
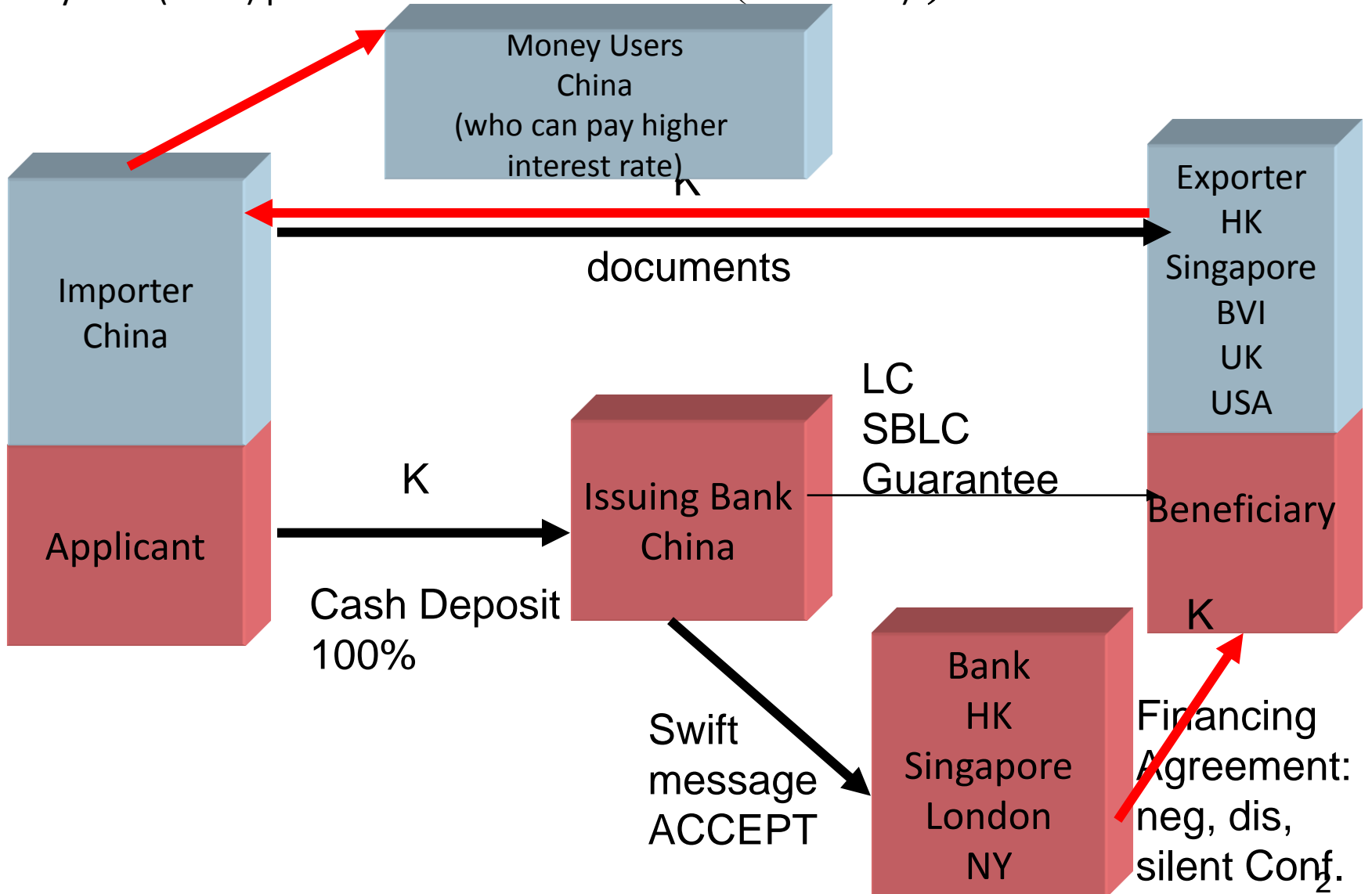


- 
- IIBLP
  - HK/Singapore/Nanjing
  - July 11-20, 2014

## ■ **New LC Fraud Court Cases in PR China: Trade Financing or Financialized Trade?**

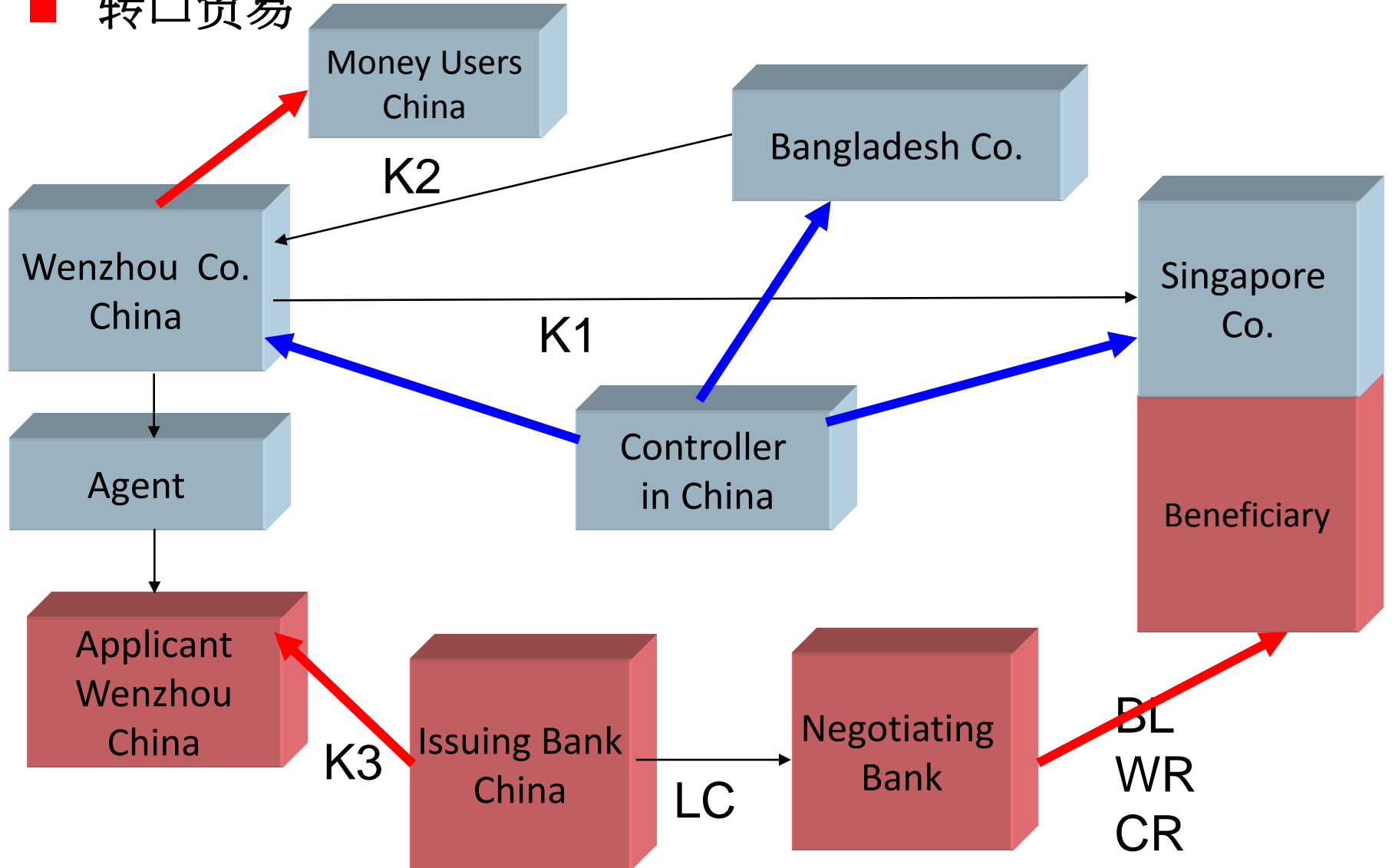
- **Dr. Jin Saibo**
  - Attorney at Law/Partner
  - Beijing Commerce & Finance Law Offices

