

# The revised AML Law: self-assessments of money laundering risks

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On 8 November 2024, the Standing Committee of the 14th National People's Congress (NPC) approved the revised Anti-Money Laundering (AML) Law of the People's Republic of China (hereinafter referred to as the "revised AML Law"), which took effect on 1 January 2025. This revised AML Law emphasizes a risk-based approach, requiring financial institutions to proactively identify and assess the money laundering risks pertinent to their specific business operations and products. Additionally, it incorporates the assessment of money laundering risks into the enforcement of penalties for legal violations and clearly defines the related legal obligations of financial institutions. As a result, conducting self-assessments of money laundering risks and implementing effective measures based on these evaluations have become legal obligations for financial institutions. The effectiveness of self-assessments is crucial for managing both money laundering and compliance risks at the institutional level.

## Background

### International Standards

The Financial Action Task Force (FATF) emphasizes in the *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation: The FATF Recommendations* that countries must identify, assess and understand the money laundering and terrorist financing risks within their jurisdictions and they are obligated to implement measures to prevent and control these risks which are commensurate with the risks identified. At the same time, it is essential for these countries to mandate that their financial institutions, along with designated non-financial businesses and professions, to identify, assess and implement effective measures to mitigate the risks of money laundering and terrorist financing.

In 2019, the FATF released its *Mutual Evaluation Report on Anti-Money Laundering and Counter-Terrorist Financing Measures of China*. While acknowledging China's progress on the multi-tiered system for assessing money laundering risks, the report highlighted areas needing improvement, including a significant deficiency in the awareness of these risks among obligated institutions and misalignments between the control measures and the actual risk scenarios. In this context, Chapter III of the revised AML Law stipulates that "Financial institutions should... tailor their operations and personnel to the scale of their activities and the associated money laundering risks... Financial institutions are required to regularly assess money laundering risk levels and develop corresponding risk management systems and procedures, implementing relevant information systems as necessary."

### Domestic regulatory requirements

On 30 September 2018, the Anti-Money Laundering Bureau of the People's Bank of China (PBoC) released the *Guidelines on Risk Management of Money Laundering and Terrorist Financing for Legal Entity Financial Institutions (Document [2018] No. 19) ("Document No. 19")*. This document marked the first instance in which a regulatory normative framework for money laundering risk assessment was established, providing essential guidelines for financial institutions to develop their own money laundering risk assessment systems.

In early 2021, the PBoC further advanced this initiative by issuing the *Guidance on the Self-Assessment by Incorporated Financial Institutions on Money Laundering and Terrorist Financing Risks (Document [2021] No. 1) ("Document No. 1")*. This document encourages corporate financial institutions to enhance their awareness and management of money laundering and terrorist financing risks and provides a comprehensive framework and guidance on the general requirements, content, process and methodology of the assessment and the application and management of results.

In April 2024, the Anti-Money Laundering Bureau of the PBoC released *the Circular on Enhancing Considerations for Money Laundering Risk Assessment of Financial Institutions (Document [2024] No. 4)* (“Document No. 4”). This document highlights the importance of risk considerations and provides new directives on the analysis and utilization of both internal and external information. At the same time, Document No.4 urges financial institutions to further refine and enhance their risk assessment processes aligned to the latest stipulations, effective from 2024.

Under the newly revised AML Law, China has integrated money laundering risk assessments into its legal framework for the first time. The revisions strengthen self-assessment requirements for financial institutions and introduce stricter penalties for non-compliance with these obligations.

## Review of the first round of self-assessment initiatives

Since the introduction of Document No.1, corporate financial institutions have successfully completed the initial round of self-assessment regarding money laundering risks. They have been effectively utilizing the assessment model to identify and quantify their own money laundering risks and implementing appropriate control measures to address high-risk areas. The self-assessment process has become an essential driving force for financial institutions in developing a robust money laundering risk management framework. We have identified several commendable practices, including but not limited to the following:

### 1. Defining accountabilities for money laundering risk management across all levels

The self-assessment of money laundering risks is a comprehensive initiative that encompasses various dimensions and requires meticulous effort. It calls for active involvement of the board of directors, senior management, all business departments and branches. In the initial round of self-assessment, each financial institution has established a dedicated working group to clarify the responsibilities related to money laundering risk management across various levels and departments within the organization.

