

Exploration of Issues Related to Confiscation of Illegal Gains in Foreign Exchange Administrative Penalties

Yuqing Wang

Dalian Ocean University, Dalian, Liaoning, 116023, China

Keywords: Foreign exchange; administrative penalties; illegal gains

Abstract: The determination and disposal of confiscated illegal gains have always been controversial in the field of administrative punishment. The new *Administrative Punishment Law* continues to regard the confiscation of illegal gains as a type of administrative punishment, affirming its connotation of recovering unjust enrichment, punishment and education for the violating parties. The provision that illegal gains shall be confiscated in addition to restitution in accordance with the law puts forward new requirements for administrative penalties in foreign exchange management, which is worth exploring and pondering.

1. Introduction

1.1 The provisions on illegal gains in the new *Administrative Punishment Law*

Article 28, Clause 2 of the new *Administrative Punishment Law* stipulates: “If the party involved has obtained illegal gains, in addition to the restitution required by law, the gains shall be confiscated. Illegal gains refer to the funds obtained through the commission of illegal acts. If there are other provisions regarding the calculation of illegal gains in laws, administrative regulations, or departmental rules, those provisions shall be followed.”^[1]

This provision has several implications. **Firstly**, it expands the scope of applying the administrative punishment of confiscating illegal gains, further emphasizing the principle that “no one should benefit from their illegal acts”. Regardless of whether relevant regulations have been issued by various administrative management departments, the confiscation of illegal gains can be carried out based on the new *Administrative Punishment Law*. **Secondly**, it clarifies the concept of illegal gains, which refers to the funds obtained through the commission of illegal acts. However, there is a debate in the theoretical field regarding whether this refers to the full amount of illegal gains or the difference after deducting costs. The theoretical consensus tends to include the entire amount of illegal gains. Different practices can be observed in law enforcement, so the provision also emphasizes that laws, administrative regulations, and departmental rules may specify the calculation method of illegal gains separately. **Thirdly**, it emphasizes the “restitution procedure” as a prerequisite for confiscation. This is in line with the provisions in the *Civil Code* that state, “If a civil subject should bear civil liability, administrative liability, and criminal liability for the same act, assuming administrative or criminal liability does not absolve them from civil liability. If the civil subject’s property is insufficient to cover the liabilities, it should be prioritized for fulfilling civil

liabilities.”^[2]

1.2 Three theories in the domestic academic community

First, there is a “Full Amount Recognition Theory”, which considers all income obtained by individuals engaged in illegal activities as illicit gains.^[3] This theory argues that all income derived from illegal activities should be confiscated because the costs incurred by the party involved in the illegal acts can be reproached, and the concept of illegal gains inherently implies the entirety of the unlawfully acquired income. **Second**, there is a “Partial Amount Recognition Theory”, which posits that costs incurred by the party involved in the illegal acts should be considered as their legitimate property and not subject to confiscation since they are not illicit gains.^[4] **Third**, there is a “Compromise Theory”, which suggests that the determination of illegal gains should be based on a case-by-case analysis, taking into account the specific circumstances of each case. This theory advocates for an individualized approach rather than adhering strictly to either the “Full Amount Recognition Theory” or the “Partial Amount Recognition Theory” to determine the confiscation of illegal gains.^[5]

1.3 Basic principles for determining illegal gains in foreign exchange management

The Reference Standards for Determining “Illegal Gains” in Foreign Exchange Administrative Penalties comprehensively outlines the concept of illegal gains in foreign exchange violations, clarifying the principles and calculation standards for determining illegal gains. It provides important guidance for law enforcement practices in the determination of illegal gains from foreign exchange violations.^[6] **First**, it further clarifies the scope and principles for the confiscation of illegal gains in foreign exchange violations. The determination of whether there are illegal gains in various foreign exchange violation cases should be based on the actual benefits and available evidence.^[7] **Second**, it further specifies the types and calculation methods of illegal gains in foreign exchange cases. It points out that illegal gains from foreign exchange violations include, but are not limited to, exchange rate differentials, exchange income, investment and financial management, loans, interest income, and commission income—six major categories. However, the calculation of illegal gains requires a legal framework and higher-level legal systems to be established, and currently, there is no effective basis for calculating illegal gains in the field of foreign exchange management from a systemic perspective.^[8]