- **NDF ( Non-deliverable Forward )** 无本金交割远期外汇交易
- 内保外贷 ( Overseas bank ( or branch ) offering FCY credits ( or loan ) which secured by SBLC ( or LC ) provided from domestic bank ( or branch ) )

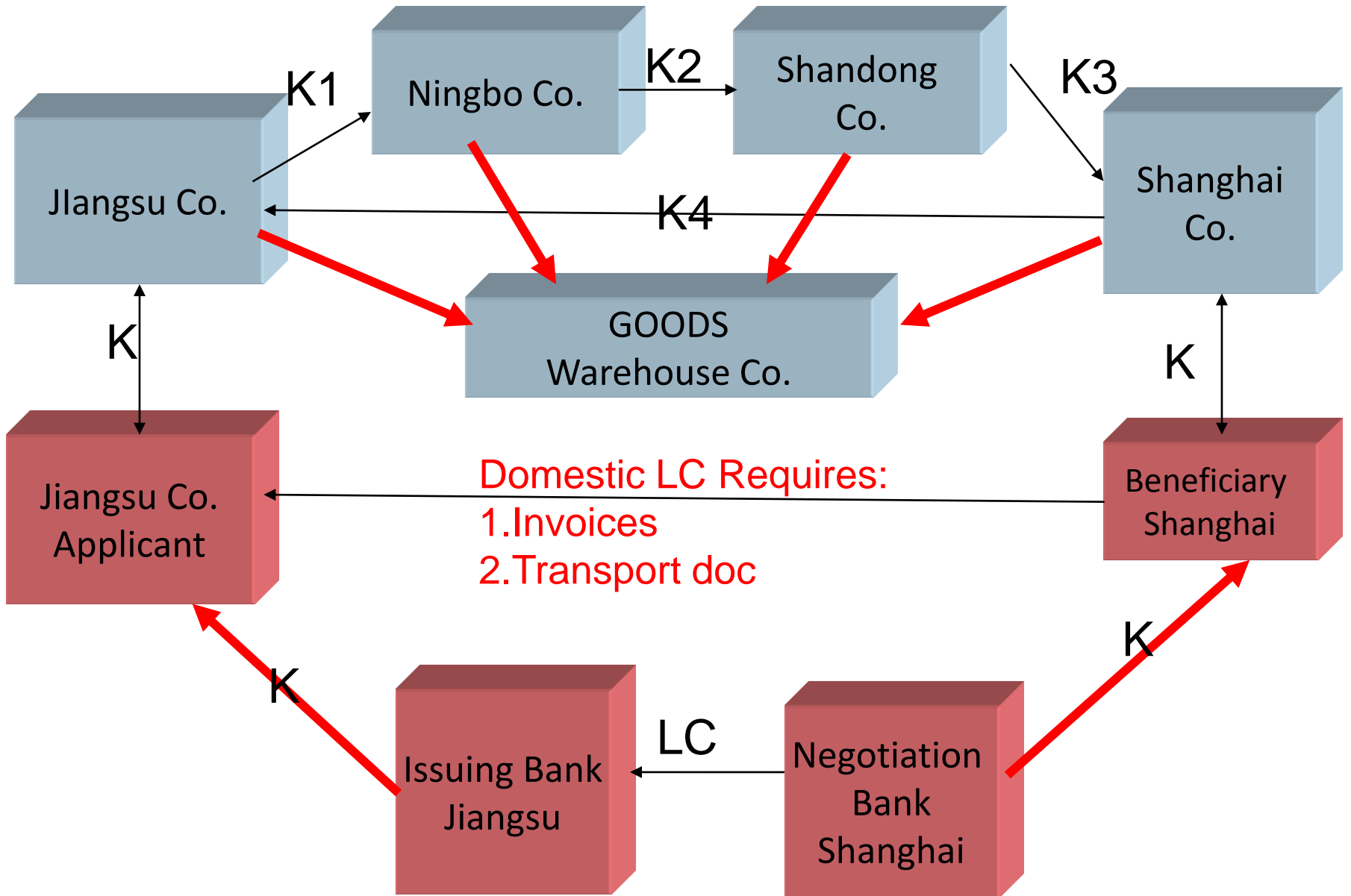


■ Re-export business

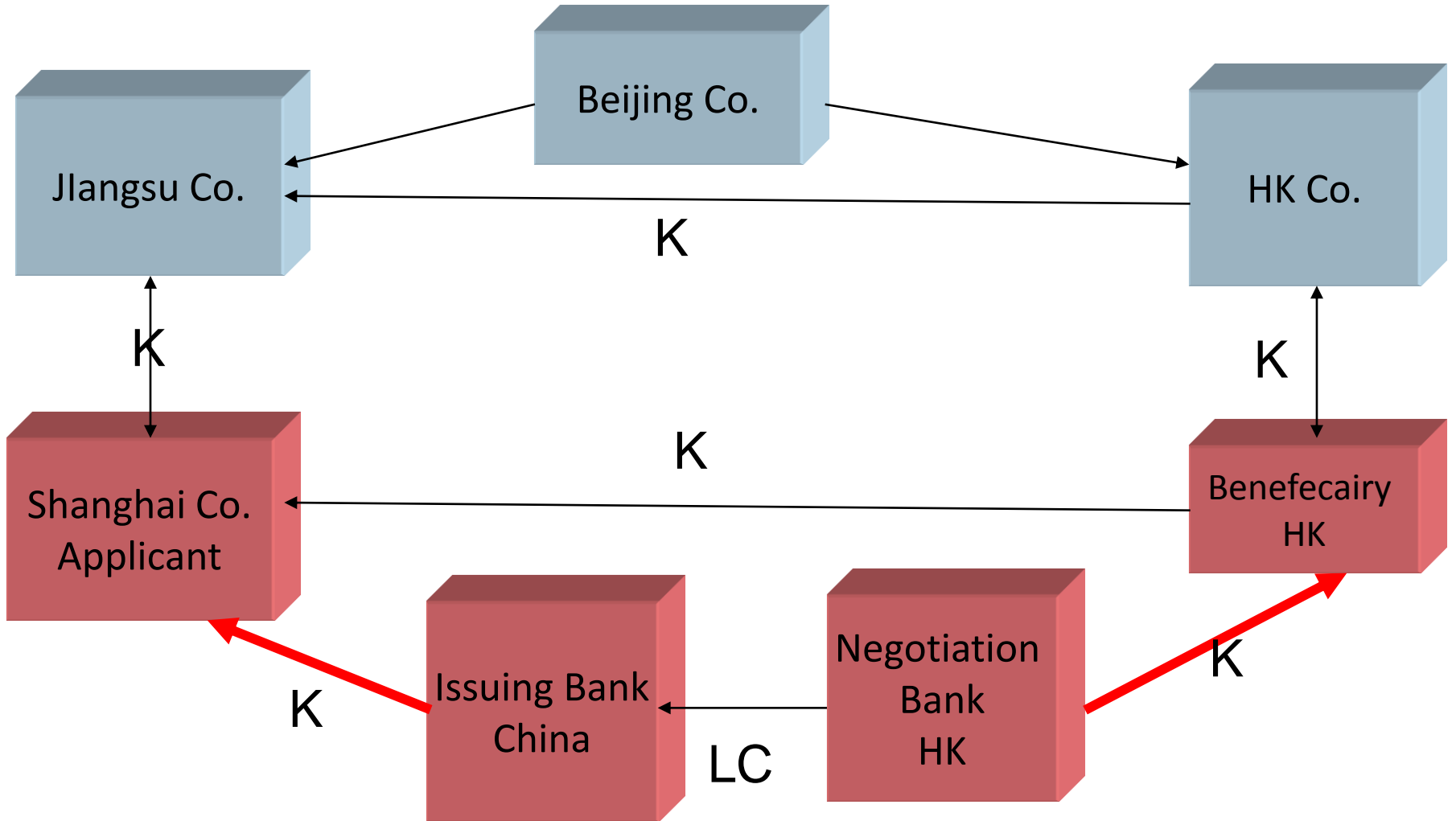
■ 转口贸易



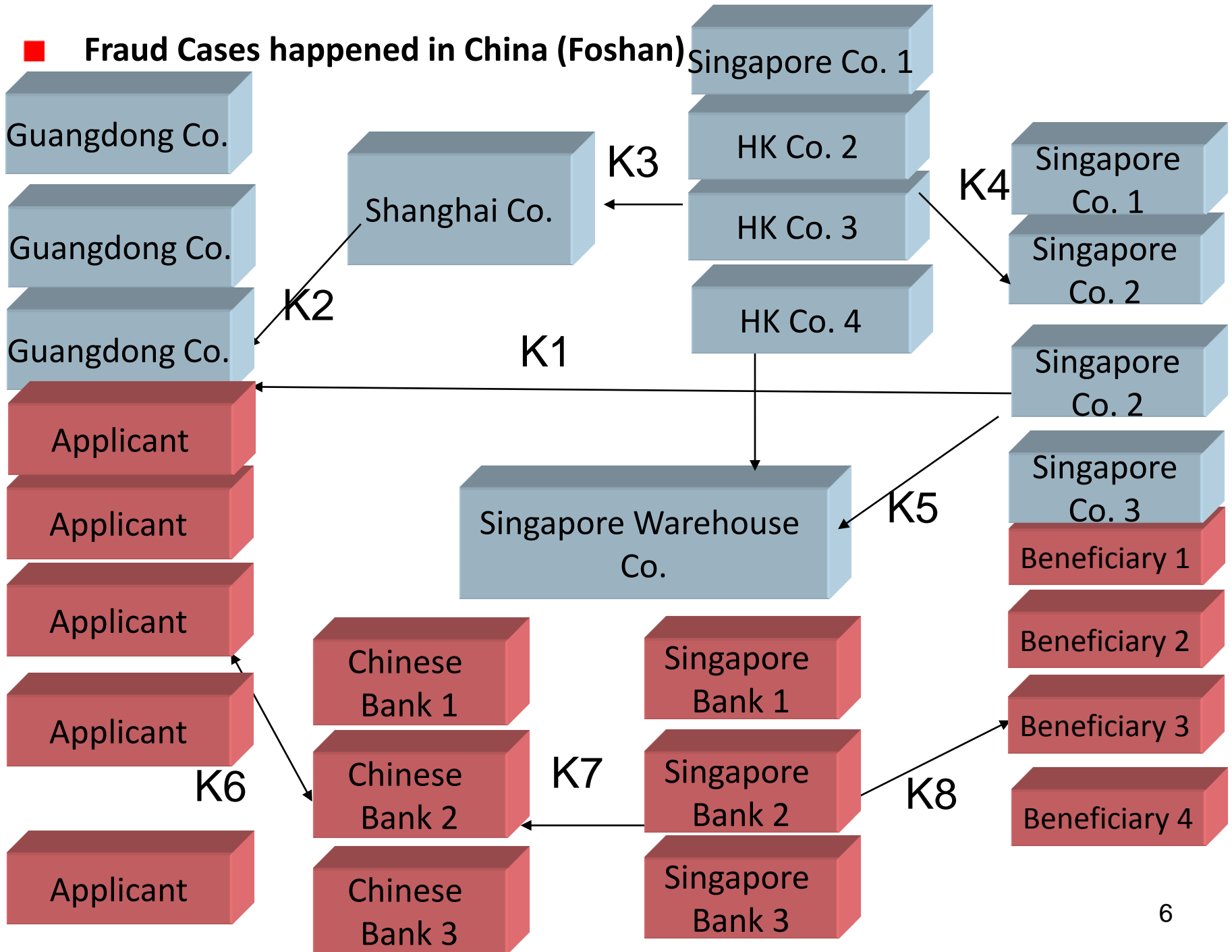
■ Domestic LC Transactions happen in China



