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Coordination Logic of Cross-border Financial Risk Prevention and Transaction Contract Allocation Within the Financial Regulation Framework

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Abstract

During the process of cross-border financial opening, the provision of risk prevention and control systems encounters a core challenge.: how to integrate regulatory rules of a public law nature with transaction contracts of a private law nature. The two sides of this paper are financial regulation and contract allocation, and their coordination logic for risk prevention and control will be examined. China has built a "dual-regulation system of macro-prudential and micro-regulation" for cross-border finance. The systems for bank foreign exchange risk transaction reporting and non-centralised clearing derivative margin management have moved risk monitoring upstream to the transaction stage. The standardised master agreements of ISDA and NAFMII incorporate regulatory requirements into private law relations via provisions such as terminating net settlement and margin arrangements, forming a micro-contract basis for risk prevention and control. The three ways that regulatory rules are translated into contract provisions are legal embedding, indirect effect and format recognition. Both are two-way interactions at the level of institutional goals, risk identification and performance guarantee: regulation defines the scope of compliance, and contracts offer a market-oriented implementation path. Strengthen the prevention and control system for cross-border financial risks, and at the same time, regulate flexibly in terms of contract risk allocation to promote effective coordination between public law regulations and the autonomy of private law.

Keywords

Cross-border finance; risk prevention and control; financial supervision; transaction contract; coordination logic.

1. Introduction

Cross-border financial activities refer to the cross-border flow of capital, credit and risk. The head of the foreign-currency risk management department will be responsible for risk control, supervision and promotion of development. The promotion of cross-border trade and investment has been continuously advanced. However, the features of financial risk include suddenness in transmission, speed of spread and wide reach. The macro-policies of the major economies have had a deeper spillover effect. New Technology and Artificial Intelligence are Changing the Form of Financial Activities. Pressure is mounting for the old regulatory model [1].

The institutional logics of the regulatory rules and transaction contracts are not the same. Regulation is a subject of public law that imposes external restrictions through administrative power, and cross-border financial transactions use the tool of private law contracts based on the principle of autonomy of will and contractual performance. Regulation aims for the stability of the system and the public interest; contracts aim to maximise the interests of the parties through transaction efficiency. An effective coordination mechanism needs to be established

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between the two sides to turn regulatory requirements into behavioural constraints for the contracting parties, and a contract mechanism can be set up as an institutional channel to achieve the goal of regulation in cross-border financial governance.

Recently, the combination of China's cross-border financial regulatory system and the system of transaction contracts has gradually become more prominent. The monitoring system for banks' foreign exchange risk transactions and regulations on non-centralised clearing of derivative transactions will directly affect the contract arrangements between financial institutions and counterparties. The International Swaps and Derivatives Association (ISDA) master agreement and the NAFMII master agreement have included compliance obligations and margin arrangements in the clause design. Coordinating logic that is not in the traditional "command-obedience" mode has begun to appear in the regulatory system and contract design.

This article explains the internal mechanism of this coordination logic, lists the main types of cross-border financial risks and the basic structure of the regulatory system, analyzes the institutional function of transaction contracts in risk prevention and control, studies the path by which regulatory rules are turned into contract clauses, and thus shows the two-way interactive coordination logic and puts forward improvement suggestions.

2. Main Types of Cross-border Financial Risks and the Basic Structure of the Regulatory Framework

The three kinds of cross-border financial risk are classified according to the source and transmission path. The first is cross-border capital flow risk, and in the form of "hot money", short-term capital flows frequently enter and leave financial markets, affecting the stability of the exchange rate [2]. The second is foreign exchange violation risk, which includes false trade and false investment and financing, underground banks, cross-border gambling, fraud in export tax rebates, illegal cross-border financial activities involving virtual currencies, etc. The third is derivatives trading risk; as over-the-counter derivatives are leveraged and cross-border, they can also spread systemic shocks.

