

## China to Facilitate New Forms of Offshore International Trade

KELLY MOK

ADVISORY DEPARTMENT  
JAPANESE CORPORATE BANKING DIVISION

T +852-2249-3938  
E KELLY\_MY\_MOK@HK.MUFG.JP

**MUFG Bank, Ltd.**  
(Incorporated in Japan with limited liability)  
A member of MUFG, a global financial group

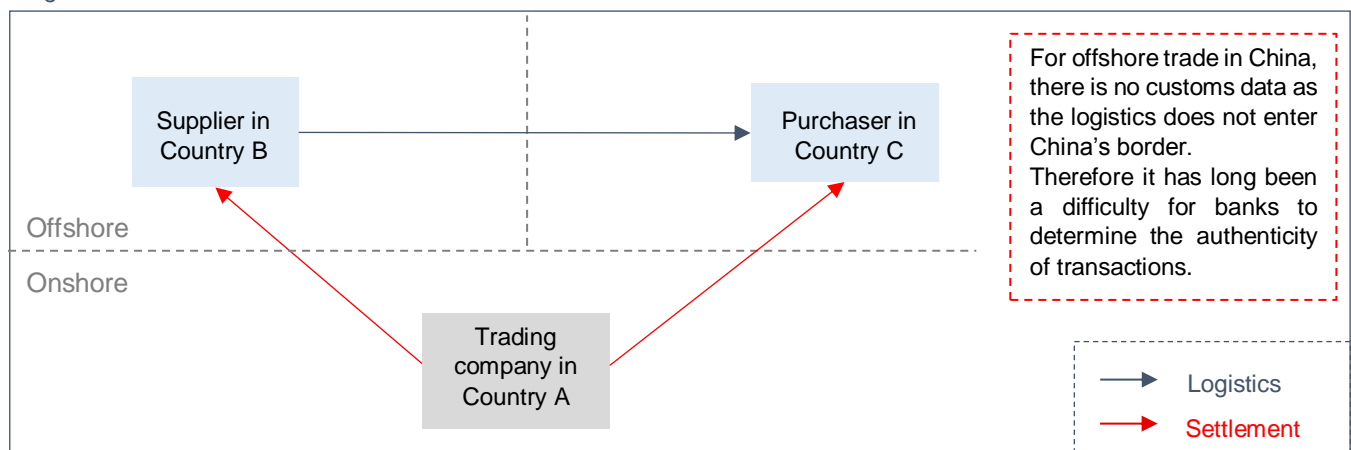
29 APRIL 2022

On 24<sup>th</sup> Dec 2021, the People's Bank of China (hereinafter "PBOC") and the State Administration of Foreign Exchange (hereinafter "SAFE") jointly released "Notice Concerning Supporting New Forms of Offshore International Trade" (Yinfa [2021] No. 329) (hereinafter "this Notice"). This Notice has taken effect since 24<sup>th</sup> Jan 2022.

### BACKGROUND

Since triangular trade (hereinafter "offshore resale", in Chinese "離岸轉手買賣". Please refer to Diagram 1) was officially recognized in China from 2012, there had been risks of unlawful cross-border fund flows due to its characteristic of "invisible" logistics or lack of transparency on logistics. Fabricated offshore resale transactions and illegal financing frauds were especially frequent in 2014. From 2015 onwards, the authorities had strengthened supervision on offshore resale and a considerable number of cases of heavy fine impositions had been reported. As a result, banks considered offshore resale as high risks transactions, and implemented strict and cautious regulatory controls on related settlements. Such measures also affected genuine offshore resale enforcement.

Diagram 1



The Chinese government is attaching much more importance to vitalizing and expanding international trades due to the recent economic slowdown in China, as well as the government's aim on "balancing dual circulation". Meanwhile, strict regulations for offshore trade do not suit the current trends. Especially when financial reform frontiers such as Shanghai's Lingang Free Trade Zone, Hainan Free Trade Port, and Greater Bay Area are not able to meet the needs of international trading companies, here comes the chance to further enhance the liberalization and convenience of various cross-border settlement including offshore resale.