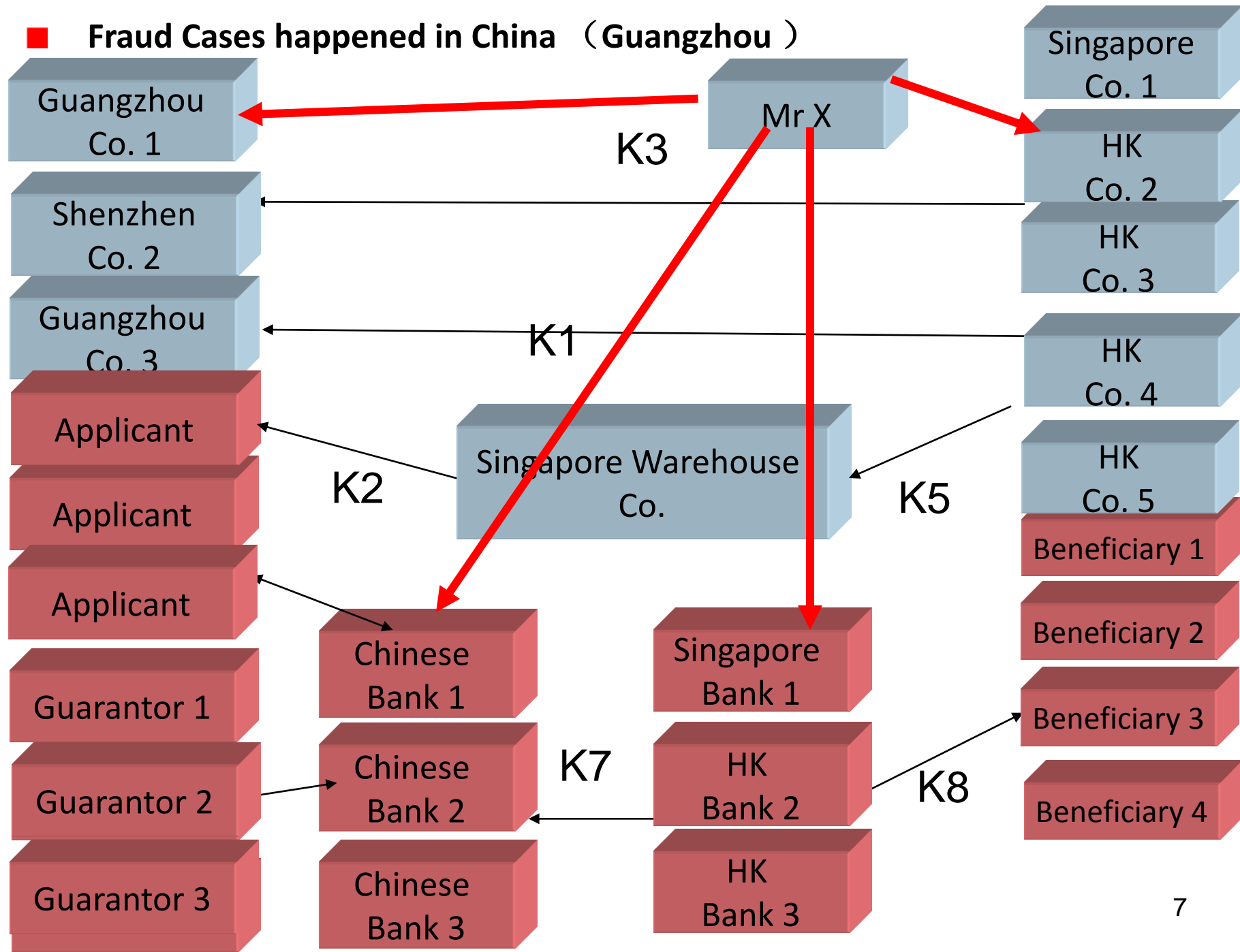
■ An Arrangement of business in China



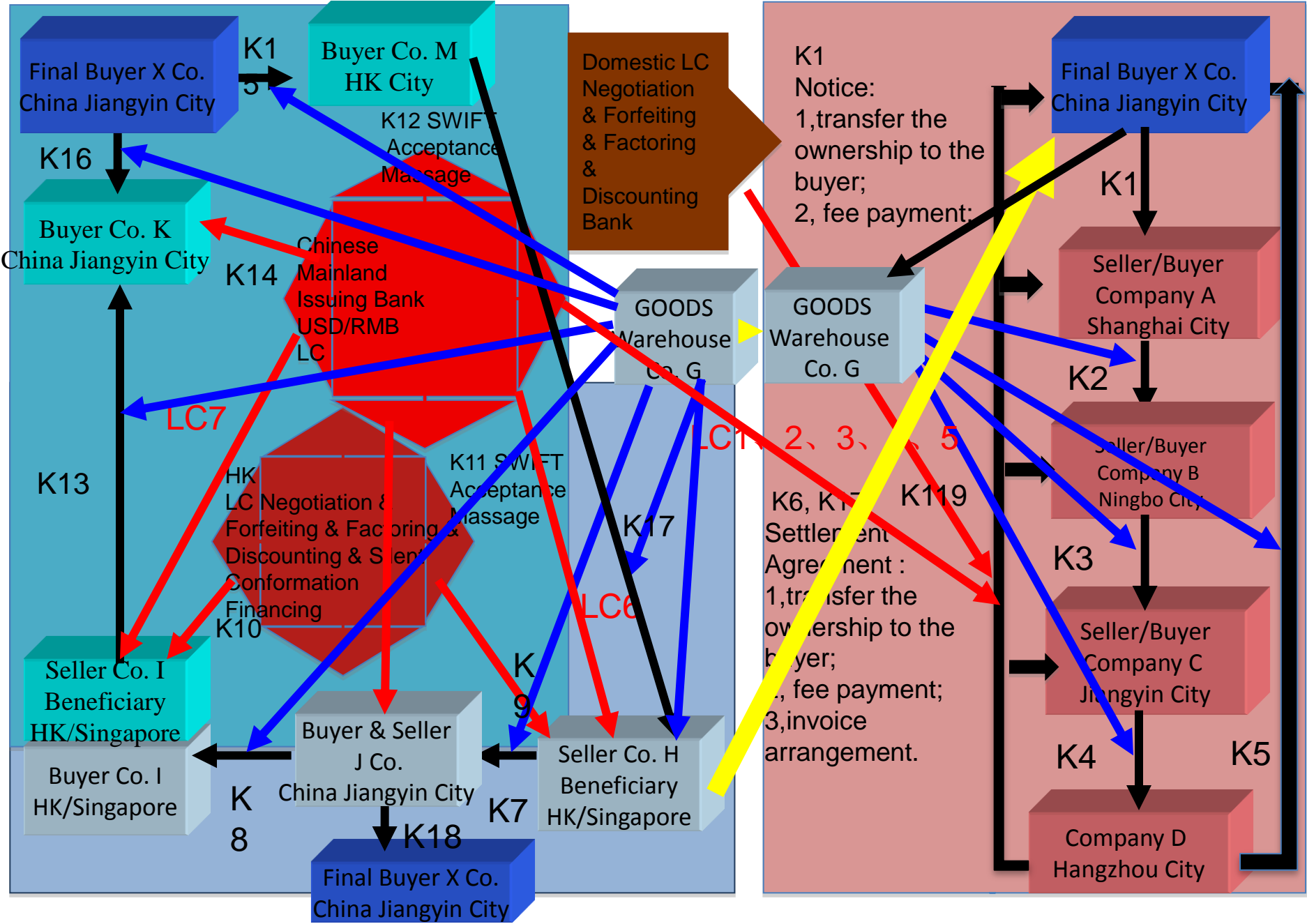
**■ Fraud Cases happened in China (Foshan)**



