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Insurance issued by the Foreign Credit Insurance Association (FCIA) not only allows commercial banks to finance or participate in trade transactions when their own internal credit limits or regulatory lending limits would ordinarily prevent them from extending credit, but it can also provide an unusual niche of profitability. This Article explains the utility of the pertinent FCIA policies, pinpoints some possible legal risks for a bank in each policy, and emphasizes new products developed by FCIA to fit closely banking needs.

I. FCIA'S UNIQUE STRUCTURE AND RELATIONSHIP WITH EXIMBANK

FCIA, as a result of its unusually cooperative relationship with the Export-Import Bank of the United States (Eximbank), offers the benefit of United States government-backed credit insurance against both political and commercial risk, and simultaneously affords the exporting and financial community the advantages and efficiency of working with a private sector entity.

Congress created Eximbank as an agency of the United States under the Export-Import Bank Act of 1945.[1] Eximbank was authorized, *inter alia,* to provide insurance against political and credit risk of loss.[2] Subsequently, Congress also authorized Eximbank to issue insurance in conjunction with "insurance companies . . . or groups thereof," and to employ such insurance companies or groups "to act as its agent in the issuance and servicing of" this insurance.[3]

1. 12 U.S.C. § 635(a)(1) (Supp. III 1985).
2. Section 2(c)(1) of the Export-Import Bank Act of 1945. In 1975, Congress amended the Act to authorize Eximbank to "insure, coinsure, and reinsure against political and credit risks of loss." 12 U.S.C. § 635(a)(1) (Supp. III 1985).
3. 12 U.S.C. § 635(c)(2) provides that:

In 1961, at the request of the Kennedy Administration, Eximbank encouraged a group of the nation's leading private commercial insurance carriers (member companies) to join in the creation FCIA. Pursuant to 12 U.S.C. § 635(c)(2), FCIA provides protection against the commercial and political risks to which United States exporters are exposed when they sell to foreign customers on credit terms. For over twenty years, Eximbank and FCIA have negotiated agency agreements under which Eximbank has consistently reappointed FCIA as its agent.

Each insurance policy divides its coverage into two categories, commercial credit risk and political risk.[4] Until 1983, FCIA insured against the commercial credit risks, and Eximbank directly insured against the political risks. FCIA only acted as Eximbank's agent in matters of political risk. Through various reinsurance agreements, Eximbank annually reinsured the liability of FCIA's member companies for commercial risks when specific foreign buyer and country "stop losses"[5] were reached. The reinsurance limited the ultimate liability for the member companies and the insureds enjoyed the comfort of United States government backing in the event of catastrophic losses to FCIA.

In 1983, the member companies requested that they be relieved of liability under the FCIA structure, due in part to dramatically increased risks in foreign markets. In September 1983, FCIA and Eximbank concluded a reinsurance agreement under which Eximbank agreed to reinsure FCIA for all commercial losses above premium income.[6] Under the agreement, member companies were relieved of any future liability. Eximbank continued to act as the direct insurer for political risk. Today, FCIA functions under the September 1983 reinsurance agreement. Despite these changes in structure, FCIA avenues for private risk participation remain open. FCIA offers a wide variety of insurance policies.

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[t]he Bank may issue such guarantees, insurance, coinsurance, and reinsurance to or with exporters, insurance companies, financial institutions, or others, or groups thereof, and where appropriate may employ any of the same to act as its agent in the issuance and servicing of such guarantees, insurance, coinsurance, and reinsurance, and the adjustment of claims arising thereunder.

4. FCIA's newer policies, beginning with the Bank Export Credit Insurance Policy for Letters of Credit (Bank Letter of Credit Policy) first issued in June 1985, no longer use the terms commercial and political risk. Instead, the policies enumerate the risks by number and assign specific numbered risks to the account of FCIA or Eximbank. Percentages of coverage are now equal across all enumerated risks.

5. Each year the reinsurance agreements were renegotiated to set new "stop losses," which are maximum claim payment amounts for each country and buyer above which the member companies would pass all liability to Eximbank.

