

FATF



Anti-money laundering and
counter-terrorist financing
measures

People's Republic of China

2nd Enhanced Follow-up Report &
Technical Compliance Re-Rating

Follow-up report



October 2021



The Financial Action Task Force (FATF) is an independent inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction. The FATF Recommendations are recognised as the global anti-money laundering (AML) and counter-terrorist financing (CTF) standard.

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China: 2nd Enhanced Follow-up Report

1. Introduction

The FATF Plenary adopted the mutual evaluation report (MER) of China in February 2019¹ and its 1st enhanced follow-up report (FUR) with technical compliance re-ratings in October 2020.² This 2nd enhanced FUR analyses China's progress in addressing the technical compliance deficiencies identified in its MER relating to Recommendations 3, 8, 16, 18, 29, 35 and 38. No Recommendations have changed since the adoption of its 1st enhanced FUR.

Re-ratings are given where sufficient progress has been made. Overall, the expectation is that countries will have addressed most if not all technical compliance deficiencies by the end of the third year from the adoption of their MER. This report does not address what progress China has made to improve its effectiveness.

2. Findings of the MER and 1st Enhanced Follow-up Report

China's MER and 1st enhanced FUR rated China's technical compliance as follows:

Table 1. Technical compliance ratings, October 2020

R.1	R.2	R.3	R.4	R.5	R.6	R.7	R.8	R.9	R.10
LC	C	PC	C	LC	PC	NC	PC	C	LC
R.11	R.12	R.13	R.14	R.15	R.16	R.17	R.18	R.19	R.20
C	PC	LC	LC	LC	PC	LC	PC	C	LC
R.21	R.22	R.23	R.24	R.25	R.26	R.27	R.28	R.29	R.30
LC	NC	NC	NC	NC	LC	LC	NC	PC	C
R.31	R.32	R.33	R.34	R.35	R.36	R.37	R.38	R.39	R.40
C	LC	LC	LC	PC	LC	LC	PC	LC	LC

Note: There are four possible levels of technical compliance: compliant (C), largely compliant (LC), partially compliant (PC), and non-compliant (NC).

Source: China 1st Enhanced Follow-up Report & Technical Compliance Re-Rating, October 2020: <https://www.fatf-gafi.org/media/fatf/documents/reports/fur/Follow-Up-Report-China-2020.pdf>.

Given these results and China's level of effectiveness, the FATF placed China in enhanced follow-up. The following experts assessed China's request for technical compliance re-rating:

¹ www.fatf-gafi.org/publications/mutualevaluations/documents/mer-china-2019.html

² www.fatf-gafi.org/media/fatf/documents/reports/fur/Follow-Up-Report-China-2020.pdf

- Ms. Lida Tsagaraki, Executive - AML Department, Ministry of Finance, Greece.
- Mr. Daniil Burda, Deputy Head of the International Law Unit -Legal Department, Rosfinmonitoring (Russia FIU), Russia.

Section 3 of this report summarises the progress China has made in improving technical compliance. Section 4 sets out the conclusion and a table showing which Recommendations have been re-rated.

3. Overview of progress to improve technical compliance

This section summarises China's progress to improve its technical compliance by:

- a) Addressing some of the technical compliance deficiencies identified in the MER, and
- b) Implementing new requirements where the FATF Recommendations have changed since China's 1st enhanced follow up report (None).

3.1. Progress to address technical compliance deficiencies identified in the MER

China has made progress to address technical compliance deficiencies identified in the MER in relation to R.3, R.8, R.16, R.18, R.29 and R.38, rated PC. As a result of this progress, China has been re-rated on these Recommendations.

The FATF welcomes the progress achieved by China in order to improve its technical compliance with R.35. However, this does not justify an upgrade of this Recommendation's rating at this stage.

Recommendation 3 (originally rated PC)

R.3 was rated PC in China's 4th MER due to several shortcomings, including: some of the predicate offences were too narrow, the existence of thresholds and the fact that self-laundering was not criminalized and prison sanctions were low compared to the penalties for some of the main predicate offences that the third-party ML criminalisation aims to deter. Legal entities were not criminally liable and it was unclear if sanctions for legal persons were proportionate and dissuasive.

Since the MER, the required elements from Palermo and Vienna Conventions, including possession, have been covered. Self-laundering is now criminalized; legal entities are liable for committing money-laundering offences and the value range to determine if a behaviour is criminal is no longer applicable. Proportionate and dissuasive sanctions now apply to natural persons convicted of money laundering. However, legal entities are not criminally liable under Art. 349 CL.