**■ Fraud Cases happened in China (Guangzhou)**

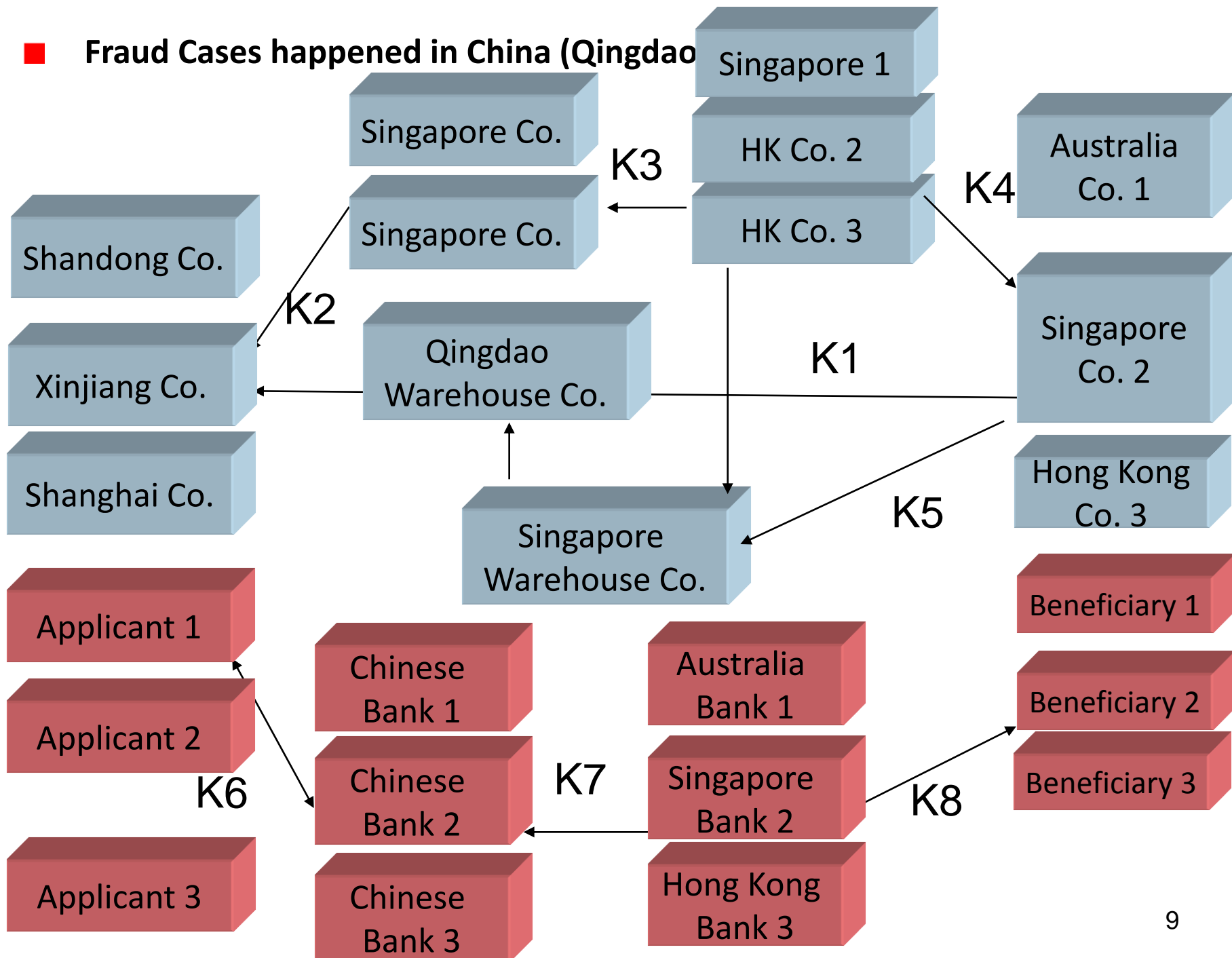


# General Picture: Why China Become No. 1 Trade Country?

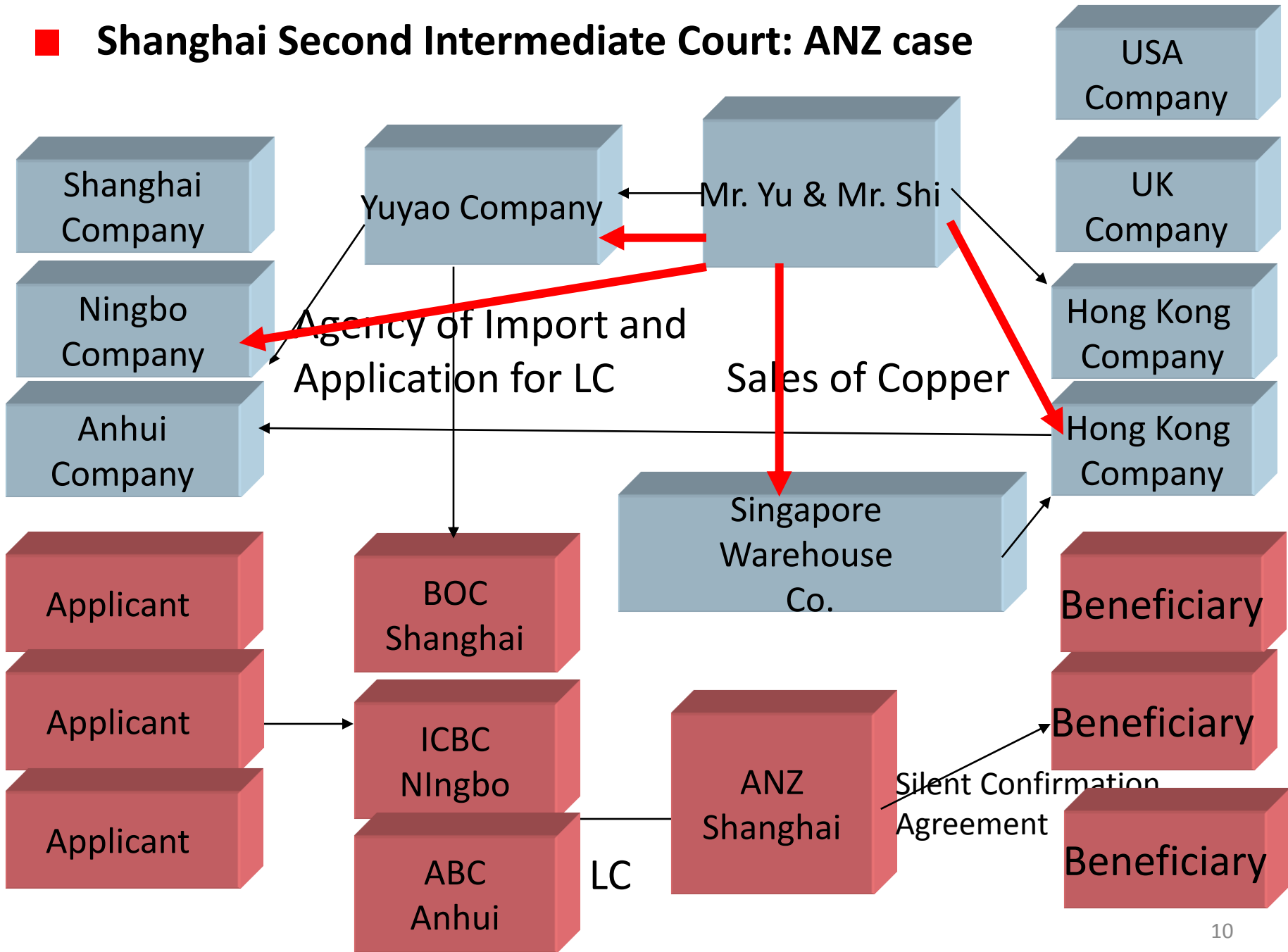




■ **Fraud Cases happened in China (Qingdao)**

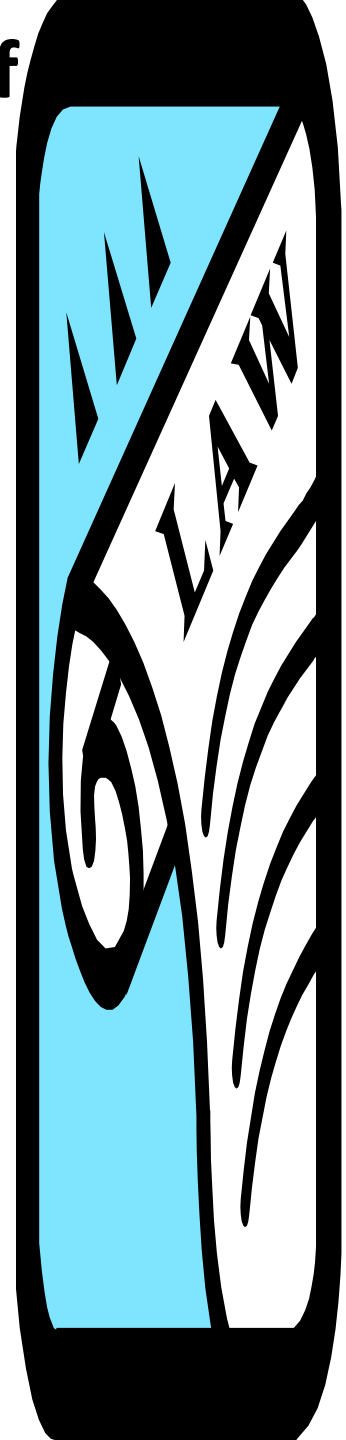


# Shanghai Second Intermediate Court: ANZ case



# ■ Criminal Law of the People's Republic of China

- **Criminal Law Article 195** Whoever commits fraud by means of a letter of credit in any of the following ways shall be sentenced to fixed-term imprisonment of not more than five years or criminal detention and shall also be fined not less than 20,000 yuan but not more than 200,000 yuan; if the amount involved is huge, or if there are other serious circumstances, he shall be sentenced to fixed-term imprisonment of not less than five years but not more than 10 years and shall also be fined not less than 50,000 yuan but not more than 500,000 yuan; if the amount involved is especially huge, or if there are other especially serious circumstances, he shall be sentenced to fixed-term imprisonment of not less than 10 years or life imprisonment and shall also be fined not less than 50,000 yuan but not more than 500,000 yuan or be sentenced to confiscation of property:
  - (1) using a forged or altered letter of credit or any of its attached bills or documents;
  - (2) using an invalidated letter of credit;
  - (3) fraudulently obtaining a letter of credit; or
  - (4) in any other ways.



# Criminal Law of the People's Republic of China

- **Article 199** Whoever commits the crime mentioned in Article 192, 194 or 195 of this Section shall, if the amount involved is especially huge, and especially heavy losses are caused to the interests of the State and the people, be sentenced to life imprisonment or death and also to confiscation of property.

