to RfP. Substantially similar likely to be acceptable.
Nigeria	Bank guarantee.	Sized in local currency by reference to acquisition value of the relevant asset.	Strict. Procuring Authority absolute discretion to disqualify for non-compliance.	Not specified other than requirement to be on-demand.
South Africa	Irrevocable and unconditional standby letter of credit.	Sized in local currency by reference to contracted capacity.	Strict. Procuring Authority absolute discretion to disqualify for non-compliance.	Form not specified other than requirement to be an irrevocable and unconditional standby letter of credit.



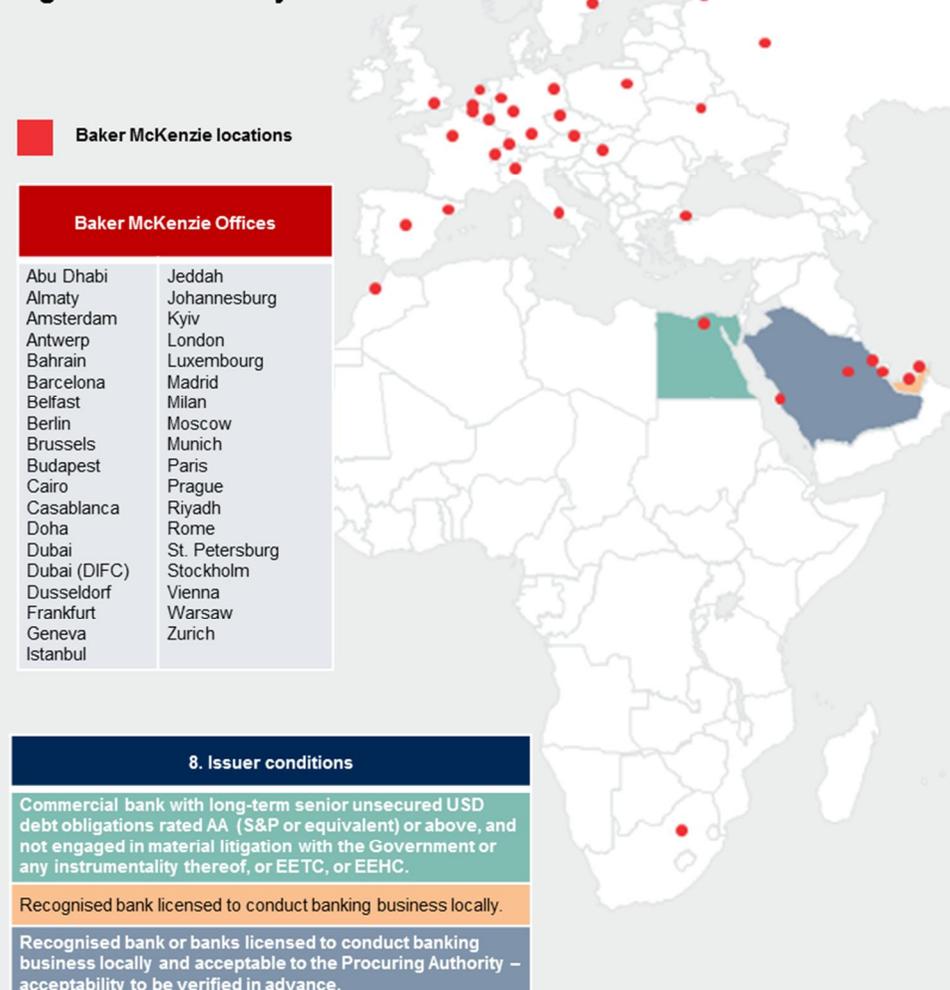
Baker McKenzie locations

Baker McKenzie offices

Morocco
Cairo
Johannesburg

6. Express triggers for forfeiture	7. Excluded Bidder rights	8. Issuer conditions	9. Validity	10. How the bid security is returned	11. Subject to local tender law	12. Governing rules	13. Governing law and disputes
<ul style="list-style-type: none"> Breach of a law or disqualification from bid process. Failure to extend the term of the security after agreeing to do so. Submission of non-compliant bid. Failure to provide the required undertaking to the Procuring Authority. 	Not specified.	Bank licensed to conduct banking business locally or a licensed short term issuer, with a rating of BBB or better by S&P or equivalent.	<ul style="list-style-type: none"> Disclosures to media regarding proposal or RfP. Withdrawal of proposal during validity period. Failure to negotiate in good faith after nomination as preferred Bidder. Material change in financial or technical capabilities. Material changes in consortium composition not approved by Procuring Authority. Failure to execute shareholders agreement. Conflict of interest, corrupt practice or fraudulent practice / violation of local law. 	Returned to unsuccessful Bidders within 30 days of announcement of successful Bidder.	Not specified.	Not specified.	Local law. Dispute settlement through local courts.
