

Bank Guarantee as a Means of Securing Contract Performance under the Law of the Republic of Serbia

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Abstract

Bank guarantees are the most widely used instrument to secure contract performance in commercial law, both nationally and internationally. They are commonly employed in sales contracts and during the execution of foreign investment projects. Establishing a bank guarantee is prompt and effective falling under neutral banking operations. As the number of business entities has grown significantly, there has been a corresponding increase in commercial contracts requiring secured performance. Despite the advantages of swift transactions at both levels, business entities face economic and legal risks that drive them to secure contracts most effectively to protect their interests and achieve their business goals. In this context, the bank is essential in fostering successful business collaborations. Given the importance and complex nature of bank guarantees in today's legal transactions, this paper examines current issues and challenges related to the key aspects of bank guarantees as a means to secure contract performance, including their efficiency and speed in enforcement, along with their advantages and disadvantages, with particular reference to judicial decisions and electronic bank guarantees in light of innovative technologies. It reviews existing statutory provisions and provides a comparative analysis across various levels. The paper focuses on eliminating uncertainties surrounding the bank guarantee institution to promote more secure business practices.

Introduction

Before adopting the Law on Obligations 1978 in the Republic of Serbia, bank guarantees were only incidentally regulated through the basic principles of obligation and commercial law. It was not until this law was enacted that bank guarantees were legally defined. The Law on Obligations outlines their concept, the discharge of obligations under a guarantee, counter-guarantee, and assignment of rights under a guarantee and guarantees "without objection." In 1978, the

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International Chamber of Commerce in Paris adopted the Uniform Rules for Contractual Guarantees, which the Republic of Serbia subsequently embraced. With the adoption of these standards, the final implementation of bank guarantees began in 1982 (Vasilić, 1995).

Given the practical application of bank guarantees to secure contract performance in legal transactions and the lack of detailed statutory regulation, several issues have arisen, including increasingly frequent cases of fraud (demand guarantees). Consequently, this paper aims to define the concept of a bank guarantee to distinguish it from similar instruments and facilitate its legal application. The paper also seeks to highlight legally relevant facts essential for its full enforcement, as judicial decisions reveal that users of bank guarantees are often negligent in submitting claims for enforcement, frequently resulting in a denial of their right to receive monetary compensation. The research concludes that the bank guarantee (hereinafter: guarantee) is a highly complex instrument that demands detailed and thorough analysis. The same applies to electronic bank guarantees, which are addressed only in passing here, in light of the impressive development of the digital economy. The paper's primary objective is to present general solutions concisely.

Legal Nature of the Bank Guarantee

According to Article 1083, paragraph 1 of the Law on Obligations of 1978 (hereinafter: LOO), a bank guarantee is defined as the bank's obligation to the beneficiary (user) to settle a monetary obligation if a third party fails to fulfil its due obligation, provided that the conditions specified in the guarantee are met. Essentially, it is a declaration by the bank committing to discharge the monetary obligation for the beneficiary if the third party does not perform upon maturity. In this process, the bank is neither the creditor nor the debtor, but rather functions as a form of guarantor (Đurović, S. Đurović, J. & Đurović, M., 2010).

The broad formulation of a bank guarantee allows banks and other guarantee providers to issue all known and customary guarantees in banking practice (Blagojević, B. & Krulj, V., 1983).

The extensive legal definition of a bank guarantee implies that at least three parties are involved in the guarantee transaction: the creditor (beneficiary), the debtor from the underlying legal transaction (principal), and the bank that issues the guarantee (guarantor). These parties establish three distinct legal relationships,

each differing in nature and legal effects (Blagojević, B. & Krulj, V., 1983).

Some theorists define a bank guarantee as an instrument for securing payment in international transactions (Vunjak, N., & Kovačević, Lj., 2006), while others emphasise that a bank guarantee, as a unilateral legal act, forms the basis rather than merely serving as a means of security (Jankovec, I., & Mićović, M., 2006). The debate over its nature is most pronounced regarding whether it constitutes a unilateral legal act or a contract.

Supporters of the unilateral legal act perspective argue that a bank guarantee cannot be regarded as a contract because its creation does not require the mutual consent of two parties, but rather the bank's consent as the guarantor. Conversely, proponents of the contract theory contend that contracts can be formed explicitly or implicitly, and that beneficiaries often express a clear preference to obtain a bank guarantee from a specific bank, with the right to retain or transfer it, thereby indicating their intent to enter into a contract. This viewpoint holds that the bank guarantee is a contract rather than a unilateral legal act (Vasilić, J., 1995). Those who view the bank guarantee as a unilateral legal act note that the LOO does not classify it as a contract, having defined it conceptually instead.