# Criminal Law of the People's Republic of China

- **Article 177** Whoever commits any of the following acts of forging or altering financial bills shall be sentenced to fixed-term imprisonment of not more than five years or criminal detention and shall also, or shall only, be fined not less than 20,000 yuan but not more than 200,000 yuan; if the circumstances are serious, he shall be sentenced to fixed-term imprisonment of not less than five years but not more than 10 years and shall also be fined not less than 50,000 yuan but not more than 500,000 yuan; if the circumstances are especially serious, he shall be sentenced to fixed-term imprisonment of not less than 10 years or life imprisonment and shall also be fined not less than 50,000 yuan but not more than 500,000 yuan or be sentenced to confiscation of property:
  - (1) forging or altering bills of exchange, promissory notes or cheques;
  - (2) forging or altering settlement certificates of a bank such as certificates of entrustment with the receipt of payment, certificates of remittance and deposit receipts;
  - (3) forging or altering letters of credit or their attached bills and documents; or
  - (4) forging credit cards.
- Where a unit commits any of the crimes mentioned in the preceding paragraph, it shall be fined, and the persons who are directly in charge and the other persons who are directly responsible for the crime shall be punished according to the provisions in the preceding paragraph.

# ■ Several Opinions on the General Principle of Civil Law of China (Tentative) Article 67 (Supreme People's Court of China)



## ■ Article 4 of General Principles of the Civil Law

Principle of Good Faith

“In civil activities, the principles of voluntariness, fairness, making compensation for equal value, honesty and credibility shall be observed.”

## ■ Article 58 of General Principles of the Civil Law shall be applied:

...

(3) those performed by a person against his true intentions as a result of cheating, coercion or exploitation of his unfavorable position by the other party;

(4) those that performed through malicious collusion are detrimental to the interest of the state, a collective or a third party;

...

