



PEOPLE'S REPUBLIC OF CHINA

DETAILED ASSESSMENT REPORT ON THE OBSERVANCE OF STANDARDS AND CODES

December 2017

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DETAILED ASSESSMENT OF OBSERVANCE OF STANDARDS AND CODES

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This report was prepared in the context of a joint IMF-World Bank Financial Sector Assessment Program (FSAP) mission in the People's Republic of China during December, 2016, and February, 2017. The FSAP was led by Simon Gray, IMF and Miquel Dijkman, World Bank, and overseen by the Monetary and Capital Markets Department, IMF, and the Finance and Markets Global Practice, World Bank. Further information on the FSAP program can be found at <http://www.imf.org/external/np/fsap/fssa.aspx> and www.worldbank.org/fsap.

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Glossary

ABS	Asset Backed Securities
AMAC	Asset Management Association of China
AML/CFT	Anti-Money Laundering/Combating the Financing of Terrorism
ASBE	Accounting Standards for Business Enterprises
AUM	Assets Under Management
CAA	China Association of Actuaries
CCP	Central Counterparty
CIS	Collective Investment Schemes
CBRC	China Banking Regulatory Commission
CET1	Common Equity Tier 1
CFA	China Futures Association
CFEX	China Financial Futures Exchange
CICPA	Chinese Institute of Certified Public Accountants
CIRC	China Insurance Regulatory Commission
CMG	Crisis Management Group
CP	Core Principle
CPA	Certified Public Accountant
CRA	Credit Rating Agency
C-ROSS	China Risk-Oriented Solvency System
CSDC	China Securities Depository and Clearing Corporation
CSIS	China Securities Internet System Co. Ltd
CSRC	China Securities Regulatory Commission
D-SIB	Domestic Systemically-Important Bank
D-SII	Domestic Systemically-Important Insurer
FCRG	Financial Crisis Response Group
GEB	Growth Enterprise Board
G-SIB	Global Systemically-Important Bank
HF	Hedge Funds
IAIS	International Association of Insurance Supervisors
ICAAP	Internal Capital Adequacy and Assessment Process
ICP	Insurance Core Principle
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
ISA	International Standards of Auditing
IT	Information Technology
JMC	Joint Ministerial Committee
LCR	Liquidity Coverage Ratio
MF	Mutual Fund
MMF	Money Market Fund
MoF	Ministry of Finance
MMOU	Multilateral Memorandum of Understanding
MOU	Memorandum of Understanding

NAFMII	National Association of Financial Market Institutional Investors
NAV	Net Asset Value
NDRC	National Development and Reform Commission
NEEQ	National Equities Exchange and Quotations Co. Ltd.
NPC	National People's Congress
NPL	Non-Performing Loan
ORSA	Own Risk and Solvency Assessment
OTC	Over the Counter
P&C	Property & Casualty
PBC	People's Bank of China
PEP	Politically-Exposed Person
PFMI	Principles for Financial Market Infrastructure
QDII	Qualified Domestic Institutional Investor
QFII	Qualified Foreign Institutional Investor
RCAP	Regulatory Consistency Assessment Program
RMB	Renminbi
RQFII	Renminbi Qualified Foreign Institutional Investor
RRP	Recovery and Resolution Plan
SAC	Securities Association of China
SARMRA	Solvency-Aligned Risk Management Requirements and Assessment
SC	State Council
SME	Small and Medium-sized Enterprise
SIPF	Securities Investor Protection Fund
SOE	State Owned Enterprise
SSE	Shanghai Stock Exchange
VWAP	Volume weighted average price
WB	World Bank
WMPs	Wealth Management Products

BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

A. Introduction

1. The assessment of the current state of the implementation of the Basel Core Principles for Effective Banking Supervision (BCP) in China was completed as part of the 2017 FSAP update.¹ The FSAP update was undertaken by the International Monetary Fund (IMF) and World Bank (WB) and the BCP assessment mission took place from February 9–28, 2017. It reflects the regulatory and supervisory framework in place as of the date of the completion of the assessment. It is not intended to represent an analysis of the state of the banking sector or crisis management framework, which are addressed in other parts of the FSAP.

2. An assessment of the effectiveness of banking supervision requires a review of the legal framework, and detailed examination of the policies and practices of the institutions responsible for banking regulation and supervision. In line with the BCP methodology, the assessment focused on the China Banking Regulatory Commission (CBRC) as the supervisor of the banking system, and did not cover the specificities of regulation and supervision of other financial intermediaries.

B. Information and Methodology Used for Assessment

3. The current assessment of the CBRC was against the BCP methodology issued by the Basel Committee on Banking Supervision (BCBS) in September 2012. The authorities opted to be assessed on the essential criteria. The last BCP assessment in the People's Republic of China was prepared in the course of the 2011 Financial Sector Assessment Program (FSAP). The BCP methodology has been revised since the last assessment took place and the revisions have led to some substantive changes.

4. In the 2012 revision of the Core Principles (CPs), the BCBS sought to reflect the lessons from the global financial crisis and to raise the bar for sound supervision reflecting emerging supervisory best practices. New principles have been added to the methodology along with new essential criteria (EC) for each principle that provide more detail. Altogether, the revised CPs now contain 247 separate essential and also additional criteria against which a supervisory agency may now be assessed. In particular, the revised BCPs strengthen the requirements for supervisors, the approaches to supervision and supervisors' expectations of banks. While the BCP set out the powers that supervisors should have to address safety and soundness concerns, there is a heightened focus on the actual use of the powers, in a forward-looking approach through early intervention.

¹ The Assessment Report was prepared by Katharine Seal, IMF, Valeria Salomao Garcia, World Bank and Yee Theng, external expert from the Monetary Authority of Singapore

5. The assessment team reviewed the framework of laws, rules, and guidance and held extensive meetings with authorities and market participants. The assessment team met officials of CBRC, including from the provincial office of the CBRC in Chongqing, and additional meetings were held with the People's Bank of China (PBC), the Ministry of Finance (MoF), auditing firms, and banking sector participants. The authorities provided a comprehensive self-assessment of the CPs, as well as detailed responses to additional questionnaires, and facilitated access to staff and to supervisory documents and files on a confidential basis. Owing to time constraints it was not possible to make as full a study of the documents as the assessors would have wished but the authorities did everything that was possible to facilitate access.

6. The team appreciated the very high quality of cooperation received from the authorities. The team extends its warm thanks to staff of the authorities, in Beijing and Chongqing, who provided excellent cooperation, including provision of documentation and technical support.