Thus, when the beneficiary expresses their intention regarding the bank guarantee when concluding the underlying contract and subsequently retains or transfers the guarantee, they have actively and implicitly manifested their will to form a contract. This counters the theoretical objection that no contract exists due to the absence of the beneficiary's will (Pavičević, B., 1989).

Furthermore, to secure obligations, the bank guarantee falls under personal security measures and is often equated in practice with a surety agreement. In this section, it is essential to distinguish between the two. A surety implies the personal liability of a third party to the creditor if the debtor fails to fulfil the due obligation; this responsibility is assumed by the surety (the third party). A surety is accessory in nature and follows the fate of the underlying transaction, with its duration tied to the term of the main contract.

In contrast, a bank guarantee is an independent transaction, separate from the underlying agreement, and its validity does not depend on the duration of the main contract but rather on the period specified in the guarantee. This principle also applies to the guarantee amount, which is determined by the guarantee itself

rather than the amount stated in the underlying agreement.

Thus, a bank guarantee constitutes a separate obligation from the main legal transaction, and its validity remains intact regardless of the validity of the primary transaction. In other words, the bank guarantee will remain valid even if the main legal transaction is annulled.

It is pertinent to note the decision of the Supreme Court of Serbia, Case No. Pev. 74/98 dated December 16, 1998 – Judicial Practice, Bulletin No. 4/1999: “The invalidity of the main legal transaction for which a guarantee was issued with a ‘without objection’ clause does not affect the validity of the bank’s obligation under the issued guarantee. Therefore, the bank may only invoke objections arising from the terms of the guarantee (such as its validity period) and not the objection of nullity of the legal transaction for which the ‘without objection’ guarantee was provided.”

From the explanation: “The Commercial Court upheld the plaintiff’s claim, ordering the defendant to pay a specified sum with interest in accordance with the Law on the Rate of Default Interest. The Higher Commercial Court rejected P’s M’ AD appeal and confirmed the first-instance decision. The Supreme Court of Serbia found that the revision by the defendant and the plaintiff was unfounded.”

The claims presented in the revision regarding the incorrect application of substantive law and the misinterpretation of general rules on unjust enrichment as per Article 212 of the Law on Obligations (LOO) are unfounded. The Higher Commercial Court correctly concluded that all claims made in the appeal concerning the bank-guarantor’s attempt to link the payment under a first-demand guarantee with its business relationship established with DD “M” from B, as the principal of the guarantee, are baseless. This is because, under a first-demand guarantee, no objections related to the underlying transaction can be raised. Thus, the revision incorrectly claims that the voidability of the guarantee arises not only from the absence of goods, which the guarantor mistakenly believed existed (as noted by the appellate court), but also from the lack of valid proof regarding the origin and legality of the debt assumed by PP “M” from DP “J” under the debt assumption agreement and its annex prepared by “S.B.”, and for which the defendant issued the guarantee. The revising party suggests that the plaintiff allegedly misused interbank business trust and violated principles outlined in Articles

12, 15, and 16 of the LOO, thereby causing the transfer and guaranteeing of a non-existent or illegal claim.

However, there is no evidence of evident fraud by the guarantee beneficiary that would justify lifting the restriction against objections by the bank-guarantor based on the underlying transaction, as the LOO explicitly establishes the principle of “full abstraction” of the “without objection” guarantee (Article 1087 LOO). Consequently, the invalidity of the underlying transaction unquestionably does not impact the validity of the bank’s obligation under an independent guarantee. The bank can only raise objections arising directly from the terms stipulated in the guarantee (such as its validity period).

Given the above, the same rules should not apply to these two entirely separate legal instruments. The regulations governing bank guarantees differ from those governing surety agreements. Similar differences exist between bank guarantees and insurance contracts. Thus, one fundamental difference, among others, is that an insurance contract is a bilateral, onerous contract that covers multiple risks. In contrast, a bank guarantee typically covers the risk of non-performance of a contractual obligation, including delay in performance or defective performance.

Therefore, it logically follows that a bank guarantee possesses a high degree of independence and practical applicability, involving multiple completely independent actions. Consequently, it should not be equated with other legal instruments, such as sureties, insurance contracts, bill-of-exchange guarantees (aval), bill-of-exchange acceptances, lombards, pledges, and similar legal mechanisms.