2. Issues to Consider in the Determination and Disposal of Illegal Gains in Foreign Exchange Administrative Penalties

2.1 Insufficient attention to illegal gains from violations without specified confiscation measures

The new *Administrative Punishment Law* has explicitly stated that all illegal gains should be confiscated. Articles 37 to 43 of the *Foreign Exchange Regulations* do not specifically stipulate the confiscation of illegal gains in cases involving violations.^[9] However, offenses such as capital flight, illegal inflow of funds, unauthorized carrying of foreign exchange in and out of the country, illegal exchange transactions, and violations of foreign exchange operations may all result in illegal gains.^[10] Currently, law enforcement practices do not pay sufficient attention to whether the above violations involve illegal gains. During the process of law enforcement inspections and investigations, there is a tendency to focus on collecting qualitative and quantitative evidence, while there is little targeted investigation and collection of evidence regarding the determination of illegal

gains and related facts.^[11]

2.2 The determination of illegal gains in cases of illegal foreign exchange trading and disguised foreign exchange transactions may not align with the actual gains obtained by the parties involved

The primary form of violation in illegal foreign exchange transactions is one-way illegal purchase of foreign exchange, which often involves the payment and utilization of the purchased foreign exchange at the time of the offense. In such cases, using the mid-rate of the People's Bank of China and the date of the offense as the basis for determining illegal gains may result in a discrepancy with the actual gains obtained by the parties involved. Furthermore, currently, there are no regulations or higher-level legal documents in the field of foreign exchange management that provide specific guidelines for calculating illegal gains.^[12]

2.3 The determination of illegal gains in foreign exchange violations involving operational activities lacks reference standards

Currently, in the field of foreign exchange management, several foreign exchange violations involve operational activities. However, there is a lack of unified standards for deducting the operational costs associated with these violations. Unauthorized changes in the purpose of foreign exchange or capital, unauthorized operation of foreign exchange settlement, sale of foreign exchange business, or other foreign exchange business beyond settlement and sale, illegal foreign exchange trading, disguised foreign exchange transactions, and violations by financial institutions can all involve operational activities.^[13] Based on the general principles of determining illegal gains and current law enforcement practices, the costs incurred as a result of unauthorized operation of foreign exchange business, changes in capital purposes, and similar violations can be deducted from confiscated illegal gains if there is evidence to support them.^[14] However, the operational costs associated with certain violations by financial institutions and the operational costs involved in underground money laundering related to illegal foreign exchange trading are rarely taken into consideration due to the difficulty in calculation. Overall, this leads to inconsistent standards for deducting similar operational costs associated with different types of violations.^[15]

2.4 The method to handle illegal gains of entities that should not be subject to punishment

In the context where all illegal gains should be confiscated, there is a legal conflict regarding the disposition of illegal gains obtained by individuals under the age of 14 who are engaged in foreign exchange violations under the employment of others. According to the new *Administrative Punishment Law* and the *Measures of the State Administration of Foreign Exchange for Administrative Penalties*, individuals under the age of 14 who commit foreign exchange violations should not be punished. However, confiscation of illegal gains is considered a form of administrative penalty, and there is a lack of clear provisions regarding whether illegal gains should be confiscated in such cases.

3. Countermeasures for Determination and Disposal of Illegal Gains in Foreign Exchange Administrative Penalties

3.1 Enhance law enforcement standardization, determine illegal gains for all foreign exchange violations

Firstly, it is necessary to promptly clarify the principles for determining illegal gains and establish standards for income determination at the departmental regulatory level. This should be done while considering fairness and efficiency, and to prevent different law enforcement authorities from adopting different methods for determining illegal gains for the same violation.^[16] From a theoretical perspective, since foreign exchange violations primarily involve fund flows and settlements, including the principal in the calculation of illegal gains would result in a significant disparity with the actual gains obtained by the parties involved. Therefore, using total income as the standard is not suitable.^[17] Adopting a case-by-case analysis approach would likely lead to inconsistent methods and amounts of illegal gains calculation for similar cases, which would impede fair and just administrative penalties.^[18] The “pure profit theory”, which deducts costs in a detailed manner, poses significant challenges in law enforcement practice. Thus, it is necessary to determine standards from the perspective of foreign exchange management that balance fairness, efficiency, and are conducive to law enforcement practice. **Secondly**, before the regulations are issued, it is important to further remind each branch to fully implement the requirements of the new *Administrative Punishment Law* in law enforcement practice. Specifically, for various foreign exchange violations stipulated in the *Foreign Exchange Regulations*, whether there are illegal gains should be determined during the inspection and investigation process. While collecting qualitative and quantitative evidence, attention should be given to the collection and acquisition of evidence related to illegal gains. Template modification for notices and decisions should explicitly include the determination of whether there are illegal gains as an element of the violation.^[19]