<ul style="list-style-type: none"> Withdrawal during validity period. Misrepresentations or false information in the proposal. Failure to provide required post-qualification security. Corruption or fraudulent practice or any form of collusion in order to affect the outcome of the bid process. 	Not specified.	Overseas bank with a correspondent local bank licensed to conduct banking business.					
<ul style="list-style-type: none"> Breach of any law relating to the relevant procurement procedure. Failure to extend the duration of the bid security where such extension has been consented to by the Bidder. Submission of a non-compliant proposal. 	Not specified.	Foreign bank S&PA rated with a correspondent local bank licensed to conduct banking business acceptable to the Procuring Authority.	365 days from submission deadline. To be extended if proposal validity period is also extended by the Procuring Authority.	Returned to unsuccessful Bidders within 4 weeks of rejection.	Yes.	Not specified.	Governing law and dispute settlement mechanism not specified.
		Bank licensed to conduct banking business locally or a licensed short term issuer, with a rating of BBB or better by S&P or equivalent.	The earlier of: 365 days from the bid submission date and 120 days after the Bidder is notified that its bid is not compliant or unsuccessful. To be extended if proposal validity period is also extended by the Procuring Authority.	Returned to unsuccessful Bidders within 15 days of expiry of the bid security.	Yes.	Not specified.	Governing law and dispute settlement mechanism not specified.

Fig. 2 - Bid Security in the Middle East

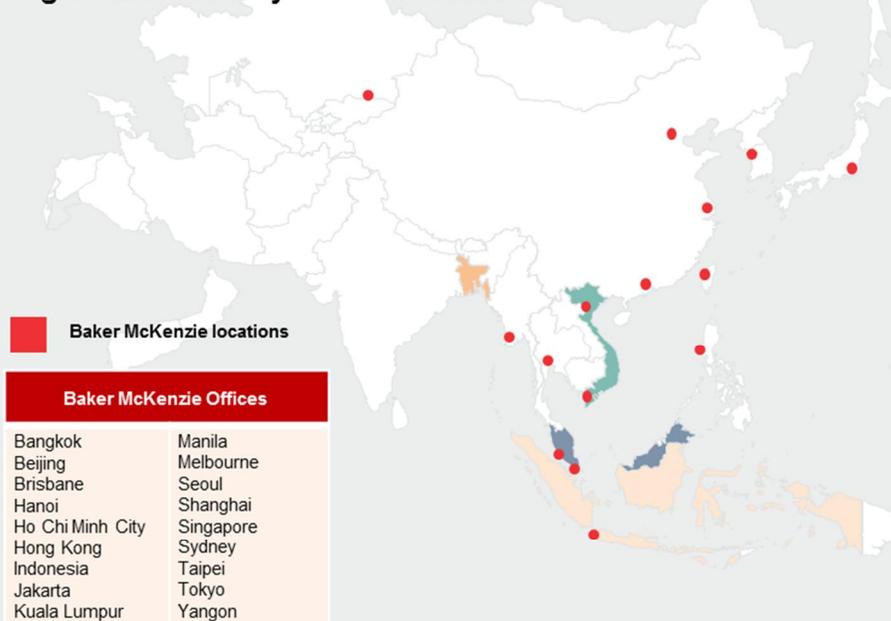


1. Country	2. Bid security	3. Sizing	4. Compliance	5. Form of bid security
Egypt	Bank guarantee.	Fixed USD.	Strict. Procuring Authority absolute discretion to disqualify for non-compliance.	Annexed to RfP.
Abu Dhabi	Bank guarantee.	Sized in local currency by reference to contracted capacity.	Bidder may explain non-material deviations and Procuring Authority may accept or disqualify.	Annexed to RfP.
Saudi Arabia	Bank guarantee.	Fixed local currency.	Strict. Procuring Authority absolute discretion to disqualify for non-compliance.	Annexed to RfP. Substantially similar likely to be acceptable.