Essential Elements of the Bank Guarantee

Before defining the essential elements of the research topic, it is useful to briefly outline the basic principles underlying bank guarantees, as these principles significantly influence the execution of guarantees and the application of legal norms. According to Prof. Dr. Božidar Pavićević, the core principles of bank guarantees are the principle of written form, the principle of independence, and the principle of fixed guarantee obligations.

Under Article 1083, paragraph 2 of the Law on Obligations (LOO), bank guarantees must be issued in written form. They must always specify a monetary obligation, even when they secure a non-monetary

obligation. The written form ensures clarity and precision regarding the bank's obligations. For a guarantee to be legally valid, it must include the essential elements of an agreement. Although the LOO does not explicitly list these essential elements, it is generally accepted that they contain the elements agreed upon during the conclusion of the underlying transaction, as well as elements inherent to the nature of the bank guarantee itself (Jankovec, I., & Mićović, M., 2006).

The principle of fixed guarantee obligation refers to the requirement that the bank must clearly specify an amount in monetary units or as a percentage of the underlying transaction's value. The bank's obligation cannot exceed the amount stated in the guarantee. Thus, the amount or percentage specified in the guarantee is fixed and unalterable.

Regarding the principle of independence, previously discussed, it suffices here to reiterate that a bank guarantee is a separate legal transaction established exclusively between the guarantor bank and the principal. Consequently, the guarantor bank cannot invoke objections arising from the underlying transaction (with the exceptional allowance that the bank may object if the guarantee beneficiary has already received payment for the secured claim from the principal, provided this is demonstrable) (Jankovec, I. & Mićović, M., 2006). Permissible objections generally concern the validity of the guarantee itself, the timeframe specified in the guarantee, or the bank's personal objections against the beneficiary, for example, compensation claims. Article 1087, paragraph 1 of the LOO explicitly stipulates that if a bank guarantee includes clauses such as "without objection," "on first demand," or equivalent wording, the bank may not invoke objections against the beneficiary that the principal debtor could assert regarding the secured obligation.

The Decision of the Supreme Court of Serbia, Prev confirms this. 348/94 dated 23 November 1994 – Judicial Practice of Commercial Courts Bulletin No. 2/1995: "In the case of a bank guarantee issued 'without objection,' the guarantor-bank cannot raise objections concerning the existence or validity of the underlying agreement secured by the guarantee. The bank may only raise objections based solely on the guarantee itself."

From the explanation: "The Commercial Court's judgment required the defendant to pay the plaintiff a specified amount in foreign currency based on the guarantee issued. The Higher Commercial Court in B rejected the

defendant's appeal as unfounded. The Supreme Court of Serbia rejected the defendant's revision appeal.

The case documents indicate that the defendant issued guarantees to the plaintiff, under which the defendant undertook to pay the plaintiff, upon the plaintiff's first demand, any amount the plaintiff had paid to a German bank under a guarantee for the proper execution of work provided to a German investor. The German bank activated the guarantee and requested payment of the disputed amount from the plaintiff's bank.

Based on these facts, the Supreme Court upheld the conclusion of the Commercial Courts that the defendant is obligated to pay the plaintiff the awarded amount under the issued guarantees. The legal basis for this decision is found in Articles 1084 and 1087 of the LOO. The guarantees issued by the defendant to the plaintiff are legally independent from the existence and validity of the underlying agreement, and the guarantee issuer can only raise objections based on the guarantee itself. Since the conditions stated in the guarantees were met, allowing the plaintiff to demand the awarded amount from the defendant under the issued guarantees, and considering the plaintiff's bank had paid the disputed amount to the German bank based on the counter-guarantee, the plaintiff has the right to recover any amount it has paid under these guarantees from the defendant as guarantor or principal.

The defendant's revision claim, arguing that no contract for issuing a bank guarantee existed between the parties, is unfounded. Issuing a bank guarantee establishes a contractual relationship between the issuer of the guarantee and its beneficiary on one side, and between the principal and the guarantor-bank on the other. Therefore, the fact alone that the plaintiff's bank paid the disputed amount to a foreign bank based on the counter-guarantee issued constitutes a valid legal basis for the bank to request reimbursement from the principal (the defendant) for any amounts paid under the guarantee, in accordance with Article 1087, paragraph 2 of the LOO."