3.2 The calculation and determination of illegal gains for specific violations can be considered separately

Since 2023, the penalties imposed by the foreign exchange authorities on individuals involved in foreign exchange violations have mostly targeted underground money market counterparts. The violations committed by these counterparts mainly involve one-way illegal purchases of foreign exchange, with the majority of the funds already spent abroad. It is difficult to determine the illegal gains for such behavior, and the standards are hard to establish as individuals engaged in one-way illegal purchases of foreign exchange generally do not have profit as their primary objective.^[20] Furthermore, the *Foreign Exchange Regulations* do not have specific provisions for confiscating illegal gains as a separate punishment; confiscation of illegal gains is implemented in conjunction with fines and other penalties. Therefore, the core function of confiscating illegal gains in the field of foreign exchange management should be to prevent individuals from benefiting from their illegal gains. In cases where individuals have engaged in one-way purchase of foreign exchange and have already spent the funds, the amount of profit is generally small, and imposing fines can serve the purposes of preventing the individuals from benefiting, as well as providing punishment and education. From the perspective of actual gains, availability of evidence, and law enforcement costs, it is suggested that for such foreign exchange violations, unless there is specific and explicit evidence, there is no need to collect additional evidence of illegal gains. The calculation should not be based on the interest differential between illegal and legitimate channels, but rather directly determined as no illegal gains found.^[21]

3.3 Further standardization can be achieved regarding the content and criteria for deducting operating costs

The calculation methods and standards for illegal gains in the same field and under the same regulatory framework may differ due to variations in the specific violation's revenue generation methods.^[22] However, there should not be differential treatment at the initial design of the system regarding whether to deduct the same category of violation costs. In the context of foreign exchange management, for violations such as unauthorized operation of foreign exchange business without approval or unauthorized use of funds for operations, the calculation of illegal gains should deduct operating costs as part of the revenue calculation. Similarly, for financial institutions involved in illegal foreign exchange transactions, their illegal gains should be calculated after deducting operating costs, rather than simply adding up commissions and fees. For underground money market activities involving illegal buying and selling of foreign exchange, the illegal gains are not solely based on the difference in buying and selling prices but may also involve unauthorized operating costs. From a practical and fair law enforcement perspective, it is recommended that the calculation of illegal gains for revenue-generating foreign exchange violations should only consider the deduction of costs from a capital perspective, with the amount of the illegal funds in foreign exchange violations serving as the cost to be deducted. For illegal gains related to service fees, commissions, and other service-related revenues, the amount of the fees should be considered as the illegal gains.^[23]

3.4 Achieve the objective of eliminating benefits derived from illegal actions through civil restitution for the illegal gains obtained by of entities that should not be subject to punishment

From the perspective of foreign exchange management practices, it is less likely for minors to directly engage in foreign exchange violations. However, there may be cases where they are employed to carry out such violations, resulting in them benefiting from these illegal actions. The principle of not allowing individuals to benefit from illegal actions is fundamental, but there are ways other than confiscating illegal gains to achieve this goal. The remuneration received by minors for participating in foreign exchange violations can be returned to the employer through restitution. Following this logic, it can also ensure the accuracy and reasonableness of the determination of the amount of illegal gains confiscated from the individual involved in the foreign exchange violation.^[24]

In the field of foreign exchange, violations involve a wide range of illegal gains with diverse forms, making it difficult to establish unified and detailed standards for calculating illegal gains. Currently, the first step should be to determine whether all violations have resulted in illegal gains as a factual determination during the enforcement and investigation process. Secondly, it is necessary to issue departmental regulations or revise the *Foreign Exchange Regulations* to clarify the principles for calculating illegal gains from foreign exchange violations. For objectively existing illegal gains that cannot be determined, consideration should be given to discretionary fines and amounts. Based on this, specific provisions should be made for calculating illegal gains for certain violations, taking into account enforcement costs, operational difficulties, and other aspects, in order to ensure fairness while maintaining enforcement efficiency.^[25]

4. Conclusion

This paper focuses on the research on confiscating illegal gains and provides a comprehensive analysis from four aspects: the conceptual definition of confiscation of illegal gains, legislative status quo, issues in the application of administrative penalties in foreign exchange, and

improvement strategies and recommendations. Starting with the analysis of legal principles, it clarifies the legal definition of confiscating illegal gains in foreign exchange administrative penalties, which refers to the monetary proceeds generated from illegal activities and is considered a burdensome administrative action.^[26] By addressing the issues at hand, it examines the current legislative status and problems faced in the application of confiscation of illegal gains in foreign exchange administrative penalties, highlighting the shortcomings of the system in terms of regulatory compliance and legal application. With a problem-solving approach, it proposes several considerations to improve the system of confiscating illegal gains in foreign exchange administrative penalties. Firstly, it suggests enhancing the uniformity of relevant laws and regulations to further standardize law enforcement practices. Secondly, it recommends considering specific calculation methods for illegal gains in certain violations. Thirdly, it advocates for a more unified approach to deducting operating costs and defining standards. Lastly, it proposes achieving the objective of eliminating benefits derived from illegal actions by implementing civil restitution for the illegal gains obtained by entities that should not be subject to punishment.