6. Premium income is the total income of the association earned by premium charges to insureds for the policies.

Depending on the FCIA policy, either the United States exporter or a bank may be the policyholder. Although exporters often hold a FCIA policy for their own risk protection, rather than for enhancement of their ability to obtain financing for their export transactions, it is the purpose of this Article to examine the financing utility of FCIA policies. Therefore, it will be assumed that when exporters are FCIA policyholders, they have assigned the insurance proceeds to the institution that is financing the export transactions.[7]

II. THE LEVERAGING EFFECT OF FCIA INSURANCE ON THE CAPACITY OF A FINANCIAL INSTITUTION TO EXTEND CREDIT TO FOREIGN OBLIGORS

A. The Effect

For banks desiring to finance exports into transitional or difficult foreign markets, effective backing of the United States government through FCIA insurance on Foreign receivables allows them to leverage their limited legal lending capacity and to satiate their credit appetite for foreign risk. Credit limitations imposed on banks that provide export loans fall into three categories. The first limitations are those of the national bank lending limits.[8] The lending limits are subject, however, to certain exceptions. One such exception is that

> [l]oans and extensions of credit to or secured by unconditional takeout commitments or guarantees of any department, agency, bureau, board, commission, or establishment of the United States or any corporation wholly owned directly or indirectly by the United States shall not be subject to any limitation based on capital and surplus.[9]

As an independent corporate agency of the United States, Eximbank enjoys substantial government backing: all contractual liabilities incurred under the authority of Eximbank's governing statute constitute full faith

7. As an overall part of FCIA's business, the use of the policies for financing appears to have grown during the past five years. Exact figures are not available to indicate what percentage of export volume has been financed under policies held directly by exporters. Premiums earned under policies held directly by banks, however, have risen to 40% of all premiums collected by FCIA as of 1985.

8. 12 U.S.C. § 84(a)(1) (Supp. III 1985). The national bank lending limit provides, in part, that total loans and extensions of credit by a national bank to any person outstanding and not secured as described therein may not exceed 15% of the unimpaired capital and surplus of the bank.

9. 12 U.S.C. § 84(c)(5) (Supp. III 1985).

and credit general obligations of the United States.[10] Two questions remain. The first question is whether FCIA as a private association of insurance companies, although reinsured by an agency of the United States Government, is a "corporation wholly owned directly or indirectly by the United States."[11] While there is no definitive answer, the Chief Counsel of the Comptroller of the Currency, in a series of cases, seems to suggest that FCIA might qualify as such a corporation for the purpose of issuing credit insurance sufficient to exempt certain loans from the bank lending limits.

The second question is whether the federal government guarantee on the loan must be unconditional. For national bank lending limit purposes a guarantee or commitment is unconditional:

> if the protection afforded the bank is not substantially diminished or impaired in the case of loss resulting from factors beyond the bank's control. Protection against loss is not materially diminished or impaired by procedural requirements, such as an agreement to take over only in the event of default, including default over a specific period of time, a requirement that notification of default be given within a specific period after its occurrence, or a requirement of good faith on the part of the bank.[12]

Thus, some doubt exists whether FCIA's policies are sufficiently unconditional. The Chief Counsel of the Comptroller of the Currency has found that FCIA's Master Export Credit Insurance Policy (Master Policy),[13] under which banks took an assignment of proceeds, sufficiently met the unconditionality requirements mentioned above.[14] The Master Policy has now been rewritten and renamed the Comprehensive Multi-Buyer Credit Insurance Policy (Multibuyer Policy).[15] Although no opinion of the Chief Counsel of the Comptroller of the Currency on the new Multibuyer Policy has to date come to the writer's attention, it seems likely that the Multibuyer Policy would rise to or exceed the levels of unconditionality expressed by the earlier Master Policy.[16]

The second limitation on foreign loans is the federal bank examin-

10. 42 Op. Att'y Gen. 327 (1966).

11. *See* 12 U.S.C. § 84(c)(5) (Supp. III 1985) and text accompanying note 9.

12. 12 C.F.R. § 32.6(e)(4) (1984).

13. These policies were issued directly to exporters prior to April 1986.

14. 12 C.F.R. § 32.6(e)(4) (1984).

15. One of the goals of the rewriting was to make the policy coverage more predictable and quantifiable. Revision has met with the enthusiastic approval of banks which will take assignments of proceeds thereunder.

16. Because the opinions of the Chief Counsel of the Comptroller are issued on a case by case basis, bank counsel should seek new opinions as FCIA policies are revised.

ers' ratings of loan portfolios. The examiners classify loans to foreign countries according to risk and derive an overall rating of a bank's loan portfolio. Ratings must be maintained within a reasonable range. FCIA coverage is recognized widely as transferring the foreign risk to the status of a United States government risk on the insured portion of the loan, thereby benefitting the overall rating.