Concerning the essential elements of a bank guarantee, it is important to highlight two crucial characteristics that make creditors readily accept it: irrevocability and unconditionality (Đurović, S., Đurović, J., Đurović, M., 2010). Since banks cannot easily withdraw from a previously issued guarantee, clearly defining its essential elements becomes vital. The LOO itself does not explicitly list these essential elements, leading to the conclusion that such elements are those without which

the guarantee would not be legally valid. They include characteristics derived from the nature of the transaction itself, but are also determined by the parties involved.

The essential elements generally recognized by scholars are: the name and registered office of the guarantor bank; the name and registered office of the beneficiary; specification of the underlying obligation secured by the guarantee; the guaranteed amount (i.e., the specific monetary value the bank agrees to pay); the validity period of the bank guarantee; signatures of authorized individuals; place and date of issuance. Additional vital elements include clauses related to the return of the guarantee document, whether the guarantee is denominated in gold or currency, the guarantee number, and any other details the involved parties consider essential.

When issuing a bank guarantee, the reputation and reliability of the issuing bank are extremely significant. "Liquidity, business reputation, and financial stability constitute fundamental prerequisites that invariably motivate creditors or guarantee beneficiaries to accept a guarantee issued by a particular bank possessing these qualities (Blagojević, B. & Krulj, V., 1983)." Thus, the bank's character is crucial, as only banks with these attributes can instil confidence and security in creditors regarding recovering their claims. Bank liquidity and stability are particularly important, especially considering that if the issuing bank ceases to exist, the guarantee it issued also loses validity.

Obligations of the Guarantor Bank

Every legally valid transaction creates rights and obligations for the contracting parties. Regardless of whether the bank guarantee is considered a contractual relationship or a unilateral declaration by the bank, obligations always arise on the side of the bank.

Although there is no consensus regarding the legal nature of bank guarantees, all theorists agree that the guarantor bank's obligations must be clearly specified. According to Prof. Dr. Stevan Šogorov, since the bank guarantee is a unilaterally binding legal instrument, the obligations of the bank must be precisely and explicitly defined (Šogorov, S., 1985).

When issuing a bank guarantee, banks take certain precautionary measures to mitigate potential risks (Antonijević, Z., 1960). Methods of issuing guarantees may vary based on agreements reached by parties in the underlying transaction that the bank's guarantee secures

(Antonijević, Z., 1961). It is indisputable that the guarantor bank issues the guarantee or guarantee letter in its own name and on its own behalf, thereby committing itself to pay the beneficiary if the debtor fails to fulfill the obligation within the agreed timeframe (Antonijević, Z., 1983).

The primary obligation of the bank is to pay the beneficiary a specified monetary amount if the debtor does not meet its obligations on time. If the bank fails to fulfil this obligation, it will be liable to the principal for any resulting damages (Velimirović, M., 1982).

As previously noted, banks discharge their obligations exclusively in monetary terms, reflecting their role as specialised financial institutions primarily involved in payment transactions. In addition to its obligations, the guarantor bank is entitled to reimbursement of any amount it pays and bank commissions from the principal.

The bank is liable for damages resulting from its failure to fulfil obligations outlined in the guarantee—particularly if it does not pay the amount due to the appropriate guarantee beneficiary. Such damages may exceed the amount specified in the guarantee, given that issuing a bank guarantee establishes an independent legal relationship between the bank and the beneficiary, separate from that between the guarantor bank and the principal, or between the principal and the beneficiary. The bank must act on the beneficiary's request for payment even if the requested amount exceeds the actual damage incurred. In such cases, the beneficiary must return any excess amount above the actual damages to the principal (Jankovec, I. & Mićović, M., 2006).

When a bank pays the guaranteed amount to the beneficiary under a bank guarantee, the principal is obligated to reimburse that amount to the bank, including any interest or commission. The bank has the right to receive its commission regardless of whether it has actually paid out the guaranteed amount.

The Decision of the Supreme Court of Serbia, Prev supports this principle. 155/94 dated 23 November 1994 – Judicial Practice of Commercial Courts, Bulletin No. 2/1995: "The guarantor bank is entitled to receive the agreed commission irrespective of whether the guarantee is activated or the guaranteed amount is paid to the beneficiary. Even if the bank guarantee is not activated, the guarantor bank maintains the right to its commission. Furthermore, initiating bankruptcy proceedings against the issuing bank does not affect the

validity of the bank's obligation; in such a scenario, the beneficiary becomes a bankruptcy creditor with a claim contingent upon the debtor's obligation becoming due."