6. Express triggers for forfeiture	7. Excluded Bidder rights
<ul style="list-style-type: none"> The Bidder is selected as the winning Bidder and (i) seeks to modify or fails to execute the project agreements; or (ii) fails to deliver performance security five days before execution of the project agreements. Withdrawal during the validity period for any reason other than non-acceptance of a request to extend. Any bribe, gift or other improper payment to a Governmental Official, political party, official thereof, or person for on-payment constituting a form of influence, inducement, means of securing an improper advantage, or inducement to influence the EETC, EEHC, or the MOEE or any related instrumentality to the advantage of the Bidder or any other person. 	Not specified.
<ul style="list-style-type: none"> Withdrawal of proposal during the validity period. Failure to enter into offtake agreement or furnish development security after signing the offtake agreement. 	Not specified.
<ul style="list-style-type: none"> Unsuccessful Bidder prevents its supporting financing parties from supporting the successful Bidder or Procuring Authority. Withdrawal during validity period. If selected Bidder (i) refuses or fails to negotiate or execute the project agreements (ii) breaches its obligation in accordance with the project development agreement or (iii) refuses or fails to furnish the development security after signing the offtake agreement. 	Bidder right to object to demand expressly excluded.

9. Validity	10. How the bid security is returned	11. Subject to local tender law	12. Governing rules	13. Governing law and disputes
Not specified.	Not specified.	Not specified.	Not specified.	Not specified.
365 days (or more if extended) plus 21 days. Validity period may be extended by request and if Bidder agrees, bid security shall also be extended. Bid security of shortlisted Bidders extended until the execution of the PPA.	Returned to non-shortlisted Bidders within 30 days after notification to them or after no proposal is accepted.	Yes.	Not specified.	Local law. Dispute settlement mechanism not specified.
Twenty one (21) days after the expiry of the Validity Period (9 months from bid submission). Validity period may be extended by request and if Bidder agrees, bid security shall also be extended.	Returned to non-shortlisted Bidders within 30 days after notification to them or after no proposal is accepted.	Not specified.	Not specified.	Not specified.

Fig 3 - Bid Security in South East Asia



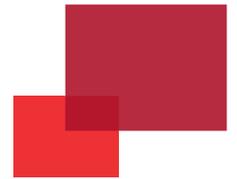
- Baker McKenzie locations**
- Bangladesh
 - Malaysia
 - Vietnam
 - Indonesia
- Baker McKenzie Offices**
- | | |
|------------------|-----------|
| Bangkok | Manila |
| Beijing | Melbourne |
| Brisbane | Seoul |
| Hanoi | Shanghai |
| Ho Chi Minh City | Singapore |
| Hong Kong | Sydney |
| Indonesia | Taipei |
| Jakarta | Tokyo |
| Kuala Lumpur | Yangon |

1. Country	2. Bid security	3. Sizing	4. Compliance	5. Form of bid security
Bangladesh	Bank guarantee.	Sized in USD by reference to contracted capacity.	Bidder may explain non-material deviations and Procuring Authority may accept or disqualify.	Annexed to RfP.
Malaysia	Bank guarantee.	Sized in USD by reference to contracted capacity.	Strict.	Annexed to RfP.
Vietnam	Bank guarantee or deposit by cheque.	Sized in USD by reference to contracted capacity.	In the case of a bank guarantee, Bidder may use a form other than that annexed to the RfP, so long as it is similar and meets the basic requirements of the bid security.	Annexed to RfP. Substantially similar likely to be acceptable, as noted above.
Indonesia	Bank guarantee and cash security.	Fixed USD.	Strict.	Annexed to RfP.

