



# **The New Chinese Independent Guarantee Rules & Legal Issues in Trade with China**

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# Presenter



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# With kind support of



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**Title: Provisions of the Supreme  
People's Court on Several Issues  
Concerning the Trial of Disputes over  
Independent Guarantees  
Fa Shi [2016] No.24**



**Adopted 7 July 2016**

**Take Effect at 1st December 2017**

# **26 Articles: Parts & Titles**

- **Articles 1-5: Part A: Definition and Scope**
- **Articles 6-8: Part B: Compliance and Waiver**
- **Articles 9-11: Part C: Reimbursement, Transfer, and Termination**
- **Articles 12-20: Part D: Independent Guarantee Fraud**
- **Articles 20-21: Part E: Jurisdiction & Law**
- **Article 23: Part F: Independent Domestic Guarantees**
- **Article 24: Part G: Cash Collateral**
- **Articles 25-26: Part H: Effectiveness & Applicability of Provisions**

## Effective as of 1 December 2016

- ▶ **Article 26: Effective 1 December 2016**
- ▶ **Article 25: [*Applicability.*]**
- ▶ These Provisions shall apply to those cases in which the final judgment is pending on the effective date of these Provisions; but these Provisions shall not apply to the cases in the retrial proceedings launched upon any party's petition or in accordance with the judicial supervision procedure by a People's Court, for which final judgments have been rendered prior to the effective date of these Provisions.
- ▶ **Retrial**
- ▶ **Apply to any dispute where no final judgment**

# Article 1: Key Terms 1<sup>st</sup> ¶:

## **“Independent Guarantee”**

- ▶ For the purpose of these Provisions, “Independent Guarantee” refers to an undertaking given in writing by a bank or a non-bank financial institution as the Issuer to the Beneficiary, by which the Issuer undertakes to pay the Beneficiary an amount up to the maximum amount of the guarantee upon the Beneficiary’s demand for payment and presentation of documents complying with the terms and conditions of the Guarantee.
- **“Issuer”:** Financial Institution
- **Written Undertaking**
- **Up to maximum Amount**
- **On demand & presentation of complying documents**



# Article 3: Independence

- ▶ Except where a Guarantee does not specify any document against which the payment shall be made or the maximum amount payable, a party's claim that the guarantee is an Independent Guarantee shall be supported by a People's Court if:

(1) the guarantee states that it is payable on demand;

(2) the guarantee states that it is subject to the *ICC Uniform Rules for Demand Guarantees* or other model rules for independent guarantee transactions; or

(3) based on the text of the Guarantee, the Issuer's payment obligation is independent from the underlying transaction relationship or guarantee application relationship, and the Issuer is liable for payment only against a complying presentation.

A party's claim that the nature of a guarantee is a general guarantee or a guarantee with joint and several liability, on the ground that such guarantee refers to the relevant underlying transaction, shall not be supported by a People's Court.

A party's claim that the rules applicable to general guarantees and guarantees with joint and several liability under *the Security Law* shall apply to an Independent Guarantee shall not be supported by a People's

## Reformulation of Article 3:

To be Independent, a Guarantee

- ▶ **must specify a document to be presented and a maximum amount**
- ▶ **and either**
  - ▶ State that it is payable on demand,
  - ▶ State that it is subject to practice rules, OR
  - ▶ Contain text making it independent from the underlying transaction and relationship between Issuer and Applicant & liability only for complying documentary presentation
- ▶ **A reference to the underlying transaction does not make it dependent**
- ▶ **If it is independent, the law related to Dependent Guarantees or Security does not apply.**

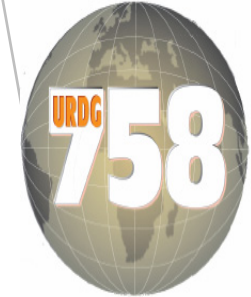




# **Compliance & Reimbursement**

# Article 5: Model Practice Rules

- ▶ Where an Independent Guarantee states that it is subject to the Uniform Rules for Demand Guarantees or other model rules for independent guarantee transactions, or where the aforementioned rules are cited without objection by both the Issuer and the Beneficiary prior to conclusion of arguments in the trial proceedings, a People's Court shall take such model rules as an integral part of the Independent Guarantee.
- **Two options: subject to or by agreement in litigation**
- **Part of Independent Guarantee**
- **Can a court refer to Practice Rules? [Article 7]**
- **Unanswered: what if the practice rule varies the Provisions?**