The third limitation, which for many banks is the most essential, is the bank's internal judgment on the prudence of incurring risk in particular markets. Banks periodically deem certain foreign markets to be totally undesirable. Moreover, they often strive to diversify their risk across several foreign markets. To accomplish this diversification, banks impose internal limitations to prevent over-concentration of a loan portfolio in certain markets. Again, banks commonly accept the FCIA insured portion of a loan as exempt from their internal limitations on foreign risk.

B. The FCIA Insured Portion of a Loan

The above discussion contains several careful references to the FCIA insured portion of a loan. The typical FCIA coverage requires the policyholder to retain a portion of the risk, commonly referred to by insurers as "coinsurance" or "retention." This portion of the risk helps assure that the policyholder maintains an interest in the transaction. Furthermore, retention encourages a careful credit decision by the policyholder, accurate documentation, and participation by the policyholder in subsequent recovery efforts. For nonsovereign obligors, the retention requirement under an FCIA policy is normally five or ten percent of the insured transaction, unless underwriters determine that a higher retention is necessary due to the nature of the risk. For sovereign obligors, insurance generally is afforded at one hundred percent with no retention requirement. When a sovereign obligor defaults, recovery success is beyond the insured's reasonable control.

When financing is dependent upon FCIA coverage under a policy issued directly to the bank, that bank must record the applicable retention as foreign risk. Nonetheless, the FCIA policy, even with retention, enables a bank to highly leverage its foreign export loan capabilities for a limited utilization of foreign country risk allocations. For example, if a \$100 export transaction is afforded ninety percent coverage under a bank's FCIA policy with a required ten percent retention, the bank can finance the entire \$100 of the transaction, yet record only a \$10 foreign risk.

If the exporter is the policyholder, the exporter must keep the retention for his or her own account. Consequently, a bank which takes assignment of an exporter's FCIA policy may wish to finance only that portion of the transaction that is fully covered by the insurance. The bank may take an assignment of policy proceeds and finance whatever amount it negotiates with the exporter. In the above example, the bank can record the financing of ninety dollars or less without foreign risk.

III. THE REDEVELOPMENT OF FCIA POLICIES TOWARD A STANDARD OF INCREASED QUANTIFIABILITY

Historically, FCIA policies, including those issued directly to banks, insure only valid credit obligations. The structure of the coverage of these policies, as well as their specific exclusions, suggests a number of circumstances under which coverage would not be perfected. While exporter policyholders can control or prevent most noncoverage situations, banks which accept an assignment of proceeds under an exporter's policy or which actually become the policyholder cannot have *total* control over these situations.[17]

For example, coverage may be denied because the requirement that the products be manufactured in the United States is not met. Only credit obligations that result from the export of United States goods can be insured.[18] The exporter may be in an excellent position to know whether the goods meet this requirement; the financing bank, however, will know only that the exporter's documents state on their face that the goods were manufactured in the United States. In either case, a subsequent finding by FCIA that the goods did not meet this requirement may result in a claim denial.[19] Additionally, the exporter may more easily

17. The concept of *total* control is intended to be distinct from control sufficient to satisfy 12 C.F.R. § 32.6(e)(4) (1984). *See* text accompanying note 12.

18. For products shipped under short-term credit obligations (usually less than 180 days but extending to 360 days for certain capital goods), the policies make the following statement about insured products: "No more than 49% of its value, exclusive of price mark-up, may consist of labor, raw materials, component parts or any combination thereof originating or manufactured outside the United States." Short Term Comprehensive Multi-Buyer-Export Credit Insurance Policy, art. 4, § A(2). For medium-term transactions, the policies provide a 100% requirement which may be lessened at the time of underwriting to allow a small percentage of products which are not manufactured in the United States.

19. Until June 1985, most FCIA policies issued directly to banks were a form of the Master Policy with a special endorsement for banks. In November 1985, FCIA introduced a Bank Export Credit Insurance Policy for Letters of Credit (Bank Letter of Credit Policy) which placed the bank in documentary position only for letter of credit confirmations and negotiations. In November 1986, FCIA introduced a new Bank Buyer Credit Policy which is also of a documentary nature. For a one-year transitional period for certain types of transac-

control other types of fraud in the transaction that are not apparent to the bank which is examining the documents.[20] Nonetheless, fraudulent documents such as invoices or bills of lading will result in a claim denial to a bank just as they result in a claim denial to an exporter.