(7) those that performed under the guise of legitimate acts conceal illegitimate purposes. Civil acts that are null and void shall not be legally binding from the very beginning.

- **Several Opinions on the General Principle of Civil Law of China (Tentative) Article 67 (Supreme People's Court of China)**
- If a party deliberately tell false information or hide the true with the intention of cheating the other party, such acts shall be determined as fraud.

# The LC Judicial Interpretations of the Supreme People's Court in the Domestic LC cases



## 中华人民共和国最高人民法院公告

《最高人民法院关于审理信用证纠纷案件若干问题的规定》已于2005年10月24日由最高人民法院审判委员会第1368次会议通过，现予公布，自2006年1月1日起施行。

二〇〇五年十一月十四日

## 最高人民法院关于审理信用证纠纷案件若干问题的规定

(2005年10月24日最高人民法院审判委员会

第1368次会议通过 法释[2005]13号)



■ **LC Judicial Interpretation Published by the Supreme People's Court of China:Article 8**

- Credit fraud shall be deemed to exist in any of the following circumstances:
- (i) the beneficiary forges documents or incorporates false contents in any of the presented documents;
- (ii) the beneficiary, in bad faith, fails to deliver goods or delivers goods with no value;
- (iii) the beneficiary, in collusion with the applicant or any other third party, presents false document whereas no real underlying transaction exists; or
- (iv) other circumstances that involve credit fraud.

■ **LC Judicial Interpretation Published  
by the Supreme People's Court of  
China**



- Article 9 The LC applicant, the issuing bank or any other stakeholder(s), may apply to a people's court with competent jurisdiction for an order to suspend payment under the LC in the event that they find out that any of the circumstances provided in Article 8 occur and irreparable damages will be caused.

# ■ LC Judicial Interpretation Published by the Supreme People's Court of China



- Article 10
- In case LC fraud is found, the people's court shall render an order to suspend or a judgment to terminate payment under the LC, except under one of the following circumstances:
- (i) A party nominated or authorized by the issuing bank has made payment in good faith in accordance with the instructions of the issuing bank;
- (ii) The issuing bank or a party nominated or authorized by it has accepted the draft under the LC in good faith;
- (iii) The confirming bank has made payment in good faith; or
- (iv) The negotiating bank has negotiated the LC in good faith.

# ■ People's Bank of China: ■ Measures for Settlement by Domestic Letter of Credit

## 国内信用证结算办法

【颁布单位】 中国人民银行

【颁布日期】 19970716

【实施日期】 19970801

【章名】 第一章 总则

第一条 为适应国内贸易活动的需要，促进我国社会主义市场经济的健康发展，依据《中华人民共和国中国人民银行法》以及有关法律、法规，制定本办法。



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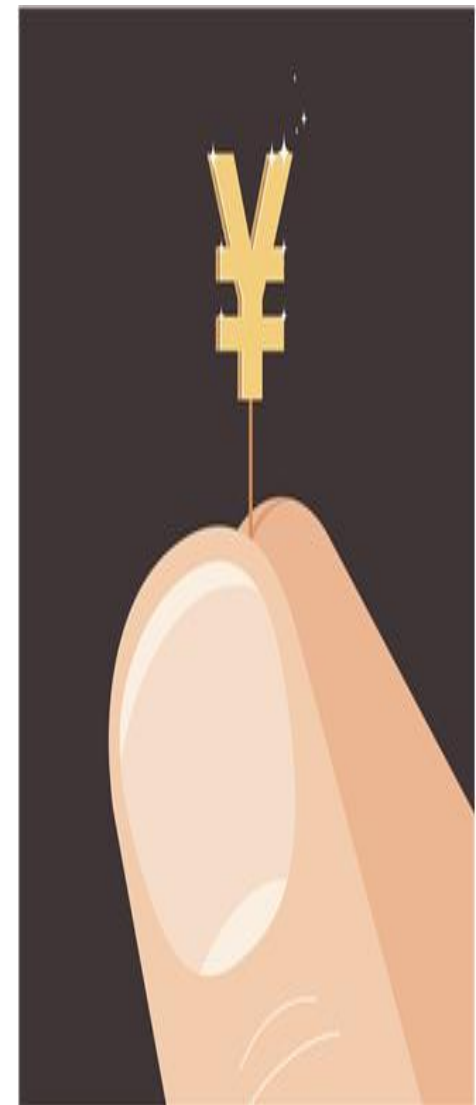
# ■ Measures for Settlement by Domestic Letter of Credit

**Article 1** These Measures are formulated in accordance with the Law of the People's Republic of China on the People's Bank of China and other applicable laws and regulations, with a view to adapting to the needs of domestic trading activities and boosting the healthy development of the socialist market economy of China.

**Article 2** For the purpose of these Measures, a letter of credit (L/C) shall refer to an undertaking issued by an issuing bank at the request of an applicant to pay an amount of money against documents that are in compliance with the terms and conditions in the L/C. The L/C as prescribed in the preceding paragraph shall be an irrevocable and non-transferrable documentary L/C.



- **Article 3** These Measures shall apply to settlement by L/C between and among domestic enterprises for commodity trading.
- **Article 4** Head offices of commercial banks that have been approved by the People's Bank of China to operate settlement business, and branch offices that have been approved by the head offices of commercial banks to operate settlement business by L/C may carry out settlement business by L/C.
- Banking institutions without approval and urban credit cooperatives, rural credit cooperatives as well as other non-banking financial institutions shall not engage in settlement business by L/C.
- **Article 5** The parties concerned in settlement by L/C shall comply with laws, regulations and these Measures, and may not prejudice social and public interests.
- The parties concerned in settlement by L/C shall follow the principle of good faith, perform their obligations conscientiously, and may not involve in fraudulent activities in violation of the law by means of L/C.



# **Notice of the State Administration of Foreign Exchange on Improving Foreign Exchange Administration over Trade Financing Business of Banks**

- Promulgating Institution: State Administration of Foreign Exchange
- Document Number: Hui Fa [2013] No.44
- Promulgating Date:12/06/2013
- Effective Date:12/06/2013

# **Notice of the State Administration of Foreign Exchange on Improving Foreign Exchange Administration over Trade Financing Business of Banks**

- **1. The trade receipts and payments of enterprises shall be authentic and legitimate.**

The trade (including entrepot trade, the same below) receipts and payments of an enterprise shall be based on authentic and legitimate import and export transactions or production and business operations. No enterprise may fabricate trade background to conduct cross-border collection and payment business by making use of bank credit.