# Article 6: Honour or Payment

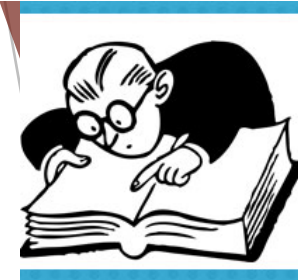
- ▶ Where the documents presented by the Beneficiary comply on their face with the terms and conditions of the Independent Guarantee and are consistent with one another, the Beneficiary's claim against the Issuer for payment under the Independent Guarantee shall be supported by a People's Court.

The Issuer may not seek to excuse its payment obligation based on defenses arising out of the underlying transaction relationship or the Independent Guarantee's relationship with the Applicant and such defenses shall not be supported by a People's Court, except under the circumstances provided in Article 12 [*Fraud*] of these Judicial Provisions

- ▶ Honour required where
  - ▶ Presented documents comply
  - ▶ Consistent with one another: Vary?
- ▶ No excuse re underlying transaction
- ▶ Fraud exception recognised



# Article 7: Compliance



- ▶ A People's Court shall decide whether documents comply on their face in accordance with the terms and conditions of the Independent Guarantee. In determining compliance, a People's Court may refer to relevant examination standards formulated by the International Chamber of Commerce.

Documents which do not appear on their face to be completely consistent with the terms and conditions of the Independent Guarantee or with one another shall be found by a People's Court to be complying on their face if no different meaning is thereby caused.

- ▶ **Relevant examination standards: what are they? ICC Opinions?**
- ▶ **Not "completely consistent" documents comply if no different meaning**



# Independent Guarantee Fraud

Articles 12-20

# Article 12: Independent Guarantee Fraud

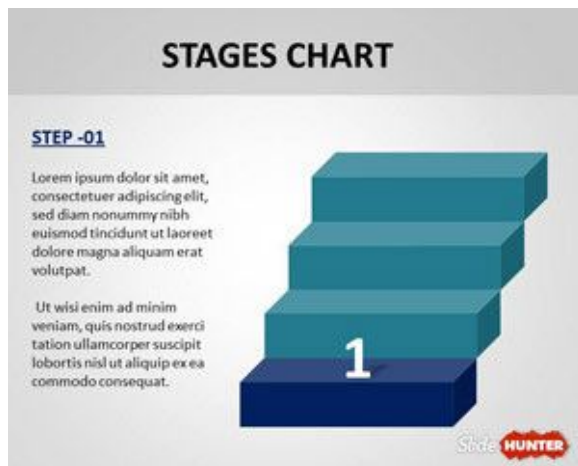
Independent Guarantee fraud shall be found by a People's Court under one of the following circumstances:

- (1) The Beneficiary, acting in collusion with the Guarantee Applicant or any other party, has fabricated the underlying transaction;
- (2) Any of the third-party documents presented by the Beneficiary is forged or contains false information;
- (3) Any court judgment or arbitral award finds that the party obligated on the underlying transaction shall not be liable for payment or damages;
- (4) The Beneficiary acknowledges that the obligations under the underlying transaction have been fully discharged or that the payment triggering event specified in the Independent Guarantee has not occurred; or
- (5) The Beneficiary otherwise knowingly abuses its right to demand payment when it has no such right.

- **Independent Guarantee Fraud**
- **Unremarkable: collusion, falsified documents or forgery, award on underlying transaction: applicant not liable**
- **payment triggering event not occurred.**
- **Abusive demand when no such right**



# The Stages of an Independent Guarantee Fraud Dispute



1. PETITION FOR SUSPENSION ORDER
2. RECONSIDERATION
3. TRIAL
4. PERMANENT ORDER
5. APPEAL

# Article 13: Petition for Suspension of Payment

The Applicant, the Issuer, or the Instructing Party of the Independent Guarantee may, prior to or during the court litigation or arbitral procedure, file a petition with a People's Court of the Issuer's domicile or any other People's Court with competent jurisdiction over the Independent Guarantee fraud dispute to suspend the payment under the Independent Guarantee in the event they find out that any of the circumstances provided in Article 12 [Fraud] has occurred.