6. Express triggers for forfeiture
Failure to comply with formalities to ensure the extension of the bid security prior to expiration.
<ul style="list-style-type: none"> Withdrawal of bid during validity period or prior to rejection. Material misrepresentations. Failing to negotiate within 14 days' notice if shortlisted where informed to do so. Failure to provide substitute bid security where required. Illegality or improper conduct.
<ul style="list-style-type: none"> Withdrawal of bid after bid closing date and within the effective period of the bid security. Violation of bidding regulations leading to cancellation of the bid. Failure to submit contract performance security when required. Refusal to proceed with preliminary contract negotiations within five working days, from the date of receiving an invitation to do so, except for the case of force majeure. Failure to negotiate, finalize and execute the contract within the timeline set out by the Procuring Authority, except for the case of force majeure.
<ul style="list-style-type: none"> Withdrawal of bid during validity period or prior to rejection. Material misrepresentations. Failure to establish project company in time required. Shareholder interest disposals prior to PPA execution; failure to agree and initial the PPA within 14 days after being issued letter of intent as preferred Bidder and failure to sign after price approval. Illegality or improper conduct.

7. Excluded Bidder rights	8. Issuer conditions
Bidder notice right expressly excluded.	Bank licensed to conduct banking business locally.
Bidder notice right expressly excluded.	Bank licensed to conduct banking business locally.
Not specified.	Bank licensed to conduct banking business locally.
None.	Bank licensed to conduct banking business locally.

9. Validity	10. How the bid security is returned	11. Subject to local tender law	12. Governing rules	13. Governing law and disputes
9 months from the bid submission deadline. To be extended if proposal validity period is also extended by the Procuring Authority.	Returned after the Procuring Authority notifies Bidder it is not selected. Procuring Authority must return the bid security to all Bidders other than the first-ranked Bidder.	Not specified.	Not specified.	Governing law and dispute settlement mechanism not specified.
6 months from the bid submission deadline. To be extended if proposal validity period is also extended by the Procuring Authority. If Bidder does not withdraw, the extension is considered accepted.	Returned to unsuccessful Bidders upon the sooner of the expiration date of the bid or 14 days after another Bidder is chosen. Returned to successful Bidders, when they provide the required substitute bond.	Yes.	Not specified.	Local law. Dispute settlement through local courts.
350 days from the date of bids closing (i.e., from the deadline for investors' submission of bids proposal).	Returned to non-successful Bidders within 20 days from the date the successful Bidder is approved. Returned to successful Bidder upon the Bidder's submission of contract performance guarantee.	Yes, for state-sponsored/financed or state-guaranteed project subject to applicable qualification thresholds.	Not specified.	Local law. Dispute settlement mechanism not specified.
6 months from the bid submission deadline. Extended if Bidder agrees to extend the validity period of its bid.	Returned if the bid is determined unresponsive and rejected. Procuring Authority has right but not the obligation to return the bid security upon the Bidder declining an extension of the validity of its bid. Also returned upon execution of the PPA.	Not specified.	Not specified.	Governing law and dispute settlement mechanism not specified.



Key bid security principles and the fraud exception

1.1 Bid security principles

The key legal principle that underpins Bid Bonds and Standby LCs in project procurement is the "autonomy principle". This principle is premised on the notion that bid security is independent from the underlying contract on which it is based. The Issuer is not concerned or bound by the terms of the underlying contract and therefore its undertaking to pay the Procuring Authority on demand, is not subject to claims or defences by any person that a party to the underlying contract has breached its terms.

Practically, the Issuer is therefore isolated from the underlying RfP and bid documents and concerns itself only with documents relating to the operation of the bid security – namely the bid security itself and a demand. It follows that an Issuer of a Bid Bond or Standby LC cannot resist (other than in exceptional circumstances) paying a Procuring Authority upon receipt of a compliant demand and has very little defence if it chooses not to pay. The only situation where an Issuer is entitled to resist paying a Procuring Authority following a compliant demand is in the case of fraud (otherwise known as the "fraud exception").