China has made progress to address the above noted deficiencies and the remaining deficiency is considered minor, on this basis, **R.3 is re-rated largely compliant.**

Recommendation 8 (originally rated PC)

R.8 was rated PC in China's 4th MER due to several shortcomings. For instance, China had not attempted to identify the subset of organisations within its broader NPO sector that meet the FATF definition of an NPO and are therefore at greater risk of TF abuse. China did not have a risk-based monitoring mechanism to address the risk of TF within this sector and had not demonstrated that it conducts outreach specific to the risk of TF, including to the donor community. Finally, it was unclear if there was sufficient investigative expertise and capabilities to examine NPOs suspected of either being exploited by, or actively supporting, terrorist activity, or terrorist organisations.

Since the MER, Chinese authorities have developed risk criteria to identify the type of NPOs that are vulnerable to TF and the risk assessment of NPOs now includes details on how the sub-sector could be vulnerable to terrorist actors. China has identified foundations as most likely to be vulnerable for terrorist financing abuse, and has taken appropriate and proportionate measures to mitigate risks including by revising provisions applicable to them, applying risk-based supervision and providing best practices. In addition, China now has the sufficient expertise and capabilities to examine suspected NPOs and has strengthened its policies to supervise and monitor NPOs in relation to TF abuse. Finally, Chinese authorities have increased their outreach to the NPO sector and awareness raising activities of TF risks, with a special emphasis on foundations. Further work could be done to further develop best practices with the sector.

China has addressed most of the deficiencies identified in its MER and the remaining deficiency is considered minor. On this basis, **R.8 is re-rated largely compliant.**

Recommendation 16 (originally rated PC)

R.16 was rated PC in China's 4th MER due to a number of shortcomings, including the lack of an obligation to verify originator information obtained on cross-border transfers denominated in Yuan and to verify beneficiary information related to cross-border transfers denominated in Yuan (unless the amount of the transfer exceeds the Yuan equivalent of USD 1 467). In addition, there was no requirement for FIs to verify their customer's information for transfers less or equivalent to USD 1 000 and to verify the identity of the beneficiary where there is suspicion of ML or other illegal activity.

China addressed the majority of these deficiencies. For instance, China addressed the deficiencies in relation to the threshold in RMB for verifying the identity of originators and beneficiaries, however, minor deficiencies in R.16 remain, including those related to R.6.

On this basis, **R.16 is re-rated largely compliant.**

Recommendation 18 (originally rated PC)

R.18 was rated PC in China's 4th MER due to several deficiencies, including the fact that the obligations for FIs on establishing internal controls did not explicitly require having regard to the ML/TF risks and the size of the business. In addition, payment institutions were neither explicitly required to have an ongoing training program and an independent audit function, nor required to implement group-wide programs against ML/TF, appoint a compliance officer at the management level and apply screening procedures to ensure high standards when hiring employees.

Since the MER, China amended the Measures for Supervision and Administration on Anti-Money Laundering and Countering the Financing of Terrorism in Financial Institutions (Measures). Payment institutions are now required to establish and improve AML/CFT internal control policies, in light of their ML/TF risk profiles and the size of business, and to have an ongoing training program and an independent audit function. In addition, they are also required to implement group-wide programs against ML/TF and to apply additional measures to manage the ML/TF risks.

Deficiencies identified China's MER have been addressed and **R.18 is re-rated compliant.**

Recommendation 29 (originally rated and maintained PC in 1st FUR)

R.29 was rated PC in China's 4th MER due to several shortcomings: China's FIU did not act as a national centre for the receipt and analysis of STRs and other information, and for the dissemination of the results of that analysis. In addition, the China Anti-Money Laundering Monitoring and Analysis Centre (CAMLMAC), part of China's FIU, did not have the power to request from the reporting institutions any additional information as needed to perform its analysis properly. Furthermore, the FIU's work was limited in terms of operational and strategic analyses, with some specific shortcomings related to its operational independence and autonomy. Finally, China did not file an unconditional application for Egmont Group membership.

Since its MER, China has taken substantial steps to address the deficiencies identified in relation to R.29. China has launched the 2nd Generation AML Monitoring and Analysis System, a new platform for large value and suspicious transaction reports of obliged institutions accessible by all parties of China's FIU: CAMLMAC, the Anti-Money Laundering Bureau (AMLB) and People's Bank of China Branches. However, a minor deficiency remains concerning the unconditional application for Egmont Group membership.

On this basis, **China is re-rated largely compliant.**

Recommendation 35 (originally rated PC)

R.35 was rated PC in China's 4th MER because there were concerns that the sanctions applicable to the financial sector were not effective, dissuasive and proportionate given their low scale and cap compared to the size and composition of the financial sector in China.