Financial institutions particulary are concerned with possible disputes between the exporter and the foreign buyer about the quality or type of products. Again, the bank that typically relies upon documents in deciding to finance the export transactions may find that coverage is denied because of product disputes over which it had no control.

In the above examples the exporter is conceivably in a better position to control the problems. Historically, the policies have also contained other nonquantifiable aspects of equal impact on both exporters and financial institutions. The historical division of coverage percentages, which was ninety percent coverage for commercial risks and one hundred percent coverage for political risks, exemplifies the problem. Commercial risks were defined as protracted default or insolvency of the foreign buyer. Political risks included not only war, expropriation, or cancellation of import and export license, but also the significant risk of currency inconvertibility. In a broad sense, inconvertibility is the inability of the foreign buyer to obtain United States currency in a lawful market in the buyer's country and to effect transfer of the currency to the insured in the United States. True inconvertibility is a difficult term to define accurately because currency conversion and transfer procedures vary greatly from country to country and from time to time. In effect, the definition of inconvertibility used by the board of Eximbank is narrow. Consequently, if foreign currency is available in *any* lawful market, whatever the size of the market and whatever the rate of exchange, there is no inconvertibility coverage under the policy.

When the conditions are not deemed sufficient to meet the definition of inconvertibility, the foreign buyer's failure to pay is regarded as a protracted default and, therefore, a commercial risk which is only ninety percent covered. Exporters or banks which had broadly assessed their coverage as one hundred percent for currency transfer risks were often disappointed at claim time when the issuer treated the nonpayment as a commercial loss and, therefore, had afforded them only ninety percent

tions, many banks will continue to hold the old policy to which these arguments are particularly appropriate.

20. For example, exporters will know whether goods were actually shipped and by what means. They will also know whether their billing invoices represent the costs of those goods. Cleverly created false versions of these documents, however, may appear genuine to the examining bank.

coverage. FCIA solved this problem by equalizing risk coverage, a concept first introduced into certain revised policies in 1985. Although coverage for both commercial and political risk is equalized in an amount less than one hundred percent in the revised policies (unless the obligor is sovereign, in which case coverage for all risks is one hundred percent), policyholders prefer the new approach. This feature is of particular importance to the financial entity that requires predictable and quantifiable risk.

Of equal concern to exporters and financial institutions were a number of vaguely defined terms in the former policy texts. For example, the FCIA policies historically required the agreement of the insured not to contract with or ship products to a foreign buyer with knowledge of a buyer's financial difficulty. Obviously, an exporter or a financial institution may disagree with an insurer regarding what constitutes "financial difficulty." The new and more quantifiable requirement is that an insured may not enter into an insured transaction with the buyer "in the event that any amount owing from the *buyer* . . . to the *insured* on any transaction is overdue more than 90 days or if the *insured* has knowledge of the *buyer's* . . . insolvency."[21] Numerous clarifications such as this have been and are continually being made throughout the FCIA policies. Each clarification is made with the specific purposes of making the scope of coverage clear for the exporter and clearly quantifiable for the bank financing the export transaction. Another noteworthy attempt at quantification in all new policies is the agreement of FCIA to process claims within sixty days of the filing of a completed proof of loss. Such a provision enables the financial institution to plan more precisely funding in the event of a default.

IV. FINANCING ON THE BASIS OF AN ASSIGNMENT OF PROCEEDS UNDER AN EXPORTER'S POLICY

The most common FCIA policy held by exporters is the Multibuyer Policy.[22] The coverage is equalized, the time for payment of claims is specified, and the language is greatly clarified from the old Master Policy. Although the Multibuyer Policy as a whole is more quantifiable than past exporter policies, a bank that provides financing on the basis of an assignment of proceeds of the Multibuyer Policy must be wary of a number of risks that cannot be readily discerned from a review of

21. Short Term Comprehensive Multi-Buyer Export Credit Ins. Policy, art. 7, § B.
22. *See supra* notes 13-16 and accompanying text.

documents.[23]

Another group of risks difficult for the bank to control generally is referred to as the risk of the exporter's performance under the policy. Accordingly, policies impose an absolute requirement on the exporter policyholder to report shipments and to pay any premium. Similarly, shipments must comply with the FCIA-issued credit limits for the particular foreign buyer.[24] If FCIA also affords the exporter a discretionary credit limit, there is a risk that the exporter will not comply with the policy's requirement to obtain, prior to shipment, credit reports evidencing the buyer's creditworthiness for the insured transaction or, alternatively, a record that the buyer has had prompt repayment experiences, as defined by the policy.[25]