The autonomy principle and fraud exception together afford a bid security Issuer certain protections Bidders should be aware of. An Issuer that pays pursuant to a compliant demand is protected from claims made against it for doing so, unless at the time of demand, fraud was "established". It is generally for the Bidder to establish the existence of fraud as the Procuring Authority is the beneficiary of the bid security. Conversely, if the Issuer does not pay where fraud has been established at the time of demand, it will generally be protected if the Procuring Authority sues. However, if the Issuer refuses to pay where fraud has not been established, the Procuring Authority may bring a claim against the Issuer, even if mere suspicions of fraud persist. It should be noted that the difference between "suspected" and "established" fraud is key, especially in the context of injunctions against payments due to fraud (as discussed below).

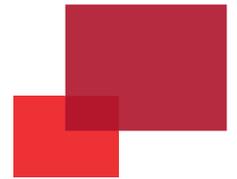
Practically, this means the Bidder should not rely on the Issuer for protection once the bid security has been issued; the risk of bid security being called (justly or unjustly), is for the Bidder to bear.

1.2 Injunctions

Other than establishing fraud in the eyes of the Issuer or otherwise dissuading a Procuring Authority from making a demand under its bid security, what legal avenues are available for a Bidder?

If the Bidder becomes aware of the Procuring Authority's intention to issue a demand under the bid security, it may apply to the court for injunctive relief to prevent either the Procuring Authority from making such demand or otherwise restrain the Issuer from making payment on receipt of the demand from the Procuring Authority. However, bearing in mind the fraud exception, as the Procuring Authority is the beneficiary of the bid security, the onus will be on the Bidder to clearly establish fraud in order to successfully access injunctive relief.

The standard of proof is high and two limbs need to be satisfied in light of general reluctance by courts to interfere in commercial relations between parties: there needs to be a realistic inference that (a) the Procuring Authority could not honestly have believed in the validity of its demand and (b) the Issuer was aware of the fraud. It is generally accepted under English law that evidence presented to an Issuer in seeking to establish the existence of fraud needs to be irrefutable, in order to avoid exposing the Issuer to a potential claim by the Procuring Authority.



A Procuring Authority's ability to benefit from payment under bid security depends on the agreed Demand Events. Conversely, its inability to do so, will depend on a Bidder's ability to establish fraud. However, there are specific mechanics that can address procedural risk surrounding a Procuring Authority's ability to demand payment from an Issuer, whether unfairly or otherwise. The importance of understanding such mechanics should not be underestimated.

Bid security mechanics

We take a closer look at the mechanics involved in most common forms of bid security.

1. Bid Bonds

1.1 An overview

Mechanically, a Bid Bond operates as an on-demand payment guarantee (in contrast to a third party performance guarantee). It is an unconditional undertaking by the Issuer (as guarantor) to pay the Procuring Authority a specified amount on demand if the Bidder fails to perform the contract, without any need for the Procuring Authority having to prove a breach by and sue the Bidder.

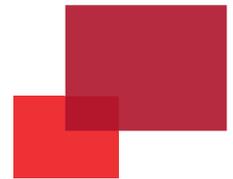
Whereas for a Bid Bond, the primary contractual obligation is simply payment of a specified sum on the occurrence of a specified event (demand by the Procuring Authority), the beneficiary of a third party performance guarantee needs to establish liability in connection with the underlying contract, before being able to seek performance – even if this involves payment. Where 'on demand' characteristics are either ambiguous to some degree or lacking outright, a Bid Bond can be construed by courts, to constitute a performance guarantee (which is less favourable to the Procuring Authority for the reasons noted above).

In such a context, the onus of establishing that the bid security is a Bid Bond (with 'on demand' characteristics and not a performance guarantee) is for the Procuring Authority and it is arguable that any ambiguity on such a point would therefore benefit a Bidder seeking to avoid payment to the Procuring Authority. This is noteworthy since courts have generally maintained a strong presumption against creating a primary payment obligation unless it is unequivocally reflected in the bid security. If an unambiguous Bid Bond has been issued there is little room for procedural deviation - it will operate strictly according to its terms. The Procuring Authority is entitled to prompt payment by issuing a demand in compliance with the agreed procedures. This is otherwise known as the doctrine of "strict compliance".