7. The standards were evaluated in the context of the sophistication and complexity of the financial system of the People's Republic of China. The CPs must be capable of application to a wide range of jurisdictions whose banking sectors will inevitably include a broad spectrum of banks. To accommodate this breadth of application, a proportionate approach is adopted within the CP, both in terms of the expectations on supervisors for the discharge of their own functions and in terms of the standards that supervisors impose on banks. An assessment of a country against the CPs must, therefore, recognize that its supervisory practices should be commensurate with the complexity, interconnectedness, size, and risk profile and cross-border operation of the banks being supervised. In other words, the assessment must consider the context in which the supervisory practices are applied. The concept of proportionality underpins all assessment criteria. For these reasons, an assessment of one jurisdiction will not be directly comparable to that of another.

8. An assessment of compliance with the BCPs is not, and is not intended to be, an exact science. Reaching conclusions required judgments by the assessment team. Banking systems differ from one country to another, as do their domestic circumstances. Furthermore, banking activities are undergoing rapid change after the crisis, prompting the evolution of thinking on, and practices for, supervision. Nevertheless, by adhering to a common, agreed methodology, the assessment should provide the Chinese authorities with an internationally consistent measure of the quality of their banking supervision in relation to the revised CPs, which are internationally acknowledged as minimum standards.

C. Preconditions for Effective Banking Supervision

9. There is a developed economic policy framework, which is increasingly aimed at reorienting the economy towards consumption-led growth. After decades of growth led by investment and exports, the authorities are targeting a more market-oriented, consumption-based and services-driven economy. The approach has been clearly articulated in the 13th Five Year Plan. Target growth levels have been reduced. GDP growth remains high, fiscal policy expansionary and inflation at a low level. China continues to run a large current account surplus.

10. There is a policy-making infrastructure in place for the financial sector. A sector-based regulatory framework has been in place since the late 1990s, comprising the China Banking Regulatory Commission (CBRC), China Securities Regulatory Commission (CSRC) and China Insurance Regulatory Commission (CIRC). The People's Bank of China (PBC) is responsible for financial stability overall. All these agencies fall under the leadership of the State Council, which is the leading body for coordinating the development of financial stability policies and also provides the mechanism for developing and publishing broad strategic plans for economic sectors, including financial services.

11. The State Council coordinates the overall planning and development of financial stability policies. After the global financial crisis, the State Council established the Financial Crisis Response Group (FCRG) to boost the progress of financial reforms and address the prevention and resolution of systemic risks. The PBC is responsible for analyzing macro-financial stability, while the CBRC, CSRC and CIRC are responsible for rolling out prudential supervisory arrangements in respective sectors. In August 2013, the Financial Regulatory Coordination Joint Ministerial Committee (JMC) was established to enhance the coordination between monetary policies and financial regulatory policies. The JMC also has a role in closing supervisory loopholes, prohibiting supervisory arbitrage, preventing cross-sector and cross-market systemic financial risks and safeguarding financial stability.

12. In order to prevent and control systemic risks, the authorities have sought to establish a comprehensive system. The coverage is intended to extend from individual financial institutions to the financial industry as a whole. Under this framework, the PBC, CBRC, CSRC and CIRC, and other relevant agencies collaborate to tackle cross-sector and cross-market risks. Economic and financial factors that may lead to systemic risks are identified and monitored so that control and mitigation can be deployed in a timely manner.

13. China has an established framework of commercial laws and judicial system. The legislative framework includes company, bankruptcy and contract laws as well as laws on the protection of consumer rights and property. The judicial system comprises investigation and prosecution services, a courts and penal system, people's mediation, and lawyer and notary services.

14. China has a developed public infrastructure, Accounting and auditing standards are aligned with international standards and practices. The Accounting Law, Law on Certified Public Accountants and Accounting Standards for Business Enterprises (ASBE) include both standards and implementation rules and material on the roles of and responsibilities of Chinese Certified Public Accountants (CPAs). Issued originally in 2006, ASBEs are in general based closely on International Financial Reporting Standards (IFRS). The Accounting Regulatory Department of the Ministry of Finance (MoF) is responsible for issuing ASBEs and auditing standards, which since 2010 have also been based on international standards. The use of IFRS is not permitted for domestic reporting, although companies whose securities trade on the Hong Kong Stock Exchange may choose to use them for reporting to Hong Kong investors. Audit firms are licensed and oversight of audit work is undertaken by the MoF and the relevant provincial governmental finance departments.

15. The CBRC has the powers to take over, restructure or close distressed banking financial institutions. Where a banking financial institution has experienced or is likely to experience a credit crisis that will severely jeopardize the lawful rights and interests of depositors and other customers, the CBRC may, take over the institution or facilitate its restructuring. Further, where a banking financial institution fails to comply with applicable laws and regulations or is not properly operated or managed, and such failure or poor operation/management will severely threaten financial order and/or undermine public interests the CBRC has right to close it (the *Banking Supervision Law*). The CBRC has the right to apply to the courts to initiate bankruptcy, reorganization or liquidation processes of a commercial bank that is unable to pay its debts or is likely to become insolvent (the *Commercial Bank Law* and the *Enterprise Bankruptcy Law*).

16. The Chinese authorities are in the process of updating their practices and legislation to meet developing international standards in the fields of resolution and recovery. Currently, the *Regulations on Resolving Bankruptcy Risk of Commercial Banks* has been drafted and is under revision. The draft makes reference to the *Key Attributes of Effective Resolution Regimes for Financial Institutions* published by the FSB to improve effectiveness and efficiency, and reflects considerations on the liquidation system stability, close-out netting, cross-border resolution, etc.

17. Deposit insurance protection has been put in place as of May 1, 2015. The *Regulations on Deposit Insurance* set forth provisions on compulsory insurance, reimbursement limits, base premium rates and differential premium systems, as required by the *Core Principles for Effective Deposit Insurance Systems* and other international deposit insurance standards. The deposit insurance system strengthens information sharing in the current financial regulatory coordination mechanism, and supports supervisory work.

D. Main Findings

Objectives, Powers and Responsibilities (CP 1)

18. The legal framework sets clear responsibilities and objectives for banking supervision in China. Overall, CBRC's legal mandate and responsibilities, supported by broad powers, enables CBRC to conduct banking supervision in an effective way, with a primary focus on safety and soundness. A comprehensive set of regulations and procedures have provided CBRC with the necessary tools to properly operationalize its mandate, while strong enforcement powers further support the effectiveness of supervisory actions. While discharging its responsibilities CBRC takes into account the national policy objectives for economic and social progress (which rely importantly on the provision of credit to the economy) aiming at balancing its primary mandate of safety and soundness with the need to support and promote particular sectors. The potential conflict between safety and soundness objectives and other objectives exists in many countries but can be more acute in China because of the predominant use of the banking system, much of which is state owned, to achieve economic and social goals. In such a context, it is even more important that CBRC communication does not mislead banks as to the CBRC's commitment first and foremost to safety and soundness.