However, the bank's commission cannot be calculated during periods when obligations to foreign creditors are suspended. This principle is illustrated in the Decision of the Supreme Court of Serbia, Prev. 548/2001 of February 28, 2001 – Judicial Practice of Commercial Courts, Bulletin of the Higher Commercial Court, No. 4/2001.

From the explanation: "For the period during which, due to changed circumstances, the obligation towards foreign creditors was suspended, the bank is not entitled to charge its commission based on the unrepaid portion of the foreign debt. In the revision, it is incorrect to claim that the right to commission arose from an intervention by the bank or from the complete fulfilment of its obligation towards the foreign creditor on June 4, 1987. The plaintiff-bank incorrectly charged a commission for the period from July 1, 1997, to June 30, 1998, during which the credit was dormant. According to the agreement between the parties, commission payments cannot be duplicated or repeatedly charged during a period when foreign obligations are suspended. Therefore, the plaintiff-bank cannot calculate or collect commissions against the unreduced balance of the credit when obligations abroad are dormant."

Bank Guarantee on Demand

Various types of bank guarantees can be categorised differently: unconditional and conditional bank guarantees, payment or performance guarantees, counter-guarantees and super-guarantees, covered and uncovered guarantees, bid guarantees, advance payment guarantees, performance guarantees, etc. Each type has its own specificity and importance. However, this section focuses on demand guarantees due to their rapid enforcement, which can sometimes lead to abuse or fraud.

A demand guarantee is an independent and irrevocable obligation by the guarantor bank to pay the beneficiary a specified amount upon presentation of a demand in accordance with the terms and conditions of the guarantee. The beneficiary of a demand guarantee exercises the right to payment by submitting a timely request in a designated place, accompanied by a statement detailing the principal's breach of the underlying agreement.

Abuse of rights occurs when the beneficiary makes an unfounded request for payment, effectively committing fraud by misleading the other party about the claim's legitimacy (Vujičić, J., 2012). Payment on an unjustified demand affects the principal, who must reimburse the amount paid. The principal is entitled to initiate legal proceedings to recover any unjustly paid amount. However, this is not always the most favourable solution, especially if the dispute involves a foreign party, which may lead to lengthy and expensive court proceedings. Even if the principal prevails in a cross-border dispute, the recognition and enforcement of foreign judicial or arbitral decisions will further prolong the process.

To address fraudulent demands under a bank guarantee, the 1978 Uniform Rules for Contract Guarantees adopted in Paris attempted to mitigate unfounded payment claims by requiring the beneficiary, when filing a payment request, to present either a court or arbitral decision confirming the principal's breach of the underlying contract, or a written statement by the principal agreeing to both the demand and the amount requested (Vujičić, J., 2012). In practice, however, these rules have not been widely implemented. Their application would entail substantial time and legal costs, thus undermining the main purpose of bank guarantees.

Under the 2010 Uniform Rules for Demand Guarantees issued by the International Chamber of Commerce (ICC), Paris, to obtain payment under a demand guarantee it is sufficient for the beneficiary, when making a demand under the guarantee, to submit a signed demand accompanied by any other documents required by the guarantee and by a statement expressly and unambiguously declaring that the applicant has breached an obligation under the underlying contract (Vujičić, J., 2012).

"In contrast to the 1992 Uniform Rules for Demand Guarantees requirements, the new rules do not obligate the guarantor to provide the principal with the beneficiary's demand for payment and other submitted documents" (Vujičić, J., 2012). In our view, the principal's protection and security should not be overlooked. Given that the guarantor bank has five (5) working days to fulfil the payment specified under the guarantee, we propose extending this period by, for example, three working days. During this extended timeframe, under the threat of having to make payment, the principal would be asked to respond to the beneficiary's statement and accompanying documents. If the principal fails to

respond within the proposed three working days (or a more extended period, if agreed), the bank would proceed with automatic payment. This approach would maintain the efficiency and speed of payment under the guarantee while offering the principal legal protection.

Naturally, the guarantor bank remains obligated to verify the documents submitted by the beneficiary and, should it detect fraudulent intent, to refuse to honour the guarantee.

Digitalisation and Electronic Bank Guarantee

Today's world is witnessing the rapid expansion of the digital economy. It is therefore reasonable to ask to what extent the bank guarantee can meet the challenges posed by innovative technology. This question particularly concerns the bank guarantee's legal nature and the previously identified characteristics, such as its independence (autonomy), strict written-form requirement, irrevocability, etc. These features are at odds with digital communication, since new technologies presuppose electronic communication.