The doctrine does not apply equally to Bid Bonds and Standby LCs. In short, Issuers of Bid Bonds do not automatically benefit from the same strict compliance requirements as Issuers of Standby LCs and case law suggests that a demand which is not strictly compliant with Bid Bond terms, can potentially be compliant 'on construction'. Bidders and Issuers should therefore be prudent about being clear and confident regarding demand rights or otherwise consider, if possible, using a Standby LC as an alternative.

1.2 Governing rules – the URDG

The International Chamber of Commerce ("ICC") Uniform Rules for Demand Guarantees, 2010 revision, ICC Publication No. 758 (URDG 758) ("URDG") reflects the accepted and encouraged international standard of governing rules for Bid Bonds. While the use of the URDG is commonplace or increasing in developed markets, its absence in emerging market bid security requirements is not unusual as it does not



afford the beneficiary the same freedom and flexibility it would prefer to enjoy without incorporated governing rules.

Pursuant to Article 15 (*Requirements for demand*) of the URDG, in addition to any documents expressly required by the Bid Bond, a demand by a beneficiary must be accompanied by a statement indicating in what respect the Bidder has breached its obligations under the underlying relationship. This is satisfied by written indication in the demand letter. The purpose of the provision is to ensure the beneficiary enquires into and provides honest justification for its demand.

Another useful mechanism from the Bidder's perspective is URDG Article 16 (*Information about demand*), which requires the beneficiary to give a copy of the notice of demand to the Bidder - this is particularly helpful if a Bidder intends to seek an injunction in the case of fraud as was previously discussed. These concepts (whether by way of the URDG or otherwise) are often omitted in RfPs as they would weaken the Procuring Authority's position.

Those provisions being satisfied however (if included), there is limited opportunity for an Issuer to not comply with the demand. Article 20(b) (*Time for examination of demand; payment*) of the URDG states that the Issuer shall pay where it determines the demand complies with the terms of the Bid Bond. Such determination is to be made on the face of the demand form, however, as we have indicated, courts are likely to take a constructive approach in the case of any Issuer resistance. Further, Article 27(a) (*Disclaimer on effectiveness of documents*) specifies that the Issuer assumes no liability for the form, sufficiency, accuracy, genuineness or falsification or legal effect of any signature or document presented to it.

2. Letters of credit

2.1 An overview

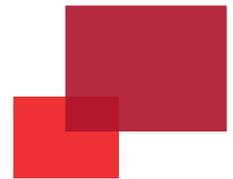
Standby LCs (in contrast to documentary letters of credit) are similar to Bid Bonds, but are more straightforward mechanically. Under a Standby LC, the Issuer undertakes to pay the beneficiary when the Bidder has allegedly failed to perform the contract, simply upon the presentation of a compliant written form of demand. While payment is conditional on default by the Bidder, the Issuer will rely on the demand form and not inquire into the truth or existence of a default nor seek any proof. In this sense, the autonomy principle applies equally to Standby LCs.

As with Bid Bonds, the Issuer has a primary obligation to pay on receipt of a compliant demand and has limited defences to resist such a demand for payment by a beneficiary, other than in the case of fraud. Accordingly, the risk of unfair demands is equally present in the case of Standby LCs and the conditions and terms for a demand will be imperative in addressing Bidder concerns.

A key point of contrast with Bid Bonds however, is that unlike Bid Bonds which may be treated as constructively compliant under English law, Standby LCs automatically benefit from a higher standard of strict compliance. This means that the Issuer may have greater payment refusal rights where a beneficiary has not, in the Issuer's determination, fully complied with the Standby LC terms in serving a demand for payment. It is perhaps because they raise the burden of compliance for the beneficiary, that Standby LCs are less common in emerging market project tenders.

2.2 Governing rules – the ISP98

The ICC has published international standards that may be imported into Standby LCs. The International Standby Practices of 1998, published by the ICC (No 590) ("**ISP98**") set out rules similar to the URDG, intended to provide generally accepted protections to Issuers (and Bidders). As with



Bid Bonds, it is not surprising that uniform governing rules are not incorporated, as they do not afford beneficiaries the same freedom and flexibility it would prefer to otherwise enjoy without incorporated governing rules.