Independence (CP2)

19. The CBRC lacks operational independence, and this might impair its ability to execute its legal mandate. The CBRC has a clear legal basis for independence (just as it enjoys a clear legal framework generally), acts with the support of the State Council, and commands industry respect, but the CBRC is not operationally independent. This leads to the potential for the CBRC to fail to execute its legal mandate and ensure that soundness and stability considerations are the primary motivation of its work. Factors contributing to this potential outcome include the fact that the CBRC's decisions can be overturned by the State Council and the fact that there is no legislative requirement to disclose publicly the reasons for the dismissal of the Chair of the CBRC. Although the CBRC has been confirming the central importance of soundness and stability in the CBRC's work, the assessors are concerned that the CBRC's independence is sufficiently compromised to call into question whether the supervisor would always be able to act on its primary, objective—stability—particularly if government policies, whether growth or social protection, conflicted with prudential considerations. Finally, and recognizing that the CBRC operates through a geographically large network, the CBRC must be vigilant in ensuring that all its offices exercise the highest standards of independence and objectivity in the course of their daily supervisory tasks, which are in pursuit of supporting financial stability.

20. Noting that the CBRC has autonomy over neither its staffing numbers nor its organizational design, it must be recognized that resource constraints stifle a supervisor from performing its role effectively. The financial sector growth does not require a linear increase in resources, but the growing complexities and interconnectedness of a system, which includes four Global Systemically Important Banks (G-SIBs), create a significant risk that the CBRC's supervisory oversight will be incomplete, thus creating the potential for system-wide vulnerabilities to emerge. While the CBRC is to be commended on its achievements in enhancing its specialist skillsets, refreshing its supervisory techniques, and adapting its tools with insight and creativity, the complement of staff has been static for a decade and key staff are increasingly attractive to and attracted by industry opportunities. Budgetary independence, allowing increased resources in salary scales and staffing for the more specialist fields, including the emerging area of supervisory stress testing, is an urgent need. It is recognized that public resources must be deployed carefully, but the supervisory authorities cannot fall behind demands created by the major banks. The supervisor forms part of the frontline defenses and ensuring best practice, intensive and early intervention supervisory approaches comes at significantly lower cost than wide-scale capital injection should one or more major banks come under pressure.

Cooperation, Consolidated Supervision and Home-host (CPs 3, 12 and 13)

21. Cooperation and collaboration with local and foreign authorities are in place. The legal and regulatory framework have enabled CBRC to set up a sound framework for cooperation and collaboration with domestic authorities and foreign supervisors. The arrangements seem to be functioning as envisioned by the authorities, albeit the depth and breadth of data and information gathered from domestic supervisors should benefit from an expected and necessary increase within the context of an effective consolidated supervisory framework. CBRC has put significant efforts

since the last FSAP in broadening its home-host relationships, following the expansion of Chinese banks' operations abroad and the classification of four Chinese banks as G-SIBs. As Chinese banks further expand their activities, and groups increase in complexity, an even more proactive approach might be needed.

22. Progress in consolidated supervision is increasingly embedded in the CBRC's practices.

The CBRC has focused on capacity development in this field and is gaining experience and confidence in probing of group-wide risk management, activities and strategies. Careful attention paid to related party transactions by the CBRC supports an important understanding of intra-group dynamics. Areas that should be prioritized for further development include a focus on the wider group and extended network of affiliates, including the upward ownership of groups—i.e., to the ultimate beneficial owners—to ensure that all potential relevant groups are mapped and understood in relation to the bank and the banking group. This mapping is a basic necessity in ensuring a group can be effectively supervised and this information needs to be kept current. The Chinese financial system is changing rapidly in terms of complexity of group structure, and with increasing liberalization and openness these conditions can be expected to intensify, so it is optimal to act now. The CBRC needs stronger powers of ex ante notification and approval of changes in the wider group to make sure that it can act, if needed, in as timely a manner as possible and be preventative as opposed to reactive, and to ensure that consolidated supervision is not undermined. In terms of cross-sectoral activity, cross product selling and provision of similar products—such as wealth management products (WMPs or other forms of collective investment schemes) by the different financial sectors—introduce new dimensions that consolidated supervision must consider, including business, contagion and reputational risks. The CBRC is encouraged to continue applying conservative prudential standards to complement its conduct requirements. Indications that there will be cross sectoral agreements to limit arbitrage opportunities are very welcome.

Permissible Activities, Licensing, Transfer of Ownership and Major Acquisitions (CPs 4 to 7)

23. Permissible activities are clearly defined and highly controlled through the licensing process. The market-entry legal framework and supporting procedures include powers to define and restrict the types of business that banks are allowed to engage in. Approvals are required for any new business line and branches, as well as sound fit and proper criteria for board and senior management. Non-banking activities are allowed on a case by case basis only, including fund management and insurance. Banks' investments in commercial enterprises and real estate not for own-use are not allowed. In the past five years, new licenses have been provided mainly to convert rural cooperatives into banks, as well as for the establishment of foreign banks' operations in China.

24. The evolving context of banks and activities in China has brought some further challenges. The increasing sophistication and complexity of business groups in China, and full implementation of procedures for the entrance of newly established private banks into the market, would require further efforts from the authorities in fully understanding the wider group. The expansion of Chinese operations abroad and increased sophistication of banks' activities might also require additional efforts in order to assess joint ventures and other strategic investments. In addition, authorities should exercise caution, when authorizing non-banking activities, to ensure that

a robust regulatory framework is in place to properly govern such activities, the risks they entail and their implications to the banks, banking groups and the banking system.

25. The ability of CBRC to control transfer of significant ownership is limited by the legal framework. CBRC has a sound process for approvals of direct transfers of significant ownership above 5 percent. But the concepts of influence or indirect control have not been captured by the legal framework. As the role of the state as a shareholder in the banking system diminishes, and banking groups and shareholders' interests increase in complexity, transfers of significant ownership and control through indirect holdings will remain outside of CBRC purview.

Supervisory Approach, Techniques, Reporting and Corrective Actions (CPs 8 to 11)

26. The CBRC plans and executes a high quality supervisory approach. The CBRC is continuing to develop its risk based approach since the last assessment. There are good processes in place for planning and executing both the on and off-site supervisory activities. Since the last assessment there has been intensive investment in the quality of the supervisory data and analytical systems and a refreshing of the analytical methodologies. Supervisory expectations are clearly communicated to banks and are followed up. The use not only of meetings but also notices and risk alerts to ensure that there is responsive feedback to the industry has been effective. Effective use is made of broad sources of information, and the CBRC's supervisory programs have focused on key emerging risks and trends such as the provision of wealth management products to clients and interbank/wholesale market activity. Assessing the resolvability of banks is one field which is still work in progress. While the largest banks, which are identified as G-SIBs have been subject to resolvability assessments, the CBRC is still deliberating on the correct approach for domestic systemically-important institutions. It should be noted that the CBRC has a sound knowledge of the banking groups in the system and of the relative lack of group complexity in most instances.