Despite the distinctive legal nature of traditional bank guarantees, there is an increasing turn toward their digitalisation. Introducing electronic bank guarantees into international commerce enables faster transactions between parties, greater transparency, and even automation. At the global level, such instruments are only partly regulated by the Uniform Rules for Demand Guarantees (URDG 758, ICC, 2010), as well as the UNCITRAL Model Law on Electronic Commerce (1996) and the UNCITRAL Model Law on Electronic Signatures (2001), adopted by the United Nations Commission on International Trade Law.

ICC Uniform Rules for Demand Guarantees (URDG 758) apply to any demand guarantee or counter-guarantee that expressly indicates it is subject to them. They bind all parties to the demand guarantee or counter-guarantee, except if the demand guarantee or counter-guarantee modifies or excludes them. (URDG 758)

UN Convention on Independent Guarantees and Stand-by Letters of Credit (1995) made by UNCITRAL. Adopted by the General Assembly on 11 December 1995, the Convention is designed to facilitate independent guarantees and standby letters of credit, where only one or the other instruments may be traditionally in use. The Convention also solidifies recognition of common basic

principles and characteristics shared by the independent guarantee and the standby letter of credit. The Convention entered into force on 1 January 2000.¹

Most countries worldwide have adapted and are still in the process of adapting their legislative frameworks to international requirements concerning electronic commerce, with a view to more successful trade and the economic development of their respective countries. In the context of electronic commerce, the law of the Republic of Serbia has enacted the Law on Electronic Commerce (2009, as amended in 2019) and the Law on Electronic Signature (2004). By these statutes, the Republic of Serbia seeks to keep pace with international standards in the digital economy.

Electronic commerce is still being shaped and aligned with international business practice, while confronting the challenges inherent in this business mode. More developed countries are adopting innovative technologies more quickly and intensively to secure successful operations.

With the adoption of the 2010 revision of the Uniform Rules for Demand Guarantees by the International Chamber of Commerce (ICC), Paris, an effort was made to modernise the rules on demand guarantees by enabling electronic dealings, curbing abuses, and, at the same time, preserving efficiency and speed. Nevertheless, in the context of bank guarantees, electronic documentation is permitted only if expressly provided for in the guarantee.

Given that the bank guarantee is a highly complex institution, its digital form is even more complex; it remains in development. It is, to some extent, of limited application, not least because not all countries are keeping pace with the evolution of the digital economy. The significance and advantages of electronic bank guarantees must not be overlooked, but neither should their drawbacks.

Among the advantages of electronic bank guarantees are their digital form (electronic signature, electronic seal, timestamp, etc.), which enables faster execution on digital platforms (e.g., SWIFT SRG) and lowers administrative costs; the environmental aspect is also not negligible. Some scholars further emphasise their security, achieved through qualified signatures and time stamps that guarantee the authenticity and integrity of the document.

¹ More: <https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/guarantees.pdf>

Among the drawbacks, it is noted that some countries still require a written form and a wet ink signature for guarantees, as there is no single international instrument that explicitly regulates electronic bank guarantees. There is also the risk of technical failures, issues with data archiving, and similar concerns.

Accordingly, for electronic bank guarantees to gain wider application, full recognition and harmonisation at both international and national levels are needed, as well as technological standardisation and support from leading IT experts. In addition, judges and arbitrators should be educated on the evidentiary validity of electronic documents in the event of disputes.

Validity Period of the Bank Guarantee

A deadline (or validity period) can be significant in any legal transaction. In some cases, it constitutes a key factor, while in others it may not be as critical. Regardless, if the contracting parties do not specify one, the law typically governs it.

The beneficiary of a bank guarantee secures the right to claim the guaranteed amount only if the payment request is submitted within the valid timeframe. When exercising this right, the beneficiary must act according to good faith and fair dealing principles.

Typically, for a bank guarantee, the parties agree on a time limit based on one of two approaches: either fix an exact date as the deadline for the guarantor's performance or set a certain number of days starting from the obligation's maturity. "The validity period of a bank guarantee is when the guarantee's beneficiary may request the guaranteed payment from the bank. If the beneficiary fails to do so within this period, the bank is released from any obligation to pay (Šogorov, S., 1985)." An example illustrating the significance of deadlines is the Decision of the Higher Commercial Court, Pž. 5704/2000, dated January 18, 2001 (Judicial Practice of Commercial Courts – Bulletin No. 2/2001):

A beneficiary's request for payment of the guaranteed amount must be submitted to the guarantor bank before the guarantee's validity expires. Otherwise, the bank's obligation ceases.