With external factors such as stable RMB exchange rates and foreign exchange reserve, the risk of capital outflow from China is being controlled comparatively. Against such a backdrop, PBOC and SAFE released this new concept of "new forms of offshore international trade" to relax long stringent offshore trade restrictions. Not limited to offshore

resale, global procurement (including service), overseas contract manufacturing and other offshore trade schemes also became possible. It is expected that offshore international trades originated from China will continue to increase.

## THE HISTORY AND DEVELOPMENT OF OFFSHORE RESALE REGULATIONS IN CHINA (EXTRACT)

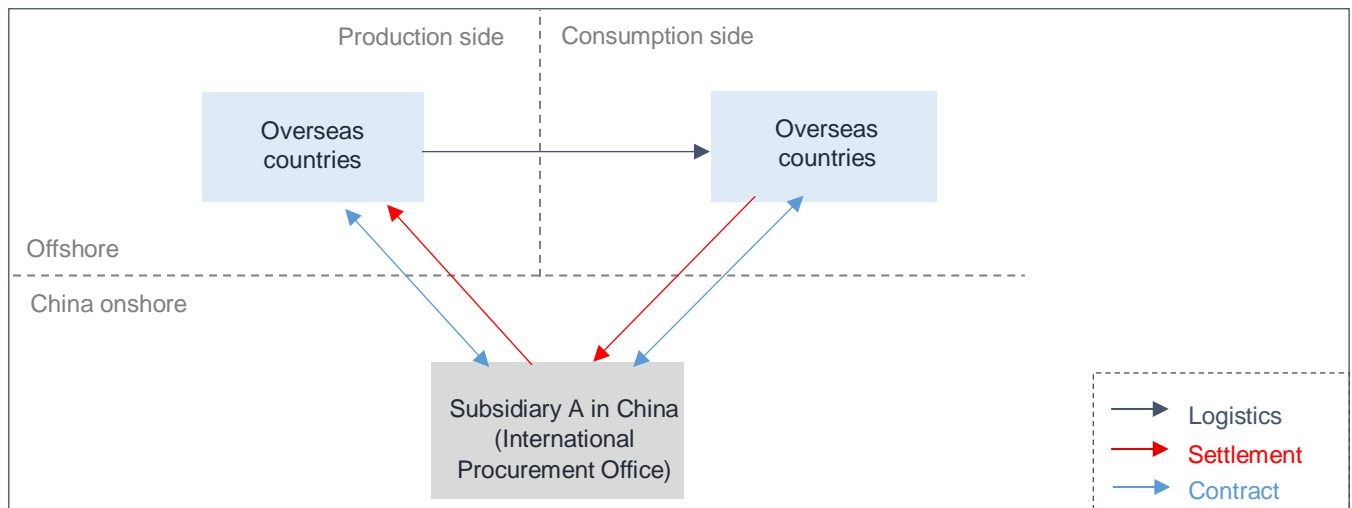
| Year | Content   | Characteristics                                     |
|------|---|---|
| 2012 | <ul style="list-style-type: none"> <li>Triangular trade was officially recognized after the reform of foreign currency regulations on goods (Huifa [2012] No.38)</li> </ul>   | Triangular trade began                              |
| 2013 | <ul style="list-style-type: none"> <li>Frequent fabricated triangular trade occurred due to simplified cross-border RMB settlement</li> <li>Review on triangular trade authenticity was strengthened</li> </ul>   | Regulations tightened                               |
| 2014 | <ul style="list-style-type: none"> <li>Alleged financing fraud (The Qingdao scandal) occurred</li> <li>SAFE announced the amount generated from fabricated triangular trade reached US\$10 billion nationwide</li> <li>Triangular trade was defined as “offshore resale” in international declaration of balance of payments and receipts</li> </ul>  | Unlawful incidents occurred<br>Definition clarified |
| 2015 | <ul style="list-style-type: none"> <li>Review on offshore resale transactions in RMB was strengthened</li> </ul>  | Regulations tightened                               |
| 2016 | <ul style="list-style-type: none"> <li>Documentation review in all aspects was tightened for offshore resale transactions. It explicitly required that the transaction should be processed by “the same bank and same branch in the same currency”. The transaction by companies in category B of trade in goods was suspended (Huifa [2016] No.7)</li> <li>Electronic evidence was allowed for payments and receipts for trade in goods, while offshore resale transactions were excluded</li> </ul> | Regulations tightened                               |
| 2017 | <ul style="list-style-type: none"> <li>Offshore resale transactions in RMB were temporarily suspended</li> </ul>  | Regulations tightened                               |
| 2019 | <ul style="list-style-type: none"> <li>For revenue generated from offshore resale, companies in category A of trade in goods were able to decide autonomously on whether to make deposit into bank account which was pending for review</li> </ul>  | Regulations partially relaxed                       |
| 2020 | <ul style="list-style-type: none"> <li>Regarding offshore resale, the regulation of being processed “by the same bank and branch, in the same currency” was revised to “by the same bank in the same currency”</li> <li>The banks were able to settle “special offshore resale” transactions upon verifying that the trade was genuine and lawful</li> </ul>  | Regulations partially relaxed                       |
| 2021 | <ul style="list-style-type: none"> <li>The authorities encouraged the development of new forms of offshore international trade (Yinfa [2021] No.329) (This notice)</li> </ul>   | Regulation fully relaxed                            |