27. The CBRC needs to continue maturing its diagnostic skills in integrating information on different risks and events to identify root causes of issues, in order to devise a more effective forward-looking approach. Although the CBRC has further enhanced its supervisory rating approach to permit a greater use of supervisory judgment, the leeway for this judgement is highly constrained and for some banking models might fail to reflect the nature of the risks in the banking institution. The next generation of risk methodologies should address this deficiency and provide further support to forward looking integrated risk analysis, so that the interaction between risks can be even more carefully examined, and supervisors identify the potential for vulnerabilities and act before issues crystallize. Continued development of the CBRC's analytical techniques in relation to banks' strategies and business models will provide a robust underpinning for greater supervisory discretion.

28. The CBRC philosophy is, rightly, that the quality of supervisory data is a fundamental pillar of effective supervision. As a consequence, the CBRC has put extensive efforts into its supervisory reporting regime and enhancing the analytical systems that depend on it. There has been an almost wholesale overhaul of the reporting data and considerable care is taken, using on and off-site methods, not only to ensure that the data received is reliable and that banks are

accountable for the information they provide, but also to ensure that the CBRC continues to obtain the data that is most relevant for its evolving supervisory tasks.

29. CBRC demonstrates willingness to act at an early stage, supported by broad corrective powers. CBRC's supervisory approach encompasses a robust early warning system, aiding early action. CBRC counts with an extensive range of tools to enforce corrective action including penalties for the board, senior management and staff, which have been systematically used over the last few years. Problem banks have been addressed primarily through restructuring.

Corporate Governance (CP 14)

30. There is clear supervisory emphasis on the effectiveness of corporate governance of banks. In both off-site surveillance and onsite examination, there is consistent focus on the internal governance structure, clear roles and responsibilities and decision-making processes within the banks. However, the regulatory framework for corporate governance of banks is based on a combination of various Guidelines and Listing Rules. It would be useful to rationalize and eliminate gaps or inconsistencies and have a single legislation as the focal point for supervisory corporate governance reviews in the future. It would also be an opportunity to consider and clarify the criteria to be used to implement corporate governance requirements in a proportionate manner across the institutions with varying size and complexity. Specifically, on board committees, there is a need to establish requirements to ensure the independence of risk management committee, and the nomination and remuneration committees of non-listed banks. Given the large and growing financial sector, CBRC needs to closely monitor and adapt its governance frameworks and supervisory expectations, aligning to best practices, to ensure that they continue to facilitate an environment of trust, transparency and accountability.

Risk Management, Capital Adequacy and Prudential Framework (CPs 15 to 25)

31. Banks have made good progress in their management of individual risks but more needs to be done to adopt an enterprise-wide risk approach. Banks are better at managing individual risks, and for the major banks, internal capital adequacy and assessment process (ICAAP) and stress tests have become an important part of their risk management. Supervisors perform more intensive review of ICAAP and stress tests annually for the large banks. However, full enterprise-wide risk approaches that integrate strategy setting, monitoring, management and stress testing in ways that consider interactions among risks are challenging, particularly for banks with business activities across geographical regions, with diverse businesses and products posing different types of risks. In this regard, assessing whether the banks are effective in adopting enterprise-wide risk approaches and are capable of fully identifying, monitoring and managing the risk interactions should continue to be a focus area of supervision.

32. Work on recovery plan and resolvability assessments is in progress, covering the G-SIBs. CBRC has required the four G-SIBs to prepare and submit recovery plans annually for review, with resolvability assessment being conducted for three. A cross-border crisis management group (CMG) has been established for each G-SIB, comprising senior officials from national authorities

including CBRC, MOF and PBC, as well as some foreign authorities. The CMG is mainly responsible for effective management and resolution of the bank in the event of cross-border financial crisis. It has commenced reviewing and assessing the bank's recovery and resolution plan (RRP) on an annual basis. Given the importance of RRP, CBRC should extend this requirement to the other large banks, in particular those assessed to be systemically important in the domestic market.

33. China has set up a comprehensive and proportionate approach to its capital regime, proactively aligning it with international standards. CBRC has fully adopted Basel III for all banks operating in China, with a few non-material deviations setting higher requirements for common equity tier 1 capital (CET1) and the leverage ratio. So far, six banks have been allowed to implement the advanced approaches for credit and market risk, and a few other banks are expected to be authorized in the near future. Particular focus has been put into the large banks in terms of ensuring the establishment of a forward-looking approach to capital. Although in principle all banks are required to implement the ICAAP, for middle size and small banks CBRC has focused on ensuring proper implementation of Pillar one and requiring mid-term capital planning. Over the last few years CBRC has set informal expectations of dividends distribution around 30 percent in order to further increase banks' reserves.

34. CBRC needs to continue its focus in ensuring that banks adopt a comprehensive approach towards identifying, monitoring and managing overall credit risks. There has been an increase in the scale and complexity of banks' credit risk origination activities since the previous assessment. Non-standard credit activities have emerged, including investments in structured products, off-balance sheet activities and interbank investments. Under this heightened risk environment, CBRC has enhanced its offsite surveillance of credit risk trends and vulnerabilities, intensified onsite examinations, and issued risk alerts and specific notices aimed at addressing challenges and containing specific risks. These are commendable efforts. Given the large number and the diversity of banks and the increased complexity of activities, it is important for CBRC to continue its focus to ensure that banks effectively implement and comply with the recently-issued guidelines targeted at emerging risks. More importantly, the banks' ability to evaluate, monitor and manage overall credit risks comprehensively should continue to be the focus of CBRC's supervisory activities. It will also be useful to develop a comprehensive guidance on credit risk management in line with international standards to ensure that supervisory expectations and minimum standards are well understood.

35. While CBRC has intensified its supervision on banks' loan classification, it should review the current loan classification requirements. Given the rising trend in non-performing loans (NPL), CBRC has taken a lot of efforts, through offsite surveillance and onsite examinations, to ensure accuracy of banks' loan classification and adequacy of provisions. It is important to continue this effort and, in addition, CBRC should review the current loan classification requirements permitting the use of collateral in influencing NPL classification. Such practice makes it difficult to properly assess any increase in credit risk and could potentially result in lower regulatory provisions. Likewise, the requirement permitting loans granted to small enterprises to be classified as NPL only when they are more than 180 days-past-due should be reviewed. The review should assess whether

this practice results in slow downgrading of problem loans and delays the detection of any increase in credit risks in this micro-lending segment.