In summary, the confiscation of illegal gains is widely applied in the field of foreign exchange administration in China. How to determine the illegal gains in foreign exchange administrative penalties is not only an urgent issue that requires procedural, standardized, and institutionalized implementation, but also a complex and significant challenge that needs to be addressed. This paper provides a limited and preliminary research contribution to the study of confiscating illegal gains in foreign exchange administration, with the hope of filling a small part of the research gap in this area and contributing to the unity and seriousness of China's administrative legal system.

References

- [1] Ying, S., & Jiang, M. (2020). *Administrative Law and Administrative Litigation Law (2nd ed.)*. Beijing: Higher Education Press.
- [2] Yan, S. (2016). *Administrative Penalty Practice and Precedent Interpretation*. Beijing: Law Press
- [3] Chen, Q. (2016). *Administrative Penalty Law*. Beijing: Law Press.
- [4] Ma, H. (2018). *Research on Frontier Issues in Administrative Law*. Beijing: China University of Political Science and Law Press.
- [5] Wu, L. (2015). A Legal Analysis and Regulatory Proposal for the Nature of China's Foreign Exchange Reserves. *Journal of Zhengzhou University of Light Industry (Social Science Edition)*, (5): 34-39.
- [6] Xiao, J. (2017). Current Situation and Countermeasures of China's Foreign Exchange Reserves. *China International Finance (Chinese-English)*, (18): 6-7.
- [7] Xue, Z. (2017). The "Go Global" Strategy and the Exploration of China's Foreign Exchange Management System. *China International Finance (Chinese-English)*, (24): 178.
- [8] Zhang, D. (2019). Research on China's Foreign Exchange Management System Reform. *Beijing Financial Review*, (1): 43-49.
- [9] Zhu, M. (2016). Effective Management of China's Foreign Exchange Reserves: Macro Strategies and Micro Measures. *Financial Think Tank*, (3): 38-66.
- [10] Cao, H., & Wu, H. (2021). Research on the Approach to Granting Administrative Penalty Power to Townships (Sub-districts). *Special Zone Practice and Theory*, (1).
- [11] Zhang, M. (2016). *Criminal Law (5th ed.)*. Beijing: Law Press.
- [12] Yan, L. (2021). Judgment Rules and Legal Effects of Confiscating Illegal Gains. *Journal of Public Security (Zhejiang Police College)*, (03).
- [13] Shi, G. (2020). Legal Guidelines for Dealing with 7 Types of Market Violations during Epidemic Prevention and Control. *China Quality Supervision and Management*, (02).
- [14] Leng, F. (2017). The Nature and Confiscatable Illegal Costs of Confiscating Illegal Gains. *Journal of Three Gorges University (Humanities and Social Sciences Edition)*, 39(S2).
- [15] Wang, G. (2020). On the Sanctioning Nature of Administrative Penalties. *Legal and Business Research*, (6).
- [16] Chen, S. (2020). Legalization of Administrative Penalty Subjects. *Zhejiang Social Sciences*, (11).
- [17] Ying, S., & Feng, J. (2021). Dilemmas and Solutions of Administrative Fines System. *Quest*, (1).
- [18] Jiang, M. (2019). *Administrative Law and Administrative Litigation Law (7th ed.)*. Beijing: Peking University

Press.

[19] Zhou, Y. (2005). *Original Theory of Administrative Law (2nd ed.)*. Beijing: China Fangzheng Publishing House.

[20] Zhang, S. (2005). *Administrative Law*. Beijing: Peking University Press.

[21] Zhang, W. (2011). *Jurisprudence*. Beijing: Higher Education Press & Peking University Press.

[22] Huang, H. (2020). *Redefinition and Classification of Administrative Penalties*. *East China University of Political Science and Law Journal*, 23(4): 31-43.

[23] Xiong, Z. (2020). *Diversification and Prevention and Control of Administrative Penalties—On the Proposed Amendment to Article 8 of China's Administrative Penalty Law*. *Politics and Law*, (03): 77-93.

[24] Wang, G. (2020). *On the Sanctioning Nature of Administrative Penalties*. *Legal and Business Research*, 37(6): 19-32.

[25] Wang, Q. (2019). *Confiscation of Illegal Gains in Administrative Law*. *Law Review*, 37(6): 160-170.

[26] Li, H. (2020). *On the Improvement of China's Administrative Penalty System—Comments on the Revised Draft of the Administrative Penalty Law of the People's Republic of China*. *Legal and Business Research*, (6).