

REGISTRATION OF GUARANTEES WITH FOREIGN BENEFICIARIES

By Prof Peter Koh*

Introduction:

Guarantees can be issued by both individuals and corporate entities. Corporate entities can be financial and non-financial. Financial entities will include insurance companies and banks and other types of financial entities. Non-financial entities include limited liability companies and joint stock limited liability companies (listed and non listed)

Guarantees issued by domestic institutions, corporate entities and individuals in People's Republic of China ("PRC") are subjected to the approval by and registration with the State Administration for Foreign Exchange ("SAFE") in situations involving either foreign debtors or beneficiaries. The foreign debtors or beneficiaries are always corporate entities or institutions.

Guarantees issued by a bank

There are two kinds of guarantee:

"Financing guarantees" generally refer to guarantees provided for loans, bond issuance and financing leases and other forms recognized by the SAFE;

"Non-financing guarantees" generally refer to quality guarantee, guarantee for liability for completion of a project, tender guarantee, advance payment guarantee, deferred payment guarantee and performance guarantee under a goods purchase and sale contract and other forms recognized by the SAFE.

For non-financing guarantees, a bank does not need to apply to the SAFE on a case-by-case basis. Such guarantees are not subjected to the quota limitation imposed on banking and financial institutions.

For financing guarantees, a bank has to apply to the local SAFE for a quota for issuance of guarantees to foreign parties. Within the quota approved by the SAFE, the bank may provide financing guarantees at its sole discretion, and need not apply to the SAFE for approval on a case-by-case basis.

Paragraph 1 of Article 5 of the *Notice of the State Administration of Foreign Exchange on the Administration of External Guarantees Provided ("the Notice") by Domestic Institutions* states:

A domestic bank shall, before April 15 of each year, apply to the local foreign exchange authority for the current year's quota, and the local SAFE branch shall gather such applications and make a preliminary examination of them.

Article 7 of the *Notice* further stipulates:

Generally, the quota for a single bank shall not exceed 50% of its paid-in capital or working capital in both RMB and foreign currency, or will not exceed its foreign exchange net asset value.

However, the domestic bank (or its headquarter in charge of the overall quota management) has to report the data involving the issuance of guarantees (including financing and non-financing) to the

SAFE every month.

Guarantees issued by a non-bank company

Guarantees (including financing and non-financing) issued by a non-financial entity has to be approved by and registered with SAFE on a case-by-case base.

First of all, SAFE has to approve such guarantees. SAFE will evaluate the qualifications of both the guarantor and the debtor. For example, if the guarantor is a non-banking financial institution, the debtor must be a corporate entity legally structured and incorporated within PRC. The debtor can also be an overseas subsidiary or associate company of the guarantor. The shares of the overseas or associate company can be held directly or indirectly by the guarantor.

After the approval is granted by SAFE, the guarantor has within 15 days to execute the guarantee instrument and register it with SAFE.

In some cases where a viable and well managed company has a large number of guarantees to be issued, it can also apply to SAFE for a quota for the guarantees. Within the approval quota, the guarantor needs not apply for case-by-case approval for every guarantee. There is still a need for registration with SAFE.

Article 13 of the *Notice* provides:

For a domestic non-banking financial institution or enterprise (including a wholly foreign-funded enterprise) which has a large number of external guarantees and sound internal management, its corporate body may apply to the foreign exchange authority for a balance quota of external guarantees (including financing ones and non-financing ones) under the procedures prescribed in Articles 5 and 8 of this Notice.

There is no specific definition on a ‘well-managed company’. According to the latest *Operational Guidelines for Foreign Exchange under Capital Project* published by SAFE in August 2013, the essential elements for deciding whether a company is with sound internal management will mainly include the paid-up capital, the operational funds, the scale of foreign exchange net assets, total assets, net assets, as well as the plan for external guarantees of the current year.

Guarantees issued by an individual

According to the *Guarantee Law of the P.R.C.*, the *Measures for the Administration of Individual Foreign Exchange*, and the *Detailed Rules for Implementation of Measures for the Administration of Individual Foreign Exchange*, an individual is allowed to provide guarantee to a foreign company or institution, subject to the approval by and registration with SAFE.

However, there is no law or regulation which provides the guidelines or procedure for such guarantee. Even in the latest *Operational Guidelines for Foreign Exchange under Capital Project* published by SAFE in August 2013, there is no guideline for such item as “overseas guarantee issued by an individual”. As a result, such individual guarantee may become practically not feasible.

Notwithstanding the above, a notice published by SAFE in June 2012 enables a domestic individual to provide the guarantee in the following way:

When a domestic enterprise provides financing guarantee for the overseas companies, a domestic

individual is allowed to provide guarantee with the domestic enterprise for the same debt. The domestic individual will authorize the domestic enterprise to apply for approval by the SAFE.

The law is silent as to whether the joint financing arrangement can be made jointly and severally. It is always an advantage to structure the arrangement on a joint and several basis.

Article 3 of the *Notice of the State Administration of Foreign Exchange on Foreign Exchange Administration Issues concerning Encouraging and Guiding the Healthy Development of Private Investment* states:

To support the international presence of Chinese enterprises, when a domestic enterprise provides security for the overseas financing of an overseas investee, a domestic individual is allowed to provide security together with the enterprise for the same debt in the form of guarantee, mortgage or pledge or any other form as permitted by laws and regulations on guarantee....

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