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PRACTICAL INFORMATION

HERMES COVER SPECIAL

Inclusion of foreign content in Hermes Cover

EXPORT CREDIT GUARANTEES OF THE
FEDERAL REPUBLIC OF GERMANY

Hermes Cover

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Inclusion of foreign content in Hermes Cover

A. BASIC PRINCIPLES FOR THE INCLUSION OF FOREIGN CONTENT IN HERMES COVER

Basically, the rules governing the inclusion of foreign content and local costs, which are described in this brochure, can be traced back to decisions taken by the Federal Government in October 2016. The regulations concerning local costs are based on an adjustment of the OECD Consensus, which was implemented in Germany in May 2021.

This document describes the conditions for including foreign content in Hermes Cover.

I. PREREQUISITES FOR INCLUDING FOREIGN CONTENT IN HERMES COVER

The question as to whether foreign goods and deliveries may be included arises only if they are of a foreign origin in accordance with the Federal Government's definition. The rules for an inclusion described below in section A apply only if the export contract with the foreign buyer is concluded directly by the German exporter (standard model). If the contractual set-up differs from this model (e.g. the contract is signed by a foreign subsidiary/affiliated company of the exporter) more restrictive regulations apply, which are explained separately in section C.

What is the definition of foreign content?

Goods produced in another country which are processed or modified within the Federal Republic of Germany and integrated in a product for which a German certificate of origin has been, or could be, issued are not classified as foreign content. This is because in accordance with the Federal Government's definition, a product for which a German certificate of origin has been issued is deemed to constitute German goods in whole regardless of whether, and to what extent, it contains foreign goods and services.

What contractual payment claims must be agreed upon?

The basic prerequisite for including foreign content in an export credit guarantee is the existence of a direct claim for payment held by the subcontractor towards the German exporter (principal supplier).

II. PERMISSIBLE FOREIGN CONTENT IN CONNECTION WITH SINGLE TRANSACTION COVER ("49 PLUS RULE")

Pursuant to the rules currently applicable, foreign content and local costs are subject to a uniform "base amount" of 49%,[1] which may be exceeded in certain circumstances.

What must generally be considered in connection with local costs?

Goods and deliveries originating from the buyer's country are generally referred to as "local costs".

As a rule, local costs qualify for cover provided that they are directly related to the German exporter's export transaction and form part of its claim for payment against the buyer.

In accordance with the OECD Consensus, which is binding on Germany, credit terms are permissible for such local costs amounting to up to 28.6% of the (total) order value in OECD high-income countries[2] and up to 33.3% in all other countries.

In connection with shorter credit periods (up to two years) this restriction imposed by the OECD Consensus does not apply.

If the local costs required for executing the order exceed this percentage, they can only be covered if separate payment in cash is agreed upon.

[1] In practice a two-level approach is applied. These rules relating to the inclusion of foreign content and local costs only apply if the buyer's country in question is not subject to any restrictions under the specific cover policy.

[2] According to the current classification of the World Bank

OVERVIEW: POSSIBILITIES FOR THE INCLUSION OF FOREIGN CONTENT IN HERMES COVER

<table>
<tr><th>Wholeturnover Policy,
Wholeturnover Policy Light</th><th colspan="2">Single transaction cover
49 PLUS rule for short-term and medium-/long-term business</th></tr>
<tr><td>► Cover of up to 100% foreign content (if necessary after prior review of the business model)</td><td>Level 1
► Foreign content – basic percentage up to 49% without giving reasons</td><td>Level 2
► Foreign content – more than 49% case-by-case decision on the basis of sufficient justification*</td></tr>
<tr><td></td><td></td><td>► Preliminary inquiry possible</td></tr>
</table>

* In connection with medium-/long-term business, local costs must not exceed 28.6% of total order value in OECD high-income countries and 33.3% in all other countries.

Additional restrictions concerning the eligibility of local costs for inclusion in cover may arise from the specific cover policy for the specific buyer's country in question.

In what amount can foreign content be included in the first level?

In the **first level**, goods and services can be included in the cover regardless of their origin (with due regard for the above explanations on local costs) up to an amount of 49% of the (total) order value without any obligation to provide further reasons.