- **Who? Applicant, Issuer, Instructing Party**
- **Where? Issuer's domicile or court with jurisdiction**
- **Prior to or during litigation**
- **Any circumstance in Article 12**





# Article 14: Suspension of Payment

A People's Court shall issue a ruling suspending payment under an Independent Guarantee, provided all the following conditions are met:

- (1) The evidence filed by the petitioner for payment suspension supports a high probability of existence of any of the circumstances provided in Article 12 [Fraud];
- (2) It is under such urgent circumstances that the petitioner's lawful rights and interests will suffer irreparable damage if payment is not suspended; and
- (3) The petitioner has provided security sufficient to cover the damage probably caused by the payment suspension to the party(ies) against whom the application is made.

A petitioner's application for payment suspension on the ground of the Beneficiary's breach of contract in the underlying transaction shall not be supported by a People's Court.

Where the Issuer has paid in good faith under the Independent Guarantee which has been issued upon instructions of the Instructing Party, a People's Court shall not suspend the payment under another Independent Guarantee whose purpose is to secure the Issuer's right to reimbursement.



# Restatement of Article 14

## ▶ Conditions for suspension:

- ▶ Evidence supports probability of Independent Guarantee Fraud
- ▶ Petitioner will suffer irreparable damage unless granted
- ▶ Sufficient security

## ▶ NOT based on breach of underlying contract

## ▶ Good Faith/Innocent party exception recognised: Counter Guarantor

### Comments on Article 14

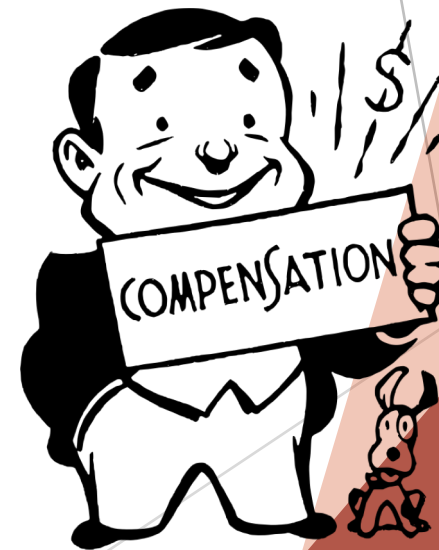
- No duty to not pay
- Issuer can petition or refuse to pay
- Broader than PRC LC Rules



# Article 15: Compensation for Wrongful Petition

A party's claim for compensation for losses caused by the wrongful petition for suspension of payment against the petitioner shall be supported by a People's Court.

- ▶ “Party”: Beneficiary/ Issuer /Local Bank



# Article 16: Payment Suspension Order

A People's Court shall rule in writing within forty-eight hours upon its receipt of the petition for suspension of payment. The ruling shall state the petitioner, the party against whom the petition is made, and any third party affected, the facts a People's Court preliminarily found, and the ground(s) on which the petition for payment suspension is granted or rejected.

A ruling granting the payment suspension shall be enforced immediately.

In relation to an Independent Guarantee fraud dispute, if the petitioner fails to initiate court litigation or an arbitration proceeding in accordance with the law within thirty days after the ruling for the payment suspension, a People's Court shall revoke the ruling.

# Restatement of Article 16: Payment Suspension Order

- **Upon receiving a Petition for Suspension of Payment, Court MUST:**
  - **Rule in writing within 48 hours of receipt by Court.**
  - **The Ruling must state:**
    - **The Parties, including any Third Parties involved**
    - **The facts and grounds for rejection/award**
- **Order has IMMEDIATE effect**
- **Party obtaining suspension must initiate legal proceedings within 30 days or order revoked**

## Comments

- Time: Binds Petitioner but not Court (unrealistic)
- Effect
- Legal Proceedings MUST be initiated (if not already)

# Article 17: Reconsideration of Suspension Order

Where any party objects to the ruling rendered by a People's Court regarding the petition to suspend the payment, that party may, within ten days after the ruling is served on it, apply to the same People's Court for reconsideration. During the reconsideration period, the enforcement of the ruling shall not be halted.

The People's Court concerned shall reconsider the case and query the parties within ten (10) days after receiving the review petition.