## MAIN CONTENT (EXTRACT)

| ① Definition of offshore international trade |  |
|--|--|
| <b>Main Content</b>                          | <ul style="list-style-type: none"> <li>“New forms of offshore international trade” refers to trade between residents and non-residents in China. The goods do not enter or exit China’s first-line border or are excluded from the customs statistics. The trades include but not limited to offshore resale, global sourcing, overseas contract manufacturing, and overseas procurement for construction contracts</li> </ul>   |
| <b>Comment</b>                               | <ul style="list-style-type: none"> <li>On top of the previous offshore resale (triangular trade), the forms and models of offshore trades listed in this Notice are applicable</li> <li>The wordings in this Notice “including but not limited to” implies the possibilities beyond the above mentioned trade models. It also indicates the authorities’ intention to promote trade diversification</li> <li>From companies’ perspectives, new forms of offshore international trades could establish new business models and thus create new source of revenue</li> </ul> |

The diagrams below show a few examples of the new forms of offshore trades listed in this Notice. As it is created based on the related notices and external news, please confirm with the authorities and banks in respective regions for actual feasibility.

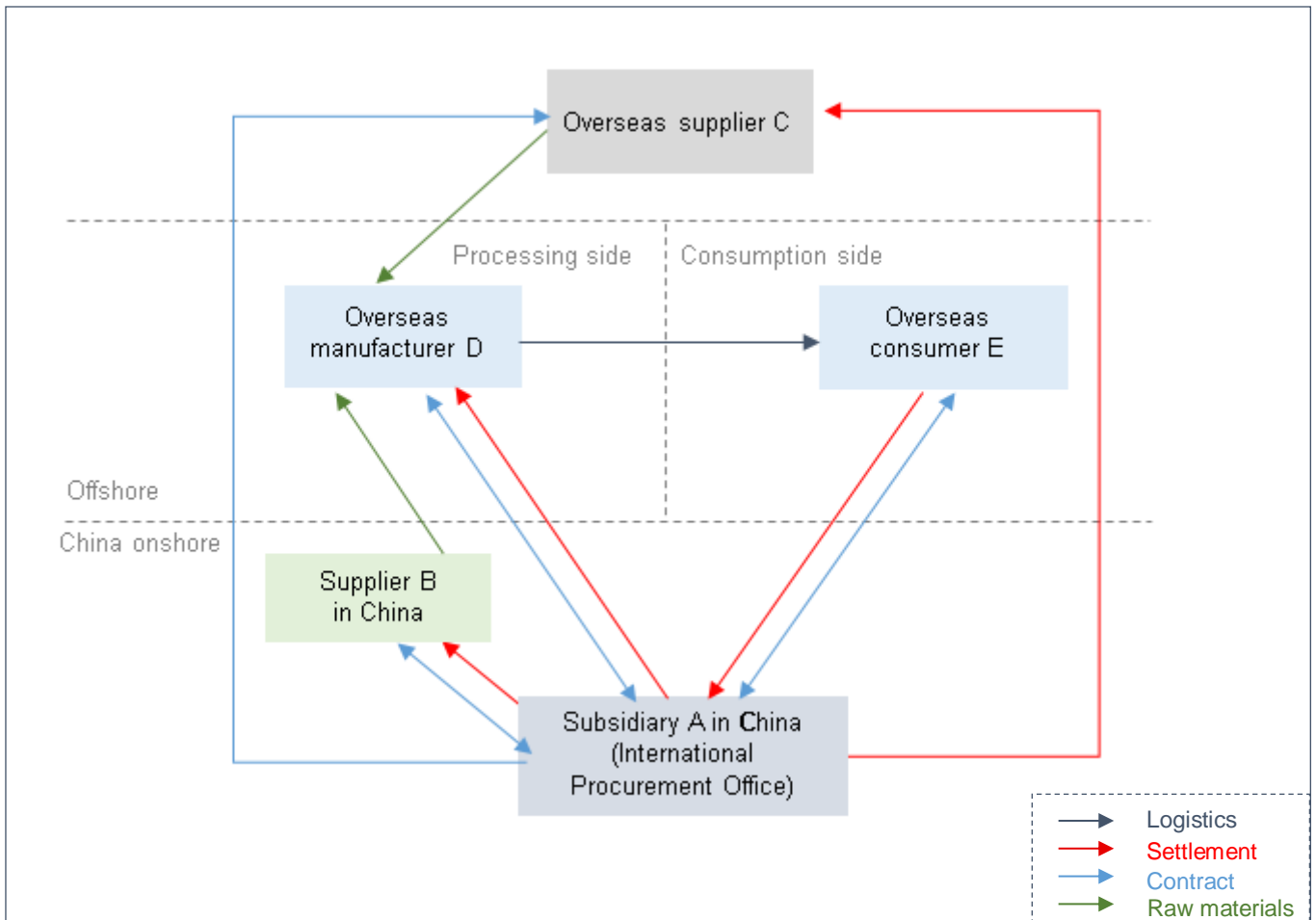
Diagram 2



[Description]

- Subsidiary A in China purchased goods or services from any overseas countries, the goods or services would then be directly sent to overseas end-users without entering or exiting China
- International procurement offices (IPOs) would be the general users of this scheme. There are advantages such as management standardization & sophistication, and easier profit adjustment by centralizing global purchasing & sales, logistics & cash flow at the IPOs

Diagram 3



[Description]

- Subsidiary A in China purchased raw materials from supplier B in China, or overseas supplier C, the raw materials were then shipped to overseas manufacturer D for processing. The finished goods would eventually be shipped from D to overseas consumer E
- International companies engaged in processing trade are assumed to be the users of this scheme. It is also suitable for domestic and foreign raw materials suppliers and companies with overseas customer resources. Purchasing high quality raw materials by low prices globally, outsourcing processing to countries with relatively low processing and manufacturing cost (RCEP members like South East Asia) can help provide high added value to finished goods