In what amount can foreign content be included in the second level?

In the **second level**, it is possible, on a case-by-case basis, to cover transactions which exhibit foreign content in excess of 49%. In this case, the exporter must explain in detail why such supplies are crucial. This requires an individual decision by the Interministerial Committee on whether a transaction qualifies for cover in the light of the reasons submitted. Here the main focus regularly is on how high the positive effect is that the German share will have, in particular, on employment in Germany.

III. PRELIMINARY INQUIRY ON THE ELIGIBILITY OF FOREIGN CONTENT FOR COVER

In cases where an exporter needs an early indication from the Federal Government as to whether and to what extent foreign content of more than 49% can be included in cover, it can submit a preliminary inquiry. Details of the procedure and possible contents of a project plan can be found in section B of this brochure.

IV. FURTHER COVER OPTIONS

If the foreign content does not come within the scope of the national rules, it may still be possible for the German exporter to obtain cover.

In this case, cover may be provided in favour of the German exporter if and when the national credit agency in the country from which the subcontracted supplies originate assumes a reinsurance commitment. If a foreign government-sponsored export credit agency agrees to assume a reinsurance commitment, the Federal Government will only cover the credit risk for the German part, while the foreign export credit agency covers the corresponding foreign content.

Generally speaking, the collaboration between the Federal Government and the foreign export credit agency is invisible to the German exporter, which receives the cover from a single source. This is because the allocation of risk is solely a matter for the export credit agencies concerned.

The reinsurance commitment is provided on the basis of corresponding reinsurance agreements.[3]

If the Federal Government is unable to provide cover for foreign content and reinsurance is also not an option, the German exporter can still obtain cover by placing the payment terms agreed upon with its subcontractors on an "if-and-when" basis. In this case, cover can take the form of co-insurance.

Detailed information on these additional forms of cover can be found in the brochure "Hermes Cover Special **Multi-sourcing projects**".

V. PERMISSIBLE FOREIGN CONTENT IN CONNECTION WITH SHORT-TERM BUSINESS (WHOLETURNOVER POLICIES, SINGLE TRANSACTION COVER)

In connection with transactions on short credit terms, foreign content can generally be included in the cover up to 100% of the order value provided that cover is granted under a Wholeturnover Policy or a Wholeturnover Policy Light.[4] Here, in particular, goods in transit are generally regarded as foreign content eligible for cover. These are products which are normally traded in transit at short credit terms (primarily raw materials, agricultural produce, fertilisers, commodities and consumer goods). As a rule, the permissible maximum credit periods for the respective type of goods must be taken into account (normally 180 days, 360 days for specific types of goods). A precondition for the complete cover of foreign content is that the exporter's business model qualifies for support, something that will be verified in cases of doubt.

The 49 PLUS rule also applies to short-term single transaction cover, this means that – as with transactions on credit terms – up to 49% of foreign content is generally permissible without the need to give reasons. If the foreign content is higher, reasons for its necessity have to be given – also by using the possibility to make a preliminary inquiry – in the course of an individual assessment of the case.

B. PRELIMINARY INQUIRY REGARDING THE ELIGIBILITY OF FOREIGN CONTENT › 49% FOR COVER UNDER SINGLE TRANSACTION GUARANTEES

The Federal Government offers exporters the possibility to find out whether a transaction is eligible for cover under an export credit guarantee even if the share of foreign supplies exceeds 49% by making a **non-binding preliminary inquiry**. For this purpose, the exporter can – prior to the actual application for cover – submit an informal project outline which should basically contain a project description, details of the planned supply structure and reasons for the high proportion of foreign content, as well as an explanation of the project's importance for the exporter and for its operations in Germany. After examining the inquiry the Federal Government will send the exporter a non-committal letter giving an indication as to whether, and up to what amount, foreign content is permissible in connection with the transaction in question. The preliminary inquiry is optional and not a mandatory step in the application procedure. The assessment of the inquiry by the Federal Government is free of charge.

[3] A list of existing agreements can be found on our website: www.exportkreditgarantien.de/en › Exports › Practice › Cooperation Agreements

[4] Different rules apply to revolving cover.