### 2. Establishing a self-assessment framework for money laundering risks

In the initial round of self-assessment, each financial institution has implemented a structured self-assessment framework that clearly defines its objectives, scope, processes, methodologies and frequency of assessments. This framework provides a robust foundation for conducting self-assessments. Financial institutions have thoroughly analyzed their jurisdiction, products/service and customer and channels, establishing metrics to evaluate the effectiveness of inherent risks and control measures based on various risk factors and management processes related to design, execution and oversight.

### 3. Advancing the establishment of anti-money laundering data systems

Building on the insights gained from the initial round of self-assessment, financial institutions have refined the processes and methodology for extracting quantitative data across each dimension of inherent risk. Furthermore, several institutions have proactively implemented the governance of anti-money laundering data, developing specific data verification rules in alignment with the data interface standards required by regulators for on-site anti-money laundering inspection. They have also implemented corrective actions to resolve data discrepancies, improving the quality of self-assessments and enhancing the overall integrity of anti-money laundering data across the organization.

At the same time, we have observed several challenges, including the evasion of responsibilities by relevant departments, a unilateral approach to establishing the indicator system, limited applicability of assessment standards, far-fetched assessment conclusions and insufficient effectiveness in utilizing the results. The journey toward effective self-assessment is a long and challenging endeavor.

## Outlook for the upcoming round self-assessment initiatives

Financial institutions must urgently strengthen the application of the risk-based approach, focusing on improving the identification of money laundering risks and enhance internal anti-money laundering management capabilities. The focus of self-assessment activities should shift from mere 'compliance in format' to a more robust emphasis on 'effectiveness in essence'. Though financial institutions and their professionals are familiar with the concept of 'effectiveness', developing practical solutions within the context of anti-money laundering remains a significant challenge.

In accordance with the stipulations outlined in Document No.1, corporate financial institutions are required to conduct regular self-assessments of money laundering risks, generally with cycle not exceeding 36 months. Organizations with higher inherent or residual risks should perform a self-assessment no more than 24 months. This means that financial institutions must initiate the new round of self-assessment by 2025 at the latest and we suggest they should pay particular attention on the following key areas:

### 1. Optimizing the assessment process and consolidating the responsibilities of each department within the organization

The self-assessment process of financial institutions requires a broad involvement of governance, management and executive levels. Clearly defining the distribution of responsibilities among different departments and business units is essential to the self-assessment process. Based on the outcomes of the initial round of self-assessment, financial institutions should consider their current systems, data, departmental structures and other relevant factors to clearly define the specific responsibilities of each department and to create a comprehensive list of duties for self-assessment. For instance, it is crucial to define the responsibilities of the business departments for the money laundering risk assessment of the product. This self-assessment should clarify the rationale and responsible parties and define the methodologies used, establishing a collaborative process with the business departments to identify and manage money laundering risks, enhancing the engagement of business departments and deepening their understanding of the money laundering risks and the necessary control measures. Additionally, it is crucial to identify and confirm the classification and extraction methods of the business data as early as possible to enhance data validity and prepare for the subsequent extraction of inherent risk data.

