OPERATIONS MANUAL
POLICIES AND PROCEDURES

These policies and procedures were prepared for use by ADB staff and are not necessarily a complete treatment of the subject. This *Operations Manual* was prepared by the Office of the General Counsel (OGC) and issued by the Strategy, Policy, and Partnerships Department with the approval of the President and is subject to compliance review. Questions may be directed to OGC.

GUARANTEE AND SECURITY ARRANGEMENTS FOR ADB LOANS

A. Introduction

1. Article 11 of the Agreement Establishing the Asian Development Bank (the Charter) states that ADB may provide or facilitate financing to any member, agency, instrumentality, or political subdivision of a member, entity or enterprise operating in the territory of a member, or international or regional agency concerned with the economic development of the region. Article 15.2 of the Charter provides that, if the recipient of loans or guarantees of loans is not a member, ADB may, when it deems advisable, require that the member in whose territory the project concerned is to be carried out, or a public agency or any instrumentality of that member acceptable to ADB, guarantee the repayment of the principal and the payment of interest and other charges on the loan in accordance with the terms thereof.[1]

B. The Policy

2. When making a loan to a member, ADB may generally rely on the full faith and credit of the member for repayment of the loan. When making a loan to a nonmember, a guarantee by the relevant member is the most effective means of protecting ADB’s interests.

C. Scope of the Policy

3. In making a loan to a developing member country (DMC), ADB pays particular regard to the financial viability of the concerned project and the creditworthiness of the proposed borrower. However, ADB, like any financial institution, must consider whether to take additional measures to protect itself in the event of default by the borrower.

4. When ADB makes a loan to a DMC, the full faith and credit of the member stands behind the obligations of repayment. Other than in exceptional circumstances, no special safeguards to protect ADB in the event of default by the borrower are considered necessary.

5. When ADB makes a loan to an agency, instrumentality, or political subdivision of a member, it must examine in detail the borrower’s standing in terms of the full faith and credit of the DMC government. To the extent that such standing falls short of the full faith and credit of the DMC government, the fullest protection against default by the borrower may be possible only through securing for the loan a guarantee from the DMC government.

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[1] This *Operations Manual* section does not deal with policies and procedures regarding guarantee operations of ADB for loans from other creditors, nor with ADB’s private sector operations.

6. When the borrower is any other entity or enterprise in the territory of a DMC, ADB needs to consider whether to obtain a guarantee from a third party, e.g., the DMC government, and/or to obtain from the borrower some other appropriate form of security to protect itself in the event of default by the borrower. In general, a guarantee by the relevant DMC government is the most effective means of protecting ADB's interests. Therefore, ADB normally protects itself against default by obtaining a government guarantee from the DMC government concerned. If the DMC government lacks the necessary authority to issue or grant the guarantee, consideration is given to making the loan to the DMC government for onlending to the nonmember, or through a public agency that can, in effect, pledge the full faith and credit of the DMC government. Alternatively, the loan might be made through a public agency when the DMC government is empowered to guarantee the loans to such agency. These considerations are particularly applicable in the case of loans from Special Funds or concessional resources. [2]

7. When the borrower is a regional or international agency, appropriate safeguards against default by the borrower depend on the character and composition of the agency. If member governments participate in the agency, ADB has to determine the extent to which they have subscribed to the financial liabilities of the agency to determine the appropriate safeguards. If such an agency is not formed on the basis of participation of member governments, its status as a borrower may legally or virtually be the same as a private entity borrowing from ADB and may involve nearly the same factors in the consideration of safeguards against default.[3]

8. Notwithstanding the above, ADB may require security to be granted to it through the operation of ADB's negative pledge clause (NPC). As part of the sovereign lending legal framework, ADB and other multilateral development banks (MDBs) typically require NPCs to be included as part of their legal agreements to enable them to provide loans to their borrowers without seeking security in respect of the MDB's debts.[4] ADB's loan regulations,[5] which are incorporated by reference into ADB's loan agreements, include NPCs that restrict (subject to limited exceptions in the loan regulations) the creation of security in favor of creditors over (i) assets of the DMC borrower or guarantor in respect of any foreign currency debt; or (ii) assets of a non-DMC borrower in respect of any debt. If such security is to be granted, ADB's NPC requires that (i) such security will equally and ratably secure the debts owed to ADB under its sovereign loans to the relevant DMC borrower and to non-DMC borrowers for loans where ADB is the beneficiary of a sovereign guarantee; or (ii) ADB will be granted an equivalent security in respect of such sovereign loans.

9. ADB's standard form of government guarantee agreement gives ADB the legal right of prompt collection from the guarantor as soon as a qualifying default occurs. This empowers ADB to demand repayment of the loan without the necessity of prior demand on the borrower. The

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[2] ADB. 2016. *Ordinary Operations (Concessional) Loan Regulations and Revised Ordinary Operations Loan Regulations, Special Operations Grant Regulations, and Externally Financed Grant Regulations*. Manila.
[3] OM Sections D9 (Guarantee Operations) and D10 (Private Sector Operations) provide guarantee and related policies applicable to ADB's private sector operations.
[4] ADB. 2021. *Revised Ordinary Operations Loan Regulations*. Manila.
[5] As of the date of this *Operations Manual*, the NPC is set out in ADB's *Ordinary Operations Loan Regulations* (Section 7.10) and *Ordinary Operations (Concessional) Loan Regulations* (Section 6.02), issued in January 2022.

guarantee agreement provides that the obligations of the guarantor will not be impaired by any extension of time or other concession granted to the borrower, or by failure of ADB to press available remedies. It also reinforces the provision of ADB's loan regulations that the validity and effect of a guarantee agreement is not affected by municipal or any other applicable law.

Bases

i ADB. 1970. *Guarantee and Other Security Arrangements*. Manila (R45-70).
ii ADB. 2021. *Revised Ordinary Operations Loan Regulations*. Manila (R75-21).