36. The supervisory framework to guard against large exposures needs to be strengthened. CBRC has put in place requirements for a more comprehensive capture of concentration risks and banks are required to include significant risk concentrations in their stress testing programs for risk management purposes. On the large exposures requirement, however, there is a need to further review and articulate the criterion in identifying relationships between entities with common local government ownership. There is also a need to reduce the existing 50 percent (of Tier-1 capital) limit on interbank exposure and establish a limit on exposures between G-SIBs, to avoid excessive risk concentrations. Such a review would also be in line with CBRC's plans to move towards adopting Basel's large exposures framework.

37. Gaps remain in the related party exposure framework. While the definition of related party is comprehensive, it does not include related banks, and ownership by the state government is not treated as a trigger for related party reporting, limits or approvals. Consistent with recommendations earlier with regard to having a focus on wider group and extended network of affiliates, it is recommended that the exclusions be reviewed to ensure the extra due diligence is accorded to all related parties.

38. Although there has been substantive growth in the Chinese banking system, market risk remains low and the complexity of banks' market risk profile, likewise, remains generally straightforward. Nevertheless, there have been some important developments since the last BCP assessment as now five banks have been approved to use internal models for capital adequacy calculation. Some medium-sized banks have also adopted the internal models approach for market risk measurement, risk appetite setting, limit management and capital management. There are also pilot schemes to introduce securitization into the market, which, if it develops, could introduce new challenges, although the CBRC confirmed that complex transactions (including correlation trading, re-securitization and synthetic products) are not permitted and there is no intention to ever permit such products. As in other risk areas, there are heightened regulatory standards in market risk for the five largest banks and the precise targets that each bank must meet is set on an individual case basis. The CBRC should be well placed to implement the revised Basel market risk standard that was published following the fundamental review of the trading book. Looking forward, however, it is imperative that the CBRC remain vigilant and continue its path in building its market risk capacity.

39. Phased liberalization of interest rates appears to have given banks time to adapt and, to date, banks' behavior is still largely conservative. For its part, the CBRC has enhanced its specialist staff to the extent possible, its outlier analyses, and is introducing pilot projects in targeted locations for more demanding stress and scenario testing (e.g. 250 and 300 basis point shifts as well as twists). Banks are also required to undertake their own scenario analysis and interest rate sensitivity is incorporated in stress testing. The CBRC is, however, encouraged to use the adoption of the revised Basel standard as a springboard for issuing more extensive guidance to the industry.

40. The CBRC approach to liquidity risk supervision is more sophisticated and intensive than at its last assessment. All banks with at least RMB200bn total assets are subject to the liquidity coverage ratio (LCR) and this represents about 90 percent of the assets of the banking system. All banks, including those below the LCR threshold, must meet the liquidity ratio (liquid assets as a percentage of liquid liabilities) and all without exception are subject to the liquidity risk management standards and monitoring tools which are based on the Basel standard. The strengthening of liquidity supervision is particularly welcome given market developments, as lower tier banks are becoming increasingly dependent on wholesale funding. To the extent that this sector is not subject to the LCR, the CBRC should devote a particular supervisory focus. Severe scenarios and parameters are needed in banks' internal stress tests, to address shocks including on wholesale funding and the potential for contagion risk in WMPs causing high demand for outflows. At the time of the assessment, the CBRC was awaiting the Basel Regulatory Consistency Assessment Program (RCAP) mission to examine the regulatory implementation of the Liquidity Coverage Ratio. The BCP and RCAP assessments have an overlapping but not identical focus and should not be seen as substitutes for each other. From the BCP perspective, the CBRC is encouraged to be highly assertive in setting industry expectations in building scenarios, stress testing and contingency planning. Such stress testing practices should, of course, be linked to stress tests required for banks' capital adequacy and risk management planning (i.e., Pillar 2).

41. The CBRC does not permit advanced modelling approaches for capital adequacy and its operational risk supervision has a strong emphasis on business continuity and IT practices. The CBRC does not employ operational risk specialists. As with market risk, there is a considerable variation in the sophistication of banks' approach to operational risk, with the most sophisticated banks using internal approaches to drive forward their risk management approaches, while less complex, typically local and regional banks are more focused on internal controls. As the less complex banks expand their businesses, the challenge for them, as the CBRC is fully aware, is to develop their approach to operational risk in a commensurate manner with their growth. It was striking that some banks are seeking to develop internal approaches for credit risk but remain content with analytical approaches to operational risk based on the basic indicator approach. There should be scope, through the implementation of the expected revised Basel standard on operational risk, to encourage development of operational risk standards within banks that is not limited to the internal controls and IT environment.

Controls, Audit, Accounting, Disclosure and Transparency (CPs 26 to 28)

42. There is a strong emphasis and attention on internal control, compliance and audit throughout supervisory processes. The effectiveness of the three lines of defense is a key area of supervisory focus. On the external audit front, CBRC has established requirements on the qualification and independence of external auditors, to mandate rotation of audit firms, and to strengthen the communication between supervisors and auditors. However, CBRC does not have the direct power to reject or rescind the appointment of the external auditor who is deemed unfit to perform a reliable and independent audit. There continues to be a need to increase audit oversight and quality review of the audit of small-to-medium sized banks.

43. Accounting, disclosures and auditing standards in China are substantially in line with the international standards, but there is room for more information disclosure on the banking sector. All banks are required to prepare audited financial statements. Listed banks, which account for close to 80 percent of total banking system assets, have appointed international accounting firms as their external auditors, and their accounting and information disclosures are generally comprehensive. CBRC has progressively enhanced its banking system disclosures in its annual reports and website. Given the size and complexity of the banking sector, there is room for more disclosures on aggregate statistics and risk indicators for the overall banking industry to facilitate a better understanding among market participants, analysts, and the public of the risk profile of and issues affecting the financial system in China.

Abuse of Financial Services (CP29)

44. Both the regulatory framework and supervisory practices have continued to develop since the last assessment but some gaps still remain. An important initiative since the last assessment has been the establishment of the Anti-Money Laundering (AML) JMC. This body has been a valuable cross-body authority to consider and develop policies and strategies in respect of Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) issues. Cooperation between the PBC and the CBRC is also strong at a policy level and the quality of the working relationships supporting this dialogue is very strong. Nevertheless, until recently, the PBC and CBRC have not focused on information exchange or coordination with respect to findings or concerns with respect to individual institutions. The recent decision for the CBRC and PBC AML Bureaus to conduct joint on-site examinations is very welcome and can be expected to yield valuable results and insights for both authorities. Regulatory guidance, while extensive, should be improved by broadening of requirements related to Politically Exposed Persons to domestic individuals as well as foreign persons. Second, requirements should be enhanced in relation to banks' obligation to identify the ultimate beneficiaries of transactions. The authorities are encouraged to reconsider the calibration of the severity of the fines permitted under the AML Law and a more explicit linkage between multiple offences and repeat offences, and additional measures being imposed by the CBRC, would be powerful.