From the ruling: "The first-instance judgment rejected the plaintiff's claim, explaining that the plaintiff concluded a wheat loan agreement with DD'A . H' from S on March 10, 1995, and an annexe on March 23, 1996. In connection with this agreement, the defendant issued

bank guarantee No. 1310/96 on April 2, 1996, with a validity period expiring September 30, 1996. The plaintiff also concluded a sugar loan agreement with 'AP' from S on August 16, 1994, and an annex on April 6, 1995, under which the defendant issued the plaintiff bank guarantee No. 5/95 on April 28, 1995, valid until June 30, 1995. Since the obligations under the first agreement were unpaid in the amount of 467,435 dinars and under the second for 196,793.48 dinars—and the plaintiff did not request payment from the guarantor within the guarantees' validity periods—the court rejected the plaintiff's claim.

Relies on common law (e.g., *Edward Owen Engineering LTD. v. Barclays Bank International LTD.* and another [1977 E. No. 1065]: The plaintiffs, English suppliers, contracted with Libyan customers to erect greenhouses in Libya and agreed that a performance guarantee for 10 per cent, of the contract price should be issued by the defendant English bank and lodged with a Libyan bank. The contract, which was governed by Libyan law, provided that an irrevocable, confirmed, or confirmable letter of credit payable at an English bank was to be opened in favour of the plaintiffs. After the plaintiffs had given a counter-guarantee to the English bank, the latter, on their own responsibility and on the plaintiffs' behalf, gave a performance bond for £50,203 to the Libyan bank and confirmed that their guarantee was payable "on demand without proof or conditions." The Libyan bank then issued a guarantee bond for the plaintiffs for the same sum in favour of the Libyan customers. No letter of credit, which complied with the terms of the contract, was opened by the customers and the plaintiffs after they had been told that the guarantee given had no effect and that they accepted their conduct as a repudiation of the contract. At the customer's request, the Libyan bank then claimed £50,203 under the guarantee from the English bank. The plaintiffs obtained an interim injunction on their ex parte application to restrain the English bank from paying the Libyan bank. Kerr J. discharged the injunction.

On appeal by the plaintiffs: Held, that a performance bond stood on a similar footing to a letter of credit and a bank giving such a guarantee must honour it according to its terms unless it had notice of clear fraud; and, accordingly, since it was impossible to say that fraud on the part of either the Libyan customers or bank had been established, the appeal must be dismissed (post, pp. 171A-C, 172A, F-H, 174A-B, 175E-H)

According to Article 1083 of the LOO, the bank's obligation becomes due when the creditor calls for

payment and if the conditions specified in the guarantee are met. If the guarantee includes a time-limit condition, the payment request must be submitted to the bank before that period ends. Thus, irrespective of how the request is submitted, it must reach the bank before the guarantee's expiration date. Once that date passes, the guarantor is released from its obligations. The guarantor bank must receive the request for payment before the expiry date because its obligation ceases on the date indicated as the guarantee's termination, pursuant to Article 77 of the LOO."

In 1978, the International Chamber of Commerce (ICC) in Paris adopted the Uniform Rules for Contract Guarantees, which provide that the parties are free to stipulate the time limit for submitting a demand under the guarantee, failing such agreement, the applicable time limits, depending on the type of guarantee in question, shall be those laid down in the Uniform Rules for Contract Guarantees.

Likewise, when a bank guarantee includes the clauses "without objection" or "on first demand," the bank may refuse to honor the guarantee if the beneficiary's request is unjustified or violates the principle of good faith and fair dealing.

The contracting parties are free to extend the validity of the bank guarantee if its term is tied to extending the deadline for fulfilling the obligation under the underlying contract. Article 1086 of the LOO provides that the beneficiary can assign its rights under the bank guarantee to a third party only by transferring both the secured claim and the associated obligations tied to that claim. An interesting fact is that in Belgium, the content of a bank guarantee used in international trade is prescribed by the Ministry of Finance; it cannot be altered by agreement of the parties (Šogorov, S., 1985). Hence, the contracting parties lack the freedom to adapt the content of the bank guarantee, which must be issued according to strict, predetermined rules.