Additionally, FCIA may deny the exporter's claim for a number of other reasons, such as failing to file a timely claim against FCIA, shipping to a buyer who is more than ninety days overdue, or failing to file certain reports that are required under the policy. Although a denial of the exporter's claim means that the assignee bank will not receive any policy proceeds, the financial institution cannot directly control the exporter's performance risks by making an assignment of proceeds under an exporter policy. The institution can only hope to carefully evaluate and monitor the exporter's compliance with the policy.

The Multibuyer Policy requires that exporters offer FCIA a spread of export credit risk by insuring many or all of their exports from the United States. The Short Term Single Buyer Policy, a recent innovation, is issued for transactions with one foreign buyer, only after the payment of a premium. Although a bank taking an assignment of proceeds under this policy is not protected against the uncontrolled risks, much of the exporter performance risk has been removed. Because the premium is paid and specific credit limits are determined before policy issuance, financial institutions are expected to feel an even greater degree of comfort when they are assignees of proceeds on such policies.

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23. *See supra* notes 18 and 20, and accompanying text.

24. Under the Multibuyer Policy, the exporters may be given a discretionary credit limit that allows them to make their own credit decisions, up to certain limits for buyers in specific countries, and report shipment and pay premiums to FCIA after the fact. For higher credit amounts, FCIA must specifically approve the financial condition of the foreign buyer and will specify in a credit limit endorsement particular terms under which it will provide coverage.

25. When a discretionary credit limit endorsement is added to a policy, the insured must gather specified credit reports or evidence of prompt repayment experience. If shipments do not comply with these requirements or if the insured is unable to produce evidence of such compliance at claim time the shipments may be deemed uninsured.

V. THE NEW AND QUANTIFIABLE "DOCUMENTARY POLICIES" FOR BANKS

In June 1985, FCIA introduced its Bank Letter of Credit Policy to insure the reimbursement obligation of a foreign bank issuing a letter of credit confirmed or negotiated by the insured bank. The policy is constructed in close conformity to the Uniform Customs and Practice for Documentary Credits (UCP)[26] and is, therefore, of a documentary nature.

Under this policy, certain Eximbank program requirements, such as United States content of the exported product, are reduced to a form of exporter certificate.[27] The bank's duties under the policy are those under UCP. The exporter certificate is simply another document necessary for the transaction. Product disputes fall into the area of the commercial transaction for which the bank is not responsible under UCP or the FCIA Bank Letter of Credit Policy. Numerous United States banks have enthusiastically received this policy.[28]

In January 1987, FCIA will make its new Bank Buyer Credit Policy, which insures the direct credit obligations of foreign buyers of United States goods, available to banks. Again, the policy is being structured on a documentary basis. The heart of the policy is the minimum requirements established by FCIA for an insurable credit obligation between the bank and foreign buyer. If these requirements are met, uncontrolled risks arising out of the export transaction will not result in claim denial if an exporter certificate form has been obtained from the exporter.

Both the new Bank Letter of Credit and Bank Buyer Credit Policies, in addition to providing a high level of quantifiablility, allow the bank policyholder to obtain recourse against the exporter for the required retention. Consequently, a bank policyholder can further leverage its foreign lending ability by transferring the remaining foreign risk that it was required to hold as retention to the status of exporter risk.

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26. INTERNATIONAL CHAMBER OF COMMERCE, UNIFORM CUSTOMS AND PRACTICE FOR DOCUMENTARY CREDITS ICC PUB. NO. 400 (1983 Revision).

27. The Bank Letter of Credit Policy supplies a printed certificate form to be completed and signed by the exporter, who is usually also the beneficiary, under each letter of credit transaction that is to be insured. Among other clauses, the exporter certificate contains statements of the price of the goods, their United States content, their shipping date, and their destination.

28. As of the date of this article, over 90 banks hold the policy and have paid required minimum annual premiums.

VI. CONCLUSION

Banks with the careful asssistance of counsel should evaluate the recently enhanced FCIA coverage for banks financing export transactions. Both the increased quantifiability of new FCIA policies for banks and the ability to obtain recourse on the retention suggest areas of profitability for bank financing of United States exports without exhausting scarce foreign lending capacity.