E. Authorities' Response to the BCP Assessment

45. The CBRC welcomes and supports the BCP Assessment. It has taken the assessment as an opportunity to reflect and evaluate the effectiveness of China's banking regulation and supervision against international standards. The assessment team demonstrated admirable professionalism and dedication. The CBRC appreciates their hard work, and the opportunity to provide the following comments on the assessment.

46. Since the previous assessment, the CBRC has improved prudential framework, undertaken internal supervisory structural reform, enriched supervisory tools, and enhanced supervisory effectiveness by benchmarking against international standards. These achievements and progress have been largely recognized in the assessment report. The assessment concludes that the banking supervision in China is broadly aligned with the BCP.

47. There are a number of issues in the assessment for which the CBRC would like to provide further clarification. The report identifies that the operational independence of the CBRC may be compromised due to the fact that the CBRC's decisions could be overturned by the State Council. However, the CBRC does not see this as an independent concern that would compromise its independence or supervisory effectiveness. Pursuant to the legislation regime established by *the Legislation Law*, only when the regulations or rules issued by an agency violate laws and/or administrative regulations or are in conflict with those issued by other government agencies, may the State Council alter or annul such regulations or rules that are deemed inappropriate. This institutional arrangement has facilitated the establishment of checks and balances which the CBRC and other agencies are subject to and helped maintain the soundness and consistency of the legal system in China. In practice, the State Council has never altered or annulled any regulations or guidelines issued by the CBRC.

48. The assessment report also indicates that the CBRC's current budgeting and headcount arrangements may stifle the CBRC from performing its role effectively. In recent years, the CBRC has continuously improved the professionalism and efficiency of its supervisors by conducting internal supervisory structural reform, refreshing supervisory techniques, leveraging information technologies and intensifying training efforts. However, the CBRC acknowledges that, like many banking supervisory agencies around the world, it faces challenges in terms of supervisory resources given the growing size and complexity of the banking sector. The CBRC will strengthen the communication and cooperation with relevant agencies to obtain more staffing and budgetary support, so that it is able to retain high-caliber supervisory staff and better maintain the soundness and safety of the banking sector.

49. The 2012 Core Principles for Effective Banking Supervision fully embodies the post-crisis international consensus on strengthening banking supervision and places more emphasis on risk management. With constant commitment to the prevention of credit risk, the CBRC has required banks to step up the disposal of NPLs, make adequate provisions and increase their resilience against risks. Currently, as banks in China are mainly engaged in deposit-taking and lending business, the risks facing the banking sector are controllable on the whole. In addition, the CBRC pays close attention to cross-sectoral financial risks, requiring banks to apply look-through principle to cross-sectoral financial activities and shorten the chain of transaction. It will also work with relevant agencies to issue harmonized supervisory rules on asset management activities and push the business back to its intended purpose. The assessment report acknowledges that the CBRC has played a major role in the impressive progress that banks have made in improving their risk management, while identifying a number of areas for further improvement. Although the CBRC's view on the overall risk profile and credit risk level of China's banking sector is to some extent different from that of the assessors, the CBRC concurs that banks should further improve their group-wide risk management and fully take into consideration the interactions between various types of risks. Meanwhile, the CBRC will continue to enhance its capability in evaluating banks' risk profiles and risk management processes together with the increase in size and complexity of the Chinese banking sector.

50. It is also identified in the report that transfers of significant ownership and control through indirect holdings remain outside of CBRC purview. The CBRC has been conducting effective supervision on ultimate beneficiary owners according to the relevant supervisory requirements in *the Banking Supervision Law, the Company Law and the Implementation Rules on Administrative Licensing of Chinese Commercial Banks*, etc. The CBRC is able to monitor the change of ultimate beneficiary owners via formulating institutional overviews, requiring regular submission of relevant information, on-site examinations, interviewing staff, and reviewing documents and takes regulatory measures as deemed necessary. With a view to increasing shareholder transparency, the CBRC is accelerating the effort to optimize the rules governing bank shareholders that will further strengthen the supervision over bank shareholders as well as changes of de facto control from approval to exit.

51. The assessment report has proven to be valuable and rewarding in generating insights and suggestions that will contribute towards the improvement of banking supervision in China. The CBRC appreciates the recommendations made in the assessment, and will take actions on those that are considered appropriate and applicable. The CBRC will continue to draw on international supervisory experience to further optimize China's banking supervision. In the meantime, the CBRC hopes to deepen and broaden the exchange and cooperation with international financial organizations, so as to contribute towards the enhancement of the resilience of the global banking system.

Table 1. China: Summary Compliance with the BCPs

Core Principle	Comments
1. Responsibilities, objectives and powers	<p>The legal framework clearly establishes CBRC responsibilities and also defines the objectives for banking regulation and supervision, granting CBRC powers to authorize banks, regulate, and conduct ongoing supervision and undertake corrective actions to address safety and soundness concerns. Although the powers to access parent companies and their affiliates are not explicitly stated in the legal framework, CBRC has in practice the powers to require information on significant shareholders as it deems necessary.</p> <p>The primary objective of banking supervision from a legal perspective, is to promote the safety and soundness of banks and the banking system. This is set out in law, as is a subsidiary objective whereby the CBRC is required, "towards the objectives" of stability and soundness, to protect fair competition in the banking industry as well as to promote the competitiveness of the banking industry.</p> <p>Hence, CBRC strategy and objectives include market and economy development considerations, support toward internationalization of Chinese enterprises and in particular preferential treatment to SMEs. Assessors did not however find concrete evidence that CBRC has jeopardized its primary mandate of safety and soundness in the pursuit of those objectives. Nevertheless, the assessors also acknowledge that CBRC is acting in a context where references within the Commercial Banks Law to developmental considerations for banks when conducting their business might result in additional pressures, in time of</p>