China has made significant progress in relation to the dissuasiveness of sanctions and especially as regards the upper limits of sanctions which are now considered to be dissuasive. However, considerations in relation to the application of measures to DNFBPs still apply, as no further documentation since the MER has been provided.

China's progress is noted, however the rating for **R.35 remains partially compliant.**

Recommendation 38 (originally rated PC)

R.38 was rated PC in China's 4th MER because there were no legal provisions or procedures to expedite foreign freezing, seizure, and confiscation requests beyond the legal provisions and procedures that apply for any MLA requests and no legal provision for executing equivalent value seizures and confiscation requests in China. In addition, there were no specific authority or procedures for providing MLA to

requests made on the basis of foreign non-conviction-based confiscation proceedings (apart from exceptional circumstances).

Since the MER, China has made significant progress and has issued measures to expedite foreign seizing, freezing and confiscation requests, allowing for seizing and confiscation of property of equivalent value and facilitating non-conviction based confiscations.

On this basis, **R.38 is re-rated compliant**.

3.2 Progress on Recommendations which have changed since adoption of the MER and where progress has been made

Since the adoption of China's MER and 1st FUR, no other FATF Recommendations have been amended which were not previously assessed during China's follow-up process.

3.3 Overview of other Recommendations rated NC/PC

China reported progress on several other Recommendations rated NC/PC. The following is a brief summary of the legislative and operational changes and other concrete measures China has taken since its 1st FUR with the intention to improve compliance with the following Recommendations:

- **Recommendations 22, 23 and 28:** The AML Law of China is currently under revision and will include general provisions of the AML/CFT obligations and supervisory framework of DNFBP sectors. In addition, the PBC, in coordination with other authorities, conducted sectorial ML/TF risk assessments (SRAs) on all DNFBP sectors, including real estate agents, dealers in precious metals and stones, lawyers, notaries, accountants, and trust and company service providers. The SRAs comprehensively analysed ML/TF threats and vulnerabilities, including deep descriptions on market conditions, scales and related activities, inherent risks, and controlling measures in place. The PBC and competent authorities are planning to draft AML/CFT regulations and conduct supervisions separately on the basis of the SRAs results.
- **Recommendations 24 and 25:** Financial institutions are continuously improving the quality of CDD, using a variety source of information to verify the identity of beneficial owners and maintain the beneficial ownership (BO) information. In addition, the AML Law of China, currently under amendments, will cover the legal basis for establishing an efficient BO regime. Finally, the PBC is conducting researches and risk assessment on legal arrangements in China and plans to update the NRA to cover assessment of all types of legal persons.

4. Conclusion

Overall, China has made progress in addressing most of the technical compliance deficiencies identified in its MER, and has been upgraded on R.3, R.8, R.16, R.18, R.29 and R.38. R.35 remains partially compliant, as insufficient progress has been made to justify an upgrade at this stage.

Considering the progress made by China since the adoption of its 1st FUR, its technical compliance with the FATF Recommendations has been re-rated as follows:

Table 1. Technical compliance ratings, October 2021

R.1	R.2	R.3	R.4	R.5	R.6	R.7	R.8	R.9	R.10
LC	C	LC	C	LC	PC	NC	LC	C	LC
R.11	R.12	R.13	R.14	R.15	R.16	R.17	R.18	R.19	R.20
C	PC	LC	LC	LC	LC	LC	C	C	LC
R.21	R.22	R.23	R.24	R.25	R.26	R.27	R.28	R.29	R.30
LC	NC	NC	NC	NC	LC	LC	NC	LC	C
R.31	R.32	R.33	R.34	R.35	R.36	R.37	R.38	R.39	R.40
C	LC	LC	LC	PC	LC	LC	C	LC	LC

Note: There are four possible levels of technical compliance: compliant (C), largely compliant (LC), partially compliant (PC), and non-compliant (NC).

China will remain in enhanced follow-up and will report back to the FATF on progress achieved on improving the implementation of its AML/CFT measures in October 2022.

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Anti-money laundering and counter-terrorist financing measures in the People's Republic of China

2nd Enhanced Follow-up Report & Technical Compliance Re-Rating

As a result of China's progress in strengthening their measures to fight money laundering and terrorist financing since the assessment of the country's framework, the FATF has re-rated the country on 5 of the 40 Recommendations.

The report also looks at whether China's measures meet the requirements of FATF Recommendations that have changed since their Mutual Evaluation in 2019.

Follow-up report