Unlike under the URDG, the ISP98 does not provide a mechanism to address fraud or non-compliance of the underlying contract as a defence to non-payment by an Issuer. Accordingly, there is no relief for the Issuer to avoid its obligation to pay pursuant to a demand. Rather, pursuant to Rule 2.01(a) (*Undertaking to honour by issuer and any confirmer to beneficiary*), the Issuer must honour a presentation of a demand that appears "on its face" to comply with the terms and conditions of the Standby LC. This is consistent with the notion the "strict compliance" principle applies to Standby LCs more than Bid Bonds.

Compliance is determined by examining the presentation of the demand on its face against the terms and conditions stated in the Standby LC (Rule 4.01(b) (*Examination for compliance*)) but documents presented must be consistent to the extent expressly required in the Standby LC (Rule 4.03 (*Examination for inconsistency*)). As with the URDG, the Issuer is relieved of any responsibility relating to the accuracy, genuineness or effect of any document presented under the Standby LC (Rule 1.08(b) (*Limits to responsibilities*)).

In contrast to under the URDG, Rule 3.10 (*No notice of receipt of presentation*) of the ISP98 expressly states that an Issuer is not required to notify the applicant of receipt of a presentation under a Standby LC. This position is not as helpful to the Bidder as the URDG and Bidders should consider amending the terms to expressly include such a requirement.

Tackling the insecurity around bid security

Reflecting on the discussion above, what are some of the steps that can be taken in response to bid security insecurity in project tenders? The considerations below are not mutually exclusive and should be considered together, rather than in isolation.

1. Accept the perceived risk

Certainly the most RfP-compliant approach would be to accept the RfP terms surrounding bid security as is prescribed under the RfP, if the Bidder is comfortable doing so. Bidders may feel that this is the most competitive approach. However, Bidders should be mindful of the risks discussed above in the context of the competitive tender process and whether, in view of its bargaining power, it is reasonable to accept the Procuring Authority's position without question or qualification.

2. Choose an appropriate form of bid security

While there are a variety of factors that need to be taken into consideration (including cost, commercial discussions with Issuers etc.), where an option is available as regards the form of bid security, one might generally consider a Standby LC to be more Bidder friendly. This is due to the fact that the strict compliance principle automatically applies more closely and the fraud exception is broader. Bidders should also consider incorporating the appropriate governing rules.

As a result, but at all times subject to the terms of the Standby LC which must be carefully reviewed, Bidders should benefit from a greater sense of certainty regarding the Procuring Authority's ability to exercise a demand in response to a Demand Event. Generally speaking, the strict compliance principle will also force a Procuring Authority to consider more closely and carefully, its entitlement to make a demand and the process required to do so.



Where a form of bid security has not been prescribed, in light of the above discussion surrounding ambiguity in drafting and the strict compliance principle, Bidders may want to consider the benefits of submitting their preferred form of bid security but not prescribing the form of demand required from the Procuring Authority. Bidders should carefully consider the risk of disqualification (if any) before doing so.

3. Chose an appropriate bid security Issuer

RfPs may prescribe "qualified bank" requirements in relation to the Issuer. Conditions may relate to location, experience and rating thresholds by reference to long-term unsecured debt obligations. Likewise, RfPs may set out restrictions against permitted Issuers of bid security by reference to sanctions standards and also ongoing litigation in the host country or against the Procuring Authority (see Egypt under **Figure 2** by way of example).

Bidders often have their own preferred banks. However where RfPs require local banks (from the same jurisdiction as the Procuring Authority) to issue the bid security, Bidders need to carefully consider risks from doing so including among other things, independence and reliability of the local bank and the risk of not being able to access a right of injunction, as would otherwise be more readily available.

Where Bidders are permitted to use preferred banks from their home jurisdictions, Bidders should carefully discuss the conditions to the indemnity arrangements behind the bid security to ensure the Bidder feels supported and is confident in the arrangement; the Issuer and Bidder should be unified in their approach to the bid security without jeopardising the bid process but also without putting the Issuer at risk.