Core Principle	Comments
	stress, for both banks and supervisors to prioritize those considerations over safety and soundness concerns.
2. Independence, accountability, resourcing and legal protection for supervisors	<p>The CBRC has a legal basis for independence but not in operational terms leading to the potential for it to fail to execute its legal mandate and ensure that soundness and stability considerations are the primary motivation of the CBRC's work. Factors contributing to this potential outcome include the fact that the CBRC's decisions can be overturned by the State Council, and the fact that there is no requirement to disclose publicly the reasons for the dismissal of the Chair of the CBRC. Although the CBRC has confirmed the central importance of soundness and stability in its work, the assessors are concerned that the CBRC's independence is sufficiently compromised to call into question whether the supervisor would always be able to act on its primary, stability, objective, particularly if government policies, such as growth and social protection, conflicted with prudential considerations. Resource constraint is another mode of stifling a supervisor from performing its role effectively. The CBRC has autonomy over neither its staffing numbers nor its organizational design. The financial sector growth does not require a linear increase in resources, but the growing complexities and interconnectedness of the system, which includes four Global Systemically Important Banks (GSIBs), create a significant risk that the CBRC's supervisory oversight will be impaired thus creating the potential for system-wide vulnerabilities to emerge. While the CBRC is to be highly commended on enhancing its specialist skillsets, refreshing its supervisory techniques, and adapting its tools with insight and creativity, the complement of staff has been static for a decade and key staff are increasingly attractive to and attracted by industry opportunities. Increased resources, in salary scale and staffing for the more specialist fields, is an urgent need.</p>
3. Cooperation and collaboration	<p>Legal and regulatory provisions, as well the arrangements currently in place, provide for a sound framework for cooperation and collaboration with relevant domestic authorities and foreign supervisors, reflecting the need to protect confidential information. Cooperation and collaboration arrangements are in place and seem to be functioning as envisioned by the authorities.</p>
4. Permissible activities	<p>The permissible activities for banks operating in China are clearly defined and the use of the word "bank" in names is controlled, with stringent punishment for the use of the word bank or deposit taking by unauthorized entities.</p>
5. Licensing criteria	<p>Powers are in place for CBRC to set criteria and reject licensing applications. CBRC licensing processes encompass the assessment of the ownership structure, including the fitness and propriety of Board members and senior management, as well as feasibility study, financial projections, internal controls, risk management etc. Prior consent or non-objection from the home supervisor is required in the case of foreign banks.</p> <p>CBRC licensing framework has been mostly used in the conversion of rural cooperatives into rural banks, as well as in the establishment of operations of foreign banks in China. Since 2014, fully private Chinese banks have been allowed into the system, which can significantly increase the complexity of the analysis necessary to ensure that the assessment of the ownership structure and</p>

Core Principle	Comments
	governance of the wider group do not impose undesired risks to the bank and the banking system.
6. Transfer of significant ownership	<p>CBRC has the power to review and reject any proposal to transfer significant ownership above 5 percent held directly in existing banks to other parties. The legal framework, nevertheless does not require authorization for changes of de facto control, i.e. controlling interests held indirectly or circumstances where although holdings are below five percent, can entail significant influence.</p> <p>CBRC collect through various means information on significant holdings in banks. Nonetheless, there is no systematic process for regularly receiving/collecting information on names and holdings of all significant shareholders or those that exert controlling influence.</p> <p>In addition, the legal framework, regulations and procedures do not require Chinese or Rural (i.e. domestic) banks to notify CBRC as soon as they become aware of any material information which may negatively affect the suitability of a major shareholder.</p>
7. Major acquisitions	Investments and acquisitions by banks are tightly controlled in China. CBRC requires approval of all acquisitions and investments. Banks are not allowed to invest in or acquire broker dealers, trusts, non-bank financial institutions or commercial enterprises unless prescribed by the State Council. So far pilots for investments asset management, insurance, leasing and finance companies have been established and are subject to specific approval. With the increasing sophistication of the Chinese banking system and expansion abroad, CBRC should ensure that is prepared to properly assess joint ventures and other strategic investments that banks may consider.
8. Supervisory approach	The CBRC plans and executes a high quality supervisory approach. Effective use is made of broad sources of information and the CBRC's supervisory approach seeks to be forward looking and responsive to systemic issues, focusing on key emerging risks and trends such as the provision of wealth management products and interbank activity. Assessing the resolvability of banks is one field which is still work in progress.
9. Supervisory techniques and tools	The CBRC's supervisory practices are of high quality and continue to develop. While the supervisory approach is more balanced towards the off-site (OSS) techniques, there is good use made of the on-site examinations and there is good coordination between the on and off-site departments and bureaus. Since the last assessment there has been intensive investment in the quality of the supervisory data and analytical systems and a refreshing of the analytical methodologies. Supervisory expectations are clearly communicated to banks and are followed up. There is scope for further development in the use of supervisory judgment and proactive supervisory actions.
10. Supervisory reporting	The CBRC has put extensive efforts into its supervisory reporting regime and enhancing the analytical systems that depend on it. There has been an almost wholesale overhaul of the reporting data and considerable care is taken, using on and off-site methods, not only to ensure that the data received is reliable, that banks are accountable for the information they provide, but also to ensure

Core Principle	Comments
	that the CBRC continues to obtain the data that is most relevant for its evolving supervisory tasks.
11. Corrective and sanctioning powers of supervisors	CBRC has a range of powers that enables early action to address unsafe and unsound practices and has exercised them extensively over the last few years, having at its disposal several tools to enforce corrective actions. The deposit insurance fund has been established in 2014 but has not been accessed thus far.
12. Consolidated supervision	The CBRC has refreshed its practice in consolidated supervision, and is starting to reap the benefits. Priority is placed on the knowledge of intra-group and related party connections, exercise of influence over a group, the structure, risk profile, and risk management of banking group. The CBRC is increasingly probing groups in terms of group activities, risk management and strategy. With the advent of less straightforward banking group structures, however, it is essential for the supervisor to consider not only the internal group structure and activities but activities and entities in the wider group that could have an impact on the banking entity and its group. Continuous monitoring of the wider group structure and activities is needed, including stronger notification and approval powers for the CBRC. More attention is needed on cross-sectoral developments, such as the growth of WMPs.
13. Home-host relationships	CBRC has made significant effort to improve its home-host relationships during the last few years including increasing the number of MoUs in place. In particular, the recent establishment of regular colleges for the G-SIBs has enabled CBRC to reach out more effectively to a wider range of host supervisors. Recovery plans have been put in place.
14. Corporate governance	<p>CBRC has progressively updated its corporate governance guidelines, keeping pace with international developments. Given the diversity in scale and complexity of banks, the policy intention is to adopt a proportionate approach with the large/listed banks being subject to the highest requirements while some flexibility is accorded to the smaller ones such as the rural banks.</p> <p>On supervisory practices, there is a clear and consistent emphasis on assessing corporate governance of banks across CBRC's onsite examinations and offsite surveillance, and the assessment constitutes one of the key components of the supervisory ratings of banks.</p> <p>The current regime for corporate governance is based on a combination of various guidelines issued by CBRC and CG Rules for Listed Companies issued by CSRC. While they are rather comprehensive taken together, there are areas that can be enhanced. For instance, there should be clearer requirements on independence of the nominating committee and remuneration committee in respect of non-listed banks. There should also be explicit requirements for risk management committee to be chaired by, and bear a majority of, independent directors.</p> <p>Internationally, there are ongoing developments as regulators continue to enhance their CG regime and supervisory processes in this respect. For such a large and growing banking system in China, there are benefits in having consolidated, clear and concise guidelines in line with international standards to</p>