### 2. Reviewing the assessment framework and improving the relevance of assessment indicators

The insufficient relevance of assessment indicators often leads to outcomes that deviate from the intended objectives, making it difficult to reflect the actual circumstances or risk in the relevant assessment areas. This issue is commonly encountered by many financial institutions during their initial self-assessment phase. It is recommended that financial institutions conduct a comprehensive review of their assessment framework and methodologies, optimizing and adjusting the relevant assessment indicators based on insights gained from the first round of self-assessment, while also considering changes in both internal and external environments. For instance, in alignment with the latest stipulations outlined in Document No.4, financial institutions should consider their unique business characteristics and include the risk factor of 'transaction transparency' into their customer assessment metrics. They should incorporate assessment indicators that address the completeness and authenticity of counterparty information. By analyzing their own suspicious transaction reports, previous transactions and investigation cases of criminal freezing and seizure, financial institutions should integrate the number of customers associated with suspicious transaction reports and those involved in investigation cases into the self-assessment model, enhancing the accuracy of the risks they encounter. In recent years, regulatory authorities have established various laws and guidelines to support financial institutions building a substantial framework of self-assessment indicators. Financial institutions are encouraged to proactively explore and develop the assessment indicators tailored to their specific business operations, enhancing the efficiency of their self-assessment processes. This will be a key focus area of the FATF's fifth round of mutual assessments as well.

### 3. Implementing the corrective actions to ensure the effective use of self-assessment results

We suggest that financial institutions should conduct a thorough review of the high-risk scenarios identified during the initial self-assessment and ensure they have appropriate corrective actions and measures implemented in the insufficient areas. In the next round of self-assessment, it is essential to continuously monitor the implementation of corrective actions related to these high-risk situations and incorporate this tracking into the assessment framework. For instance, it is crucial to determine whether risk mitigation strategies have been established for high-risk customer segments concerning due diligence prior to onboarding, ongoing due diligence throughout the business relationship and enhanced due diligence in response to risk flags. The effectiveness of these measures in daily operations should also be a focal point in the self-assessment process. Upon completing this round of self-assessment, it is important to analyze the results in comparison to the previous, identify the root causes of any issues, clarify the responsibilities and corrective actions and develop a detailed plan to ensure a closed-loop management approach.

### 4. Monitoring the changing risks and implementing a comprehensive lifecycle management system for money laundering risks

We suggest that financial institutions should enhance the effectiveness of self-assessment processes by developing a real-time monitoring system for critical money laundering risk indicators. These indicators could include the number of high-risk customers associated with money laundering, the volume of customers engaging with high-risk money laundering products, the frequency of transactions involving such products and other significant risk indicators. Institutions should establish a risk threshold based on their specific risk appetite and external guidelines, enabling them to issue early warnings when indicators surpass this threshold. At the same time, it is essential to evaluate and adjust the relevant risk management framework promptly. Timely reassessment and modification of control measures will support the development of a comprehensive lifecycle monitoring and management system for money laundering risks, ensuring the dynamism and sustainability of the assessment process.

### 5. Expanding the scope of assessment to gradually include new areas, such as proliferation financing risks and specialized preventive measures

At the international level, the FATF Recommendation 1 (*Risk assessment and application of risk-based approach*) requires nations or regions, along with the private sector, to identify, assess, understand and manage the proliferation financing risks they encounter. In June 2021, the FATF released its *Guidance on Proliferation Financing (PF) Risk Assessment and Mitigation* to further assist in conducting proliferation financing risk assessments. It is also noteworthy that several FATF member countries intend to align the assessment of proliferation financing risks with their assessments of money laundering and terrorist financing risks.

Domestically, the revised AML Law introduces specific preventive measures aimed at combating money laundering, leveraging anti-money laundering strategies to support counterterrorism and non-proliferation efforts. Furthermore, on 19 October 2024, the State Council issued regulations on export control of dual-use items, in line with the international norms to support global non-proliferation efforts.

Financial institutions are encouraged to gradually familiarize themselves with concepts related to proliferation financing and the associated risk assessment methodologies, drawing on the principles of self-assessment used for money laundering risks. They should incorporate the incremental findings from the previous self-assessments into the new operational frameworks whenever fit to enhance the coherence and effectiveness of risk evaluations.

Since 2019, EY team has supported numerous financial institutions in conducting self-assessments of money laundering risks, observing the evolution and development of their self-assessment processes. We are fully aware of the challenges and obstacles faced by financial institutions at various stages of this work. We hope to work together with the industry to explore, investigate and improve the methodologies, enabling financial institutions to effectively identify money laundering risks through self-assessment and to enhance their overall risk management capabilities.

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