A bank guarantee is considered a formal legal instrument. Once the guarantor bank fulfils its payment obligation to the beneficiary, the beneficiary must return the bank guarantee document. The decision of the Higher Commercial Court, Pž confirms this. 4556/2006(1), dated June 27, 2007:

From the explanation: "...A bank guarantee is a strictly formal legal instrument; thus, the bank's obligation, which becomes due when the guarantee beneficiary requests payment—assuming all conditions in the

guarantee are met—expires on the date indicated as the guarantee's validity period. When the guarantee specifies certain validity conditions, the demand for payment must be submitted before the guarantee expires to fulfil these conditions. At the end of the guarantee period, the guarantor is released from its obligations. The guarantor bank must receive the demand for payment before the expiration date, since its obligation ceases on the last valid date of the guarantee. Therefore, the first-instance court correctly rejected the plaintiff's claim regarding the amount of USD 1,310,199.98 under guarantees that had already expired."

Conclusion

The bank guarantee, whether in traditional or electronic form, is a highly complex legal instrument requiring robust national and international legislative support. Its extensive use in commercial transactions is evident, as it simplifies operations at both levels—particularly in international trade. Business entities are more inclined to enter into contracts with foreign partners when the obligations under the main contract are "secured" through a bank guarantee. This mechanism has gained prominence as a vital means of protecting creditors, especially in the context of sales contracts, which are indisputably the most prevalent type of agreement in international markets.

Besides allowing for swift and effective enforcement, a bank guarantee is valuable because it covers many types of risk, including insolvency, force majeure, administrative bans, and other restrictions. A defining characteristic of the bank guarantee is its independence, a feature critical not just for the evolution of the instrument itself but also for the harmonized legislative framework surrounding it at the international level.

Taking into account the significant growth in industry, particularly digital commerce, and the cross-border sale of goods, it becomes essential to incorporate widely accepted international rules into domestic regulations and adapt those rules to the global context. The advantage of legal transactions undertaken for the exchange of goods and payments lies in the freedom to determine contract terms, select security instruments, and regulate contract termination and judicial remedies—always under the constraints of public policy, mandatory provisions, established business practices, and moral standards.

The main obstacle to a fully regulated bank guarantee system—both in domestic and international law—is the

lack of uniformity in defining its legal nature and the potential abuses of the beneficiary's rights, and, in the context of the electronic bank guarantee, in the absence of a single international instrument that explicitly regulates it. By providing a unified definition of the bank

guarantee's legal characteristics, one can analogously apply the rules governing other similar instruments. In this regard, the most practical approach would be to tailor the existing legal regulations more precisely to each type of bank guarantee.

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Bančna garancija kot sredstvo za zavarovanje izpolnitve pogodbe po pravu Republike Srbije

Izvleček

V gospodarskem pravu, tako na nacionalni kot mednarodni ravni, so bančne garancije najpogostejše uporabljen instrument za zavarovanje izpolnitve pogodbe. Običajno se uporabljajo v prodajnih pogodbah in pri izvajanju tujih investicijskih projektov. Izvršitev bančne garancije je hitra in učinkovita, saj spada v okvir nevtralnih bančnih operacij. S pomembnim povečanjem števila gospodarskih subjektov se je ustrezno povečalo tudi število gospodarskih pogodb, ki zahtevajo zavarovano izpolnitev. Kljub prednostim hitrih transakcij na obeh ravneh se gospodarski subjekti soočajo z gospodarskimi in pravnimi tveganji, ki jih spodbujajo k zavarovanju pogodb na najučinkovitejši način, da bi zaščitili svoje interese in dosegli svoje poslovne cilje. V tem kontekstu je banka bistven partner pri spodbujanju uspešnega sodelovanja med podjetji. Glede na pomembnost in kompleksnost bančnih garancij v današnjih pravnih transakcijah ta članek proučuje aktualna vprašanja in izzive, povezane s ključnimi vidiki bančnih garancij kot sredstva za zavarovanje izpolnitve pogodb, vključno z njihovo učinkovitostjo in hitrostjo izvrševanja ter njihovimi prednostmi in slabostmi, s posebnim poudarkom na sodnih odločbah in elektronskih bančnih garancijah v luči inovativnih tehnologij. Pregleduje tudi obstoječe zakonske določbe in ponuja primerjalno analizo na različnih ravneh. Glavni cilj članka je odpraviti negotovosti v zvezi z institucijo bančne garancije, da se spodbudi varnejše poslovne prakse.

Ključne besede: bančna garancija, sredstva za zagotavljanje, nevtralne bančne operacije, sodne odločbe, digitalizacija, elektronska bančna garancija