Core Principle	Comments
	<p>ensure that CBRC's supervisory expectations are well understood, and to establish a clear minimum standard for the smaller and less complex banks in line with the proportionate approach taken.</p>
15. Risk management process	<p>While much of banking in China is lending and deposit taking, the market is complex by virtue of its scope and diversity, and banks are getting into new areas of lending and other activities, in response to competition and changes in macro-economic environment. There is also an increasing contribution from the small-and-medium sized banks to the banking system over the past years.</p> <p>Since the previous assessment, there has been significant progress in the banks' risk management capabilities. The five large banks have moved on to adopting advanced approaches for capital measurement, and internal capital adequacy and assessment process (ICAAP) and stress tests have become an important part of their risk management. For the other large and medium sized banks, while their risk management capabilities may vary depending on the scale and complexity of activities and risk profile, their management of individual credit risks, market risk, liquidity risks and operational risk have also evolved over time.</p> <p>CBRC issued the Comprehensive Risk Management Guidelines in September 2016, and have been in discussions with banks for months prior to that. Full enterprise-wide risk approaches that integrate strategy setting, monitoring, management and stress testing in ways that consider interactions among risks are challenging, particularly for banks with business activities across geographical regions, with diverse products or non-standard credit posing different types of risks. Some banks are still working on fully complying with the comprehensive risk management guidelines, addressing challenges in IT systems, aggregating non-standard credit, overseas exposures, etc. Assessing whether the banks are fully effective in adopting enterprise-wide risk approaches and fully identify, monitor and manage the risk interactions should continue to be a focus area of supervision for CBRC.</p> <p>CBRC has thus far required only the four globally systemically important banks to prepare and submit recovery plans annually for review. There is a need to extend this requirement to the other large banks, in particular those that CBRC assess to be systemically important in the domestic market.</p> <p>In line with the progress towards adopting enterprise-wide risk management approach, CBRC and the banks should further develop their stress testing capabilities, and enhance the robustness of stress testing programs, including stress scenarios design, stress parameters and assumptions, stress testing techniques and interaction of risks under stress.</p>
16. Capital adequacy	<p>China has implemented Basel III, setting higher requirements for CET1 and leverage ratio. Capital is calculated on a solo and consolidated basis and CBRC has the authority to impose additional capital requirements on individual banks, as deemed necessary. The CBRC is to be commended for requiring, in principle, the ICAAP to be implemented for all banks, in a proportionate basis. Domestic systemically-important banks (D-SIBs) methodology and regulation are under development.</p>

Core Principle	Comments
17. Credit risk	<p>Credit risk is the most significant risk factor in the Chinese banking sector. CBRC's offsite surveillance has benefitted from enhanced data gathering and information systems, and it identifies and monitors credit risk trends and vulnerabilities of banks for further action. Numerous onsite examinations have been conducted on credit risk.</p> <p>On the other hand, there has been an increase in the scale and complexity of the banks' credit risk origination activities since the previous assessment, including a shift towards non-standard credit activities such as investments in structured products, off-balance sheet activities, interbank investments, etc. Various guidelines and consultation papers were issued by CBRC in late 2016, setting out important requirements and proposed policies to address these issues that have emerged in recent years.</p> <p>CBRC has made commendable efforts aimed at addressing these challenges and containing specific risks. Given the large number and the diversity of banks and the increasing complexity of activities, it is challenging to ensure that these supervisory expectations have been effectively communicated to all banks across all regions and implemented effectively by them on a timely basis. The fact that banks needed reminders and scrutiny from CBRC to subject these activities to consistent credit risk measurement/management and regulatory requirement also suggests that there is room for banks to have a better appreciation of risk principles and to be more robust and comprehensive in identifying, monitoring and managing bank-wide credit risks.</p> <p>Banks' compliance with these recently issued guidelines and proposed policy positions, and more importantly, their ability to evaluate, monitor and manage overall credit risks comprehensively should continue to be the focus of CBRC's supervisory activities.</p> <p>Most regulators have issued broad supervisory guidance on credit risk management. Given the size and complexity of the banking sector, CBRC should consider developing a comprehensive guidance on credit risk management in line with international standards to ensure that its supervisory expectations and minimum standards are well understood.</p>
18. Problem assets, provisions, and reserves	<p>CBRC has taken a lot of efforts, through offsite surveillance and onsite examinations, to ensure that banks classify loans correctly and maintain provisions in line with accounting and regulatory requirements. Industry representatives that assessors met supported the view that loan classification and provisioning have been the focus of CBRC's supervision and external audit in recent years.</p> <p>There is a need for CBRC to continue its supervisory focus in this area, given the strains that have emerged in several highly indebted corporate sectors coping with overcapacity. It is particularly important to review the current loan classification requirements permitting the use of collateral in influencing NPL classification. While the impact of collateral in NPL classification currently affects only a small proportion of total loans, based on CBRC's estimate, permitting such practice makes it difficult to properly assess the increase in credit risk at individual bank level and at a system-wide level. Also, in those cases where collateralized loans past due are not in fact classified as NPLs, it could also</p>

Core Principle	Comments
	<p>potentially result in lower provisions being held under CBRC's minimum requirements (requirements as mentioned in EC 7).</p> <p>Likewise, CBRC should review the requirement permitting loans granted to small enterprises to be classified as NPL only when they are more than 180 days past due. The review should assess whether this practice results in slow downgrading of problem loans and delays the detection of increase in credit risks in this segment.</p>
19. Concentration risk and large exposure limits	<p>CBRC has enhanced its supervision of concentration risks and monitors concentration risks of banks by industries, geographies, corporate groups, etc. Banks are required to include significant risk concentrations in their stress testing programs for risk management purposes.</p> <p>On large exposures, it remains that (under the Company Law) entities with common local government ownership are not considered connected parties by virtue of local government ownership alone. In order for two parties to be deemed as connected, at least one additional relationship has to exist and in September 2016 the CBRC clarified that there should be a consideration of "economic interdependence" between the two parties in making a determination.</p> <p>Since 2014, exposures to banks are subject to a regulatory limit of 50 percent of a bank's tier 1 capital. This appears excessive, in view of the lower inter-bank limits and inter-G-SIB limits as set out in the BCBS large exposures framework which will take effect from 1 January 2019.</p>
20. Transactions with related parties	<p>As in the previous FSAP assessment, while the definition of related party is comprehensive, it does not include related banks, and ownership by the state government is not treated as a trigger for related party reporting, limits or approvals. Thus, in theory, a commercial bank owned by the local government can lend to local government-owned entities without being covered by the extra due diligence required for related parties.</p> <p>The Related Party Transactions Rule also sets a limit on the aggregate exposures to all related parties of 50 percent of the bank's capital, and hence are not as strict as the allowable large exposure limit for a single counterparty or groups of connected counterparties (EC6).</p>
21. Country and transfer risks	<p>Country and transfer risk exposures at banking system level have increased slightly over the past few years, and are expected to increase further as Chinese banks expand their presence overseas or finance more overseas projects.</p> <p>Since the issuance of Country Risk Guidelines in 2010