## **Notice of the State Administration of Foreign Exchange on Improving Foreign Exchange Administration over Trade Financing Business of Banks**

- **2. Banks shall improve the authenticity and compliance review of trade financing.**

A bank shall follow the principle of "know your clients", effectively perform the duties to review the authenticity and compliance of trade financing, actively support the real trade financing needs of the real economy, and prevent enterprises from fabricating trade background to defraud bank financing.

(1) Where an enterprise applies to the bank for handling trade financing business under cross-border transactions by way of letters of credit, collection, etc., the bank shall, based on the enterprise's production and business operations, financial conditions, products, market conditions and other information, confirm the authenticity and compliance of the relevant trade background, and verify whether the amount and the term of trade financing match the corresponding trade background.

- (2) As regards forward trade financing business (referring to a period of over 90 days, including a cumulative period of over 90 days in the event of an extension of spot business or the continuation thereof as other forms of trade financing business, the same below), regardless of whether the bank has collected deposits in full or of a high percentage, the bank shall step up review based on its knowledge of the client as long as any of the following circumstances exists; and where the bank has doubts over the authenticity or compliance of the trade financing business, it shall require the enterprise to provide transaction-related contracts and the originals of the certificates proving its rights to the goods concerned, so as to effectively identify financing activities against fictitious trade background:
  - a. Where the client's financing business has any of the following features: the client engages in financing business in a high frequency or on a large scale; its transaction counterparties are relatively concentrated or are affiliated enterprises; or there is a prominent mismatch between foreign currencies and RMB in the client's trade receipt and payment;
  - b. Where the goods corresponding to the financing have any of the following features: the goods are of high value themselves; the goods enjoy high production value-added; the goods are easy to transport due to small size; the packaging and storage of the goods can be easily standardized; etc.; or
  - c. Where the client engages in foreign trade activities through entrepot trade, resale (referring to the import of goods via special customs regulatory zones and the subsequent export thereof through resale) and other forms.

- (3) The bank shall strengthen due diligence investigation of the authenticity and compliance of trade financing, develop relevant risk prevention internal control systems, and step up the initiative and sensitivity to identify suspicious transactions. It shall strengthen the supervision and guidance over its business departments, branches and outlets, and strictly prohibit the circumstances where the grass-roots departments, branches or outlets of the bank relax review requirements, or even help clients evade provisions on foreign exchange administration for the purpose of achieving performance assessment targets.  
(4) Where the bank, during daily business handling, finds that an enterprise falls under any of the circumstances prescribed in Item (2) of this Article and that the transaction in question is suspicious, it shall promptly report pertinent information to the relevant branch or sub-branch of the State Administration of Foreign Exchange ("SAFE") (hereinafter referred to as the "Foreign Exchange Bureau"), and actively cooperate with the Foreign Exchange Bureau to take measures to prevent the inflow of abnormal cross-border capital.

- **3. The classified administration over the foreign exchange trade receipts and payments of enterprises shall be improved.**

A Foreign Exchange Bureau shall issue to a Class-A enterprise that falls under any of the following circumstances a Written Risk Reminder, and require the said enterprise to explain relevant situations within ten working days: where there is a serious mismatch between the flow of funds and the flow of goods; where the said enterprise has large and fast-growing receipts and payments under entrepot trade; where the said enterprise has large amount of forward trade financing which accounts for a high percentage of all its trade financing; or where the said enterprise has the typical characteristics of cross-border financing arbitrage transactions, etc.

- Where the Class-A enterprise fails to promptly explain relevant situations or is unable to provide reasonable explanations, the Foreign Exchange Bureau shall put the said enterprise under Class B pursuant to Article 55 of the Detailed Rules for Implementation of the Guidelines on Foreign exchange Administration over Trade in Goods (printed and distributed by the document of Hui Fa [2012] No. 38) and other relevant provisions, and shall, under grave circumstances, put the said enterprise under Class C for rigorous regulation.

Where the said enterprise meets relevant indicators for three consecutive months and satisfies other conditions after being listed as a Class-B enterprise pursuant to the preceding Paragraph, the Foreign Exchange Bureau shall re-classify the said enterprise as a Class-A enterprise. Where the said enterprise fails to satisfy the conditions for being restored as a Class-A enterprise, the period of classified regulation shall be extended by three months. Where the said enterprise still fails to satisfy such conditions upon expiry of the six-month regulatory period, depending on the severity of the circumstances, the period of classified regulation shall be extended by another year, or the said enterprise shall be changed to a Class-C enterprise from a Class-B enterprise, and be subject to a regulatory period of one year.

- **4. The monitoring and verification of the authenticity and compliance of banks' trade financing business shall be stepped up.**

A Foreign Exchange Bureau shall step up the monitoring of the authenticity and compliance of a bank's trade financing business. Where the bank has a high percentage of forward trade financing business and provides trade financing services for enterprises suspected of fabricating trade background for cross-border arbitrage, the Foreign Exchange Bureau may randomly inspect a certain percentage of the bank's business data, assess the bank's due diligence review of the authenticity and compliance of transactions, and conduct on-site verification or inspection where necessary.

Where the bank obstructs or refuses to accept the on-site verification or inspection of the Foreign Exchange Bureau, or where it is found during random business inspection and on-site verification or inspection that the bank has failed to fully perform its review duties when handling trade financing business, the Foreign Exchange Bureau may issue risk reminders to the bank, or mete out punishments pursuant to the Regulations on Foreign Exchange Administration and other relevant regulations.

- **5. Heavier punishments shall be meted out.**

Banks and enterprises in violation of this Notice shall be punished by Foreign Exchange Bureaus in accordance with the Regulations on Foreign Exchange Administration and other relevant regulations. Whoever engages in fictitious trade to remit foreign exchanges into Mainland China by forging or altering certificates and commercial documents or by repeatedly using the same certificates and commercial documents shall be punished based on the nature of generating illegal foreign exchange inflow; whoever settles foreign exchange earnings shall be punished based on the nature of illegal foreign exchange settlement; whoever purchases foreign exchange by fraudulent means shall be punished based on the nature of illegal foreign exchange arbitrage; and whoever remits domestic foreign exchanges abroad shall be punished based on the nature of foreign exchange evasion. Where criminal offenses are constituted, criminal liabilities shall be investigated for pursuant to the law.

- **Four Most Important Lessons when you dealing with China**
- **Yes, KYC (Know Your Customer)**
- **But, KYCC (Know Your Customer's Customer)**
- **the Most Important Today: KYCM (Customer Manager )**
- **Do not Know What You Should Not Know!**



## ■ Thanks & Disclaimer

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- All the views and material in the lecture can not be regarded as my official legal opinion.
- I accept no responsibility for loss occasioned to any person acting or refraining from acting as a result of views and material contained in this article.
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■ More information available at

**Jinsaibo's blog:**

**<http://blog.sina.com.cn/jinsaibo>**

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