Given the above risks, China has set up an all-weather regulatory system. The People's Bank of China and the State Administration of Foreign Exchange carry out comprehensive macro-prudential management of cross-border financing at the macro level. Modify parameters to link the scale of cross-border financing with economic growth, debt-repayment ability and international balance of payments. In January 2025, the macro-prudential adjustment parameter was increased from 1.5 to 1.75, and the upper bound for the weighted balance of cross-border financing risks of financial institutions was adjusted accordingly [3]. At the micro level, the risk management department of the foreign-currency risk has introduced a risk-based regulation concept and now requires banks to build a monitoring system for foreign-currency risk transactions. The Measures for the Reporting of Bank Foreign Exchange Risk Transactions (Trial) have four chapters and 23 articles. Banks should set their own monitoring standards, carry out monitoring and analysis, and report risk transaction information to the State Administration of Foreign Exchange to raise the risk identification threshold to the level of transactions.

The Regulatory Authorities work together in a multi-departmental way. The People's Bank of China will take the lead in all areas of macro-prudential and monetary policy coordination; the Foreign Exchange Administration Bureau will regulate cross-border capital flows and supervise the foreign exchange market; and the National Financial Regulatory Administration (NFRA) will provide behavioural supervision and risk disposal. Eight departments have jointly organised a campaign to address illegal cross-border securities, futures and fund management activities, and the implementation plan has been released. At the Lujiazui Forum in June 2026, NFRA Director Ding Xiangqun of the National Financial Regulatory Administration (NFRA)

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proposed strengthening coordination among central and local governments and departments, closing regulatory loopholes, and ensuring full coverage without exceptions.

The main content of the above arrangement is an integrated system of "macro-prudential and micro-supervision". Macro-prudential policy uses counter-cyclical measures to curb excessive fluctuations in cross-border capital flows and addresses systemic risk; micro-supervision monitors the compliance of institutional operations and risk behaviour, and sets daily limits. The two together will build a regulatory system for preventing and controlling cross-border financial risks, and also provide an external constraint on the inclusion of transaction contracts in this system.

3. The Institutional Function of Transaction Contracts in Cross-border Financial Risk Prevention and Control

The Legal Basis for cross-border financial transactions is a contract. Loans and guarantees across borders, derivative transactions, securities investments, etc., all have their own rights and obligations for the parties involved under the contract. In terms of risk prevention and control, a transaction contract will also specify the conditions of the transaction and take on institutional functions for risk identification, allocation and mitigation.

A typical master agreement will be employed to manage the risk of cross-border transactions. The ISDA master agreement is widely used by market participants in all countries, and the definition of a default event, close-out netting and credit support arrangements jointly form the credit risk management system [4]. Close-out netting can be used to close out all outstanding transactions prematurely in the event of a default, calculate a net payable amount, and reduce exposure to default. The foundation for derivatives transactions in the interbank market in China is the NAFMII Master Agreement. The National Association of Financial Market Institutional Investors (NAFMII) has published the Master Agreement for Financial Derivatives Transactions in the China Inter-bank Market (Cross-border Edition - 2022 Edition) (i.e., the NAFMII cross-border version master agreement). Standardised contracts have a unified design for the terms and, thus, reduce information asymmetry to some extent; they provide an operational contractual basis for risk identification and measurement.

The provisions of the contract will also serve to realise the objectives of regulation. Margin Management Measures released by the National Financial Regulatory Administration (NFRA) require regulated financial institutions to meet the standards for variation margin and initial margin within a specific time [5]. The above administrative orders need to be implemented via the credit support annex of the ISDA master agreement or relevant clauses in the NAFMII master agreement. The two parties to the contract agree on the margin calculation method, eligible collateral and delivery arrangements in the annex, and convert the regulatory standards into contractual provisions. Therefore, the contract will serve as the implementation platform for the regulatory provisions.

Risk allocation in a contract and risk prevention and control by regulation work together to the extent that is convenient. Regulation uses external coercion as the means of constraint, and the contract is based on the obligations of the parties. Add the regulatory requirements to the contract, and any behaviour that violates these regulations will also be considered a breach of contract. Regulatory Penalties and Contractual Remedies are a Dual Constraint. In accordance with the foreign exchange management regulations, if the guarantor is a non-bank financial institution, it must complete the registration of the internal guarantee for external loans within 15 working days after signing the contract, and keep-well agreements that are in substance guarantees are also subject to this requirement. The above regulations will make the actual contents of the contract the subject of regulatory review, and the requirements for registration will also be included in contract performance.