4. Propose appropriate terms in the bid security

4.1 Ensure the bid security has governing law

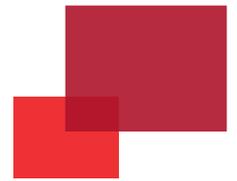
Depending on the amount of care and attention that has gone into the preparation of the RfP by the Procuring Authority, governing laws may sometimes be omitted in the prescribed form of bid security (or the rules in relation to the RfP). This can be intentional or inadvertent, but either way, is not ideal. Conflict of law rules generally propose (in common law and EU jurisdictions at least) that where parties have not chosen a governing law, the law will be: (a) the law of the country of residence of the principal party carrying out the contract; or (b) the law of the country where the party required to effect performance of the contract is customarily resident.

To address the ambiguity and potential costs associated in determining which law governs the bid security if a dispute arises, it is prudent and preferable to include a governing law clause at the outset.

While English law is the most developed and often therefore preferable in the context of dealing with the fraud exception and injunctive relief, Bidders should carefully consider its appropriateness in cross-border enforcement through legal advice on alternate applicable laws. Bidders should note court mentality in intervening in commercial agreements and the standards to be achieved in order to obtain an injunction against payment upon demand (should injunctions be available under applicable law).

4.2 Include governing rules

Regardless of the form of bid security, there needs to be certainty regarding the rules that govern how the bid security operates and how demands can be made (and associated rights arising from demands). Incorporating the URDG into a Bid Bond or the ISP98 into the Standby LC is a useful way for a Bidder to achieve certainty in the mechanics of bid security. An argument that the URDG and ISP98 reflect terms and



conditions that are generally accepted (and should be included) in international projects, can be made. An alternative approach is to expressly include key provisions from the URDG or ISP98 directly into the bid security for certainty. This may be the more practical approach particularly where the Procuring Authority is not familiar with the ICC governing rules.

Whether or not the incorporation of such rules or provisions will be accepted by a Procuring Authority or whether this could increase the risk of disqualification, however, needs to be assessed on a case by case basis.

4.3 Include a notice requirement

As an example, subject to a review of potential disqualification risk arising from amending bid security (where the form is prescribed), Bidders should consider drafting in a notice requirement such that the Procuring Authority must submit a copy of a demand for payment on the Bidder at the same time as the Issuer.

If the URDG has been incorporated (in the case of a Bid Bond), an additional notice requirement is not needed as the URDG already imports this mechanism and this can be relied on – though we would encourage Bidders to make sure they are familiar with the URDG first. However, where the URDG has not been incorporated and in the case of Standby LCs (because ISP98 does not contemplate such a notice requirement), Bidders should expressly include a notice requirement to give the Bidder an express entitlement to notice from the Procuring Authority.

Interestingly, some RfPs expressly exclude this right (see Bangladesh and Malaysia under **Figure 3** by way of example). Bidders should carefully assess the consequences of accepting such exclusions and the practical impact it will have on a Bidder trying to establish fraud in the eyes of the Issuer or seek an injunction to prevent a demand from being effected by a Procuring Authority.

4.4 Third party verification

Depending on the level of concern surrounding a particular project tender process, a Bidder should consider amending a prescribed form of bid security (or alternatively, include the requirement in its own proposed form) requiring independent third party verification, a judgment or an award as a requirement for the Procuring Authority to be entitled to demand payment. This will ensure the Procuring Authority enquires into and provides honest justification for its demand.

Again, however, the feasibility of such an approach needs to be assessed on a case by case basis and weighed against the risk of disqualification for doing so. If successful, however, and the Procuring Authority is persuaded to accept the mechanism, a Bidder would benefit from robust protections against any unfair demands made against the bid security accompanying its bid.

Disclaimer

This briefing is an overview of the potential risks faced by Japanese investors in emerging market economies and some of the mechanisms involved in bid security.

It is provided for reference purposes only and does not constitute legal or commercial advice to be relied by clients. While clients may want to refer to some of the concepts in this briefing, clients are encouraged to seek formal legal advice.