I. STEPS OF THE INQUIRY PROCEDURE

The inclusion of foreign content (including local costs) exceeding the 49% threshold is possible only by way of exception and in justified individual cases. For this reason, exporters planning a transaction with elevated foreign content would often like to get an indication, prior to submitting an application for cover, as to whether a particular transaction is, in principle, eligible for cover even with elevated foreign content if necessary, in order to increase their planning security. Against this backdrop, the Federal Government offers the option to submit a “Preliminary Inquiry regarding the Eligibility of Foreign Content for Cover”.

For this, the following procedure should be followed:

1. Submission of the preliminary inquiry

The exporter sends an informal, written project outline that contains all the details described in section B II of this brochure by mail to “Exportkreditgarantien der Bundesrepublik Deutschland, Postfach 500399, 22703 Hamburg”, by fax to +49 (0)40/88 34-9175 or via email to “antrag@exportkreditgarantien.de”.

2. Assessment of the preliminary inquiry

On the basis of the project outline and the details of the project presented, Euler Hermes will check whether the reasons given to explain why, from the exporter’s point of view, foreign content amounting to more than 49% is necessary are convincing. No fees are charged for the assessment of the preliminary inquiry.

3. Project presentation (optional)

If necessary, the exporter will be given the opportunity to explain the specific circumstances of its project to the responsible Federal Ministries in the form of a short presentation.

4. Decision and information of the exporter

The Federal Government will take a decision on the maximum amount of foreign content which will be eligible for cover after examining the preliminary inquiry on the basis of the facts given in writing and, possibly, an additional project presentation by the exporter. The exporter will be informed of the results of the pre-assessment through a written indication. Such an indication is not binding and not limited in time. The final decision on granting cover for a transaction will continue to rest with the Interministerial Committee after the submission of a formal application for cover.

5. Application for cover

As soon as a project has taken shape, the exporter can submit a formal application for cover. Only at this stage will all project details (creditworthiness, environmental aspects, etc.) be verified. Whether previously a preliminary inquiry had been made or not is not relevant in this context. The only purpose of such a preliminary inquiry is to give the exporter an indication regarding the amount of foreign content eligible for inclusion in the cover in order to allow it to plan ahead on a more reliable basis.

II. ELEMENTS OF THE PRELIMINARY INQUIRY

The project outline should contain, in concise form (about 2–5 pages), information on the following details, in particular, as far as they are already known at the time of the submission of the preliminary inquiry:

- **Project description**
  Foreign buyer; guarantor (if involved); forms of cover required (e.g. supplier credit cover); type of goods/project; destination of the goods/project site; order value; terms of payment; security instruments; planned date of delivery/service performance.

- **Planned supply structure**
  Maximum percentage of foreign supplies/local costs inquired about; details of the supply structure: among other things, local costs, supplies and services originating in third countries and, if applicable, goods supplied by affiliated companies of the exporter.

- **Reasons**
  Necessity of the foreign supplies and services to be included; the project's importance for the exporter and its operations in Germany (inter alia for the employment situation).

Other relevant aspects may be added if need be. There are no formal requirements which have to be met.

III. PRACTICAL EXAMPLES

In the past, the Federal Government was prepared to accept foreign content amounting to more than 49% or to give a positive indication after examining the individual case if the exporter could offer conclusive reasons justifying the inclusion in cover. It turned out that it was not one single aspect that was the decisive factor. Normally, there was in fact a combination of various reasons and their holistic evaluation that led to a positive decision on a transaction's eligibility for support. Therefore, it is not possible to comply with the request frequently made by exporting companies that individual, objective criteria should be stated, which would enable the exporter to determine permissible foreign shares in excess of the threshold of > 49% autonomously and with sufficient reliability.

The justification will always focus on how a major beneficial effect can be achieved, in particular with regard to employment, with the share remaining in Germany. For instance, it was argued that

- the key technology would continue to originate in Germany,
- the overall project would be managed from Germany,
- for technological reasons, certain components needed for the project in question were only available abroad,
- the foreign buyer had specifically named certain suppliers abroad and/or
- the exporter would be unable to meet delivery deadlines for lack of sufficient production capacity in Germany.