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4. The Mechanism for Converting Regulatory Rules into Transaction Contract Terms

The connection between regulatory rules and transaction contract provisions is not automatic; institutional design and practical adaptation are required for this link [6]. In short, this change aims to incorporate administrative requirements into private law relations by way of the autonomy of will. In recent years, China's regulatory practices have provided some observation cases, from which three mechanisms can be extracted.

First, fixed embeddings are used. The regulatory rules directly require the inclusion of certain provisions in the contract or the undertaking of some procedures. The "Measures for the Administration of Foreign Exchange Risk Transactions by Banks (Trial)" is a typical example. Therefore, the bank will build a monitoring system and file reports. Banks can only add the obligation to collect information in the account opening agreement and trade confirmation; otherwise, they will not obtain the data authorisation required for regulatory reporting. The registration requirements for cross-border guarantees are the same; even if registration does not automatically void the contract, it may lead to administrative penalties and performance difficulties, and only then can the parties include an obligation to register in the contract. Based on the above analysis, the main content of the contract will be determined by regulations, and there will be little room for negotiation.

The second is a weak instruction. Regulatory rules change the transaction costs or legal consequences for the parties involved, and thus they enter into contracts in pursuit of the aims of regulation [7]. The supervision of margin regulation for non-centralised clearing of derivatives transactions is a typical case. The regulatory rules only set the lower bounds, and the particular terms were agreed upon by the trading parties in the credit support annex. Institutions that do not meet the conditions will have a higher cost of capitalisation. In this way, the authorities will set the rules; they will not reduce the options in contract construction.

The third way is format recognition. Regulatory authorities have approved some form contracts or provided model texts to guide the market in using standardised risk prevention and control clauses. Foreign institutional investors will be subject to regulatory approval for the NAFMII master agreement and thus have a lower compliance risk. Standardised contracts are thus institutions that link regulation and the market.

The three ways are in harmony and together form a full-featured channel for introducing regulatory rules into the contractual relationship. The first method works well if the regulations are specific and enforceable, and if the terms of the contract are clear and legally binding. Change is not always easy; there are many unclear regulations and therefore no contract; there are also too many rigid provisions that cannot adapt to changes in policy. As a result, the link between the regulatory system and contract design will be even more convoluted.

5. The Two-Way Interaction Logic Between the Regulatory Framework and Contract Configuration

The transformation of regulatory rules into contract clauses is a one-way top-down imposition. In practice, the connection between the regulatory system and contract Design is not limited to the above. There is also a two-way interactive coordination logic that can be understood at three levels [8].

The first is the target connection. The regulatory system addresses systemic risk prevention and control, and the core of contract design is the division of transaction risk and the guarantee of contract execution. The two systems connect at "risk prevention and control". Regulation should use the private law system of contracts to constrain transaction behaviour, and contracts themselves need to ensure effectiveness within the regulatory system. The People's

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Bank of China, the State Administration of Foreign Exchange and other departments have issued the "Action Plan for Developing Offshore Finance in Shanghai International Financial Centre", which proposes the principle of "one-line liberalization, one-line control, transaction traceability, and risk prevention and controllability". "Control" and "controllable" refer to the regulatory boundary, and "transaction traceability" is achieved through contracts and trade confirmations. Regulation does not replace transactions but conducts management through traceability penetration.

Mechanism Integration is the second level. The mechanism for regulation issues relates to the problems of regulatory entry into contracts and whether the contract system induces regulatory change via bidirectional connections. After a few other parties have adopted these contract provisions, the regulatory authorities will add them to the rules. The widely used close-out netting provision in the ISDA master agreement is now recognised by regulators as reducing the risk and lowering capital requirements for the capital adequacy ratio calculation. Many central banks around the world have used the NAFMII master agreement in the interbank market to improve the quality of data for derivative reporting. Contract configuration is no longer passive instruction-following but provides feedback to the regulator during operation.

Mutual reinforcement of legal effect is the third kind. The two types of restraints are regulatory sanctions and contract violations; if market subjects fail to meet regulatory requirements, they may be subject to administrative penalties and civil liability for breach of contract, or even have their contracts deemed invalid due to conflict with laws and regulations. Although unregistered guarantee contracts are not necessarily void in cross-border guarantee practice, the foreign exchange administration may not process external payments; thus, the main purpose of the contract fails to be realized and the counterparty can claim remedies for breach of contract. The combination of the three levels can construct a more elaborate network of the regulatory system and contract structure [9].