| ② Principles of banks' review |  |
|-------------------------------|--|
| <b>Main content</b>           | <ul style="list-style-type: none"> <li>■ Banks are to align with the rules of “substance over form” to perform “know your customer”, “know your business” and “customer due diligence” when processing cross-border fund settlement for new forms of offshore international trades</li> <li>■ Based on the above premises, banks are to determine the types of documentations for review at their own discretion by following the below rules:               <ul style="list-style-type: none"> <li>○ The trade is genuine, lawful and commercially rational and logical</li> <li>○ Review does not find the companies or parties to have suspected transactions of new forms of offshore international trades (e.g. trades for speculation and arbitrage, unlawful funds shifting, bank loan fraud etc.)</li> </ul> </li> </ul> |

|                |  |
|----------------|--|
| <b>Comment</b> | <ul style="list-style-type: none"> <li>■ The extent of simplification for documentation review is left to banks' determination. It implies the authorities requires flexible support from the banks for offshore international trades. Therefore the previous strict review could be avoided</li> <li>■ On the other hand, enterprises should pay attention to the ways to prove the transactions to be genuine, logical and rational</li> </ul> |
|----------------|--|

|   |   |
|---|---|
| <b>③ Centralized payment and receipt and net settlement services are also available</b> |   |
| <b>Main content</b>   | <ul style="list-style-type: none"> <li>■ Multinational corporations that possess sound internal control with genuine needs for offshore resale transactions, could apply for centralized payment and receipt and net settlement services under current account, in accordance with the requirements of <i>Regulations on the Centralised Operation and Management of Cross-border Capital of Multinational Companies</i> (Huifa [2019] No.7)</li> </ul> |
| <b>Comment</b>  | <ul style="list-style-type: none"> <li>■ Centralised payment and receipt and net settlement services were once prohibited and it is now executable. Multinational corporations could enjoy efficient settlement and financial management</li> </ul>   |

|   |   |
|---|---|
| <b>④ “Special offshore resale” is now enforceable</b> |   |
| <b>Main content</b>                                   | <ul style="list-style-type: none"> <li>■ In general, the same offshore resale transaction should be processed by the same bank in the same currency (either RMB or foreign currency)</li> <li>■ If the above rules is not feasible, upon verifying the transactions are genuine and lawful, the banks may directly handle the settlement and note “special offshore resale” in the remark section on reporting system</li> <li>■ The banks are to report the transaction to the respective local SAFE branch within five business days</li> </ul> |
| <b>Comment</b>  | <ul style="list-style-type: none"> <li>■ The measure provides more flexibilities for banks to handle reviews for offshore resale transactions</li> <li>■ After confirming the trade is genuine and lawful, it is possible for the banks to settle the payments and receipts even if the offshore trade rules could not be satisfied. Therefore flexible utilization is expected</li> </ul>  |

## INFLUENCES ON ENTERPRISES

- Enterprises are able to generate new sources of revenue from constructing new forms and models of offshore trade
- With RCEP coming into effect from 1<sup>st</sup> Jan 2022, international trades among RCEP member countries are expected to be more active. By utilizing the regulation relaxation, subsidiaries in China can participate in new RCEP business flow, also to expand business in China as well as overseas
- Being recognized by the Chinese authorities, the trade in goods circulating overseas or direct offshore usage do not have to go through customs clearance in China. Logistics costs and customs taxes could be alleviated
- On the other hand, overseas logistics information fact-checking is still difficult. However, the collaboration between banks and enterprises is essential for confirming whether the trade is genuine and lawful. Enterprises' internal management system enhancement is required for the development of offshore international trade

We will keep an eye closely on related policy trend and update the development accordingly.

|            | Publish date | Title   |
|------------|--------------|---|
| No.1, 2022 | 2022/3/2     | <a href="#">Higher Level of Opening Up for Cross-border Trade and Investment in Selected Areas in China</a> |

- Please refer to the below links for previous News Focus:

(English) [https://www.bk.mufg.jp/report/chi200402/Archive\\_ENG.pdf](https://www.bk.mufg.jp/report/chi200402/Archive_ENG.pdf)

(Japanese) [https://www.bk.mufg.jp/report/chi200402/Archive\\_JP.pdf](https://www.bk.mufg.jp/report/chi200402/Archive_JP.pdf)

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