The criteria and aspects stated above can and should only enhance transparency and improve the exporters' understanding of what is important when the eligibility for cover of a transaction with a particularly high portion of foreign content is determined.

CRITERIA FOR DETERMINING WHETHER FOREIGN CONTENT IS ELIGIBLE FOR INCLUSION IN COVER

Are the goods manufactured by the German exporter eligible for a German certificate of origin?

Yes → According to the definition of the Federal Government, such goods are deemed to be of German origin in whole, meaning that no additional restrictions apply to the foreign content of the German product.

No ↓

Is the exporter only obliged to pay its foreign subcontractors on an "if-and-when" basis?

Yes → Co-insurance

No ↓

Are several transactions on short credit terms to be covered under a Wholeturnover Policy or Wholeturnover Policy Light?*

Yes → Inclusion of foreign content up to 100%, if necessary, after prior review of the exporter's business model with regard to its eligibility for cover

No ↓

Is only one transaction to be covered under single transaction cover and does the foreign content in question originate from the buyer country?

Yes → In accordance with the OECD Consensus, local costs amounting to up to 28.6% of the (total) order value in OECD high-income countries** and up to 33.3% in all other countries (40% or 50%, respectively, of the value of the export order) can be included in the cover, if credit terms (credit period of two years or longer) are agreed.

Yes/No ↓

Is only one transaction to be covered under single transaction cover and does the foreign content only account for up to 49%?

Yes → Inclusion is possible without giving further reasons. The rules governing local cost explained above have to be observed.

No ↓

Inclusion may be possible following a case-by-case decision on the basis of sufficient justification. The rules governing local cost explained above have to be observed.

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* Different rules apply to revolving cover.
** According to the current classification of the World Bank

C. REQUIREMENTS IN CASES WHERE THE CONTRACT IS CONCLUDED BY AN AFFILIATED COMPANY/SALES PARTNER ABROAD

The rules explained above apply to the normal form of an export transaction where the contract is concluded by the German exporter (standard model).

In certain cases, e.g. due to tendering conditions, it may be necessary that the contract is concluded by a subsidiary of the exporter domiciled in the buyer's country. Such contractual arrangements, too, can be supported by the Federal Government in individual cases, e.g. under the assignment model or by means of extended supplier credit cover.

Detailed information on these extended cover facilities and the preconditions for cover applicable to them can be found in the brochure ***"Praktische Informationen – Grundzüge der erweiterten Lieferantenkreditdeckung"*** (in German).

www.exportkreditgarantien.de/en

Export Credit Guarantees and Untied Loan Guarantees: instruments to promote foreign trade and investment provided by the

Federal Ministry for Economic Affairs and Energy

Commissioned to implement the federal funding instruments Export Credit Guarantees and Untied Loan Guarantees:

EULER HERMES

Cover from the Federal Republic of Germany for foreign business

Export Credit Guarantees and Untied Loan Guarantees as well as effective foreign trade promotion instruments of the Federal Government have been established for decades. Export Credit Guarantees (so-called Hermes Cover) protect German exporters and banks financing exports against political and commercial risks. Untied Loan Guarantees are to support raw material projects abroad regarded as eligible for promotion by the Federal Government. Both promotion instruments play an important role in fostering economic growth as well as in protecting and creating jobs. The Federal Government commissioned Euler Hermes Aktiengesellschaft to manage the federal funding instruments Export Credit Guarantees and Untied Loan Guarantees.

Information on other foreign trade promotion instruments of the Federal Government can be found at **www.bundeswirtschaftsministerium.de/en** under the heading Promotion of Foreign Trade and Investment.

Euler Hermes Aktiengesellschaft

Postal address:
P.O. Box 500399
22703 Hamburg, Germany

Office address:
Gasstrasse 29
22761 Hamburg, Germany

Phone: +49 40 8834-9000
Fax: +49 40 8834-9175

info@exportkreditgarantien.de
info@ufk-garantien.de
www.exportkreditgarantien.de/en

Branch offices: Berlin, Dortmund, Frankfurt, Stuttgart, Hamburg, Munich, Nuremberg, Rhineland

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