6. Realistic Tensions in Coordination Logic and Institutional Improvement

The above coordination logic is, in theory, a relatively closed institutional loop. However, when considering the situation in practice, some of the tensions have not been addressed to this day.

First of all, the regulatory policy cannot be altered, so the terms of the contract will not change. In January 2025, the macroprudential adjustment parameter for cross-border financing was increased, and thus the upper limit on financing amount was reduced. As a result, some of the existing contracts entered a state of contractual performance difficulties [10]. If the contract does not contain a clause for alterations in laws or substantial adverse events, then due to policy modifications during the period of the transaction, both parties will be in a difficult situation. First, how to add clauses for adapting to changes in regulations in the contract; second, how to balance the stability of the relationship between the contract and the policies formulated by regulators in practice.

Secondly, the regulations in the different places also vary, and cross-border contracts are therefore more complex. The validity and enforceability of the ISDA master agreement under Chinese law often require a joint review by regulatory authorities and the courts [11]. When foreign institutional investors sign the NAFMII bond repurchase master agreement, they must comply with Chinese regulations and consider the compliance requirements of the jurisdiction where they are located at the same time. The scope of application and rules for collateral management under the close-out netting provisions in various countries differ significantly. The parties to the transaction need to meet many regulatory standards in one contract; thus, negotiation costs will be higher and compliance risks will also increase.

Third, the new financial business models are adding new complexities to the current system. New Areas for cross-border business, such as digital finance and green finance, are developing

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at a high speed, and their transaction structures and risk characteristics differ from those of traditional financial products. The current standardised contracts mainly cover traditional financial products and have not yet established a system of clauses for the new areas. The National Financial Regulatory Administration (NFRA) has proposed to speed up the construction of international standards for digital finance, green finance, etc., and at the same time, update regulatory frameworks and contract configurations are necessary.

The following four problems can be addressed to resolve the above conflicts. First, set a reasonable transition period for revising the regulatory policies to prevent an immediate effect on the existing contracts due to parameter changes. Second, through judicial recognition or legislative provisions, guarantee the legal effect of close-out netting arrangements and reduce the risks of conflicting legal systems. Thirdly, convert regulatory demands into standardised contract clauses to address the rule deficiency in the new area. Fourthly, provide some scope for the autonomy of the contracting parties in the scope of regulation and avoid excessive regulation that may harm market vitality.

7. Conclusion

Based on the interaction between the regulatory system and transaction contract design, this paper investigates the coordination logic of cross-border financial risk prevention and control at multiple levels. In short, the foundation of this institutional design is the cooperation between the two sides. The regulatory system has introduced a system of macro-prudential regulation, micro-behavioural supervision and multi-departmental cooperation mechanisms to establish all-round safety boundaries for cross-border financial activities. At the same time, the transaction contract incorporates regulatory requirements through standardised master agreements, risk allocation clauses and compliance obligations, thus converting regulatory requirements into enforceable private law obligations. The two are in the following three ways: legal embedding, indirect influence, and format recognition. The three attributes of this institutional system are target alignment, mechanism linkage and joint reinforcement of legal effects.

The construction of this institutional system does not imply that the operation of coordination logic will be free from problems. There are still some deficiencies in practice. There is an inherent conflict between the slow-moving adjustment speed of regulatory policies and the demand for stability in contract relations; a lack of uniformity in regulatory rules across different jurisdictions makes cross-border contract enforcement more difficult; and standardised construction of contracts in new fields, such as digital finance and green finance, has not been institutionally realised. To address the problems above, it is necessary to keep the binding force of the regulatory system and fully use the elastic function of contracts for risk allocation. In particular, the next institutional reforms will aim to increase the foreseeability of regulatory policies, promote the coordination of international rules, and speed up the standardised construction of contracts in new areas.

In fact, the coordination logic of the regulatory system and contractual provisions is the result of rule constraints and contractual designs in financial governance. Given the complexity and rapid changes in the field of cross-border finance, a single governance instrument cannot be employed to manage all risks of prevention and control independently. The reason for the rule is to limit damage and maintain order; the strength of a contract is that it is flexible. Only by combining the two sides can a feasible balance point be reached between expanding openness and controlling risks, and thus an institutional foundation for high-level financial opening is provided.

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