CivilSure

Frequently Asked Questions

Why do I need a guarantee? In a construction context there are a myriad of micro and macro-economic risks which could impact a projects success. This is where Guarantees come in – they are an important tool to mitigate the risk for the Employer and their project funders. The ultimate purpose of any guarantee is to cover the Employer for the increased costs of completion as a result of the non-performance or default of the Contractor.

What types of guarantee do I need? Different Guarantees, for different risks exist:

- Performance Guarantees – which protects the Employer against the increased costs of completion as a result of non-performance.
- Retention Guarantees – which enable the recovery of retention funds paid to address remedial works.
- Advance Payment Guarantees – enables contractors to be pre-financed by making payments before the commencement of the contract.
- Bid Bonds – which cover the costs of re-tendering or re-negotiating, if the awarded contract cannot be fulfilled by the appointed contractor.

Who are the parties involved? There are typically three parties to a Guarantee: The Employer – also known as the "Principal Creditor" or the "Beneficiary" who awards a contract to the Contractor who is also known as the "Principal Debtor". In order to attain the appropriate security, the Employer will require the Contractor to furnish a Guarantee, this is where the Insurer comes in. The Insurer is also referred to as the "Guarantor" or "Co-Principal Debtor".

What is the difference with a bank guarantee? A Construction Guarantee from an Insurer has several distinct advantages compared to a Bank Guarantee:

- Wordings can be tailored to your needs whereas banks are unlikely to accommodate bespoke wordings
- Guarantees remain in force for the duration of the project whereas bank guarantees usually have a defined expiry date
- No pledge is made towards a lending institution and so your borrowing capacity is not diminished whereas with the bank your line of credit will be diminished

Why are the wordings so important? What should I be aware of? The contract governing the Guarantee will be underpinned by either industry accepted wordings such as a JBCC, GCC, NEC, etc, Employer prescribed wordings, or insurer proposed wordings. The type of wordings used will dictate whether the agreement is a contract of suretyship or a guarantee. Guarantees are based on demand wordings, which are either conditional or unconditional, and must respond if triggered within a defined period. The main difference between a demand guarantee and a suretyship contract is that a demand guarantee is a separate and independent contract from the underlying contract between the Employer and the Contractor, i.e. the Principal Building Agreement. In other words, if the construction contract between the Employer and the Contractor is found to be invalid, this will not invalidate the demand guarantee contract as it is a distinct and separate contract. The Guarantee Premium and the amount of Collateral required will largely depend on the type of wordings required. Typically on Demand guarantees are more expensive and carry a great risk as they are not always linked to the performance of the contract.

What does this mean for you the Contractor? In each instance, the wording needs to be examined and, if necessary, discussed with the Guarantor – you need to understand whether you are contracting to receive an on-demand guarantee as a primary obligation placed on a Guarantor or whether the Guarantee is akin to a suretyship, which is conditional on underlying performance. Often the wording of the guarantee is not examined at the inception of the contract and the document is simply treated as a matter of process and filed away with the other contract documents, and regrettably this realisation is only emerges when a dispute arises. By then, unfortunately, the proverbial horse would have already bolted to remedy the expectations of the contracting parties.

Why do I want to avoid calling on a guarantee? It is important to remember that the Contractor wants to avoid a Guarantee from being called up at all costs as it will have a severe impact on the Contractor's credit status, reputation, and can potentially lead to the liquidation of the Contractor. Even if liquidation is avoided, the damage to the Contractor's reputation could prevent Guarantors from supporting the Contractor with future contracts and / or drastically alter the premium and collateral terms. Guarantees are similar to credit or financing a business in that they finance your risk, and that the Guarantor has right to indemnity in the event that the Guarantee be called up.

What are the costs involved?
Please play around with our pricing tool to understand the costs that are involved. You can find it here.