## Comments

- **Same court: Value?**
- **Not appeal**
- **Optional**
- **Timing: Ten Days**
- **Enforcement not halted**



## Article 20: Where Fraud Found

After hearing a case on an Independent Guarantee fraud dispute, if a People's Court **finds beyond reasonable doubt** that there is Independent Guarantee fraud, and that the circumstances provided in the third paragraph of Article 14 [Suspension of Payment] have not occurred, **it shall enter a judgment terminating the payment obligation of the Issuer under the Independent Guarantee.**

### Comments

- Standard: beyond reasonable doubt
- 3<sup>rd</sup> Paragraph of Article 14: No good faith payment by Local Bank
- Termination per Article 11(5)



**FRAUD  
ALERT**

# Miscellaneous Issues

**Application of the Independent  
Guarantee Provisions to Counter  
Undertakings and their Impact on  
Chinese and Foreign Counter  
Guarantees and Local Guarantees,  
Local Beneficiaries, and Applicants  
and Instructing Parties**



# Article 21:¶ 1: Jurisdiction

A People's Court of the Issuer's domicile or of the defendant's domicile shall have jurisdiction over disputes between the Beneficiary and the Issuer in relation to an Independent Guarantee, unless the Independent Guarantee states that such dispute should be submitted to jurisdiction of any other court or for arbitration. Any party's claim for court jurisdiction or arbitration as a result of application of the dispute resolution clause stipulated in underlying transaction shall not be supported by a People's Court.

## Comments

- General disputes (not Independent Guarantee Fraud)



# Article 21:¶ 2: Jurisdiction

A People's Court of the domicile of the Issuer of the Independent Guarantee, under which the payment is requested to be suspended, or of the defendant's domicile, shall have jurisdiction over the Independent Guarantee fraud dispute, unless the parties agree in writing that such dispute should be submitted to jurisdiction of any other court or for arbitration. Any party's claim for court jurisdiction or arbitration as a result of application of the dispute resolution clause contained in the underlying transaction or the Independent Guarantee shall not be supported by a People's Court.

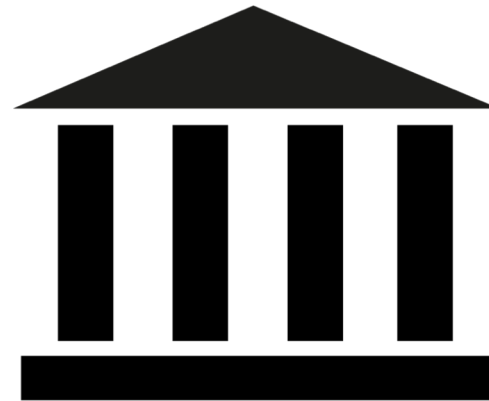
## Comments

- General disputes (not Independent Guarantee Fraud)



# Article 21: Jurisdiction

- **People's Court of Issuer's domicile or defendant's domicile has jurisdiction for disputes between Issuer and Beneficiary unless guarantee states another jurisdiction or requires arbitration**
- **In fraud cases, the People's Court of Issuer's domicile or defendant's domicile has jurisdiction unless parties agree in writing to another jurisdiction**
- **Courts will not enforce any claim for jurisdiction or arbitration based on the application of the dispute resolution clause contained in the underlying transaction**



# Article 22:¶ 1: Choice of Law

Where no governing law is specified in a foreign-related Independent Guarantee, and the Issuer and the Beneficiary fail to reach consensus on the governing law prior to conclusion of court arguments in the trial proceedings, the dispute between the Issuer and the Beneficiary shall be governed by the law of the Issuer's habitual residence; and where an Independent Guarantee is issued by a legally registered branch of a financial institution, the law of the branch's registration place shall govern.



## Comments

- General Disputes (not Independent Guarantee Fraud)

## Article 22:¶ 2: Choice of Law

In relation to disputes of foreign-related Independent Guarantee fraud, if the parties fail to reach consensus on the governing law, the law of the habitual residence of the Issuer of the Independent Guarantee, under which the payment is requested to be suspended, shall govern. Where an Independent Guarantee is issued by a legally registered branch of a financial institution, the law of the branch's registration place shall govern. Where the parties have the same habitual residence, the law of such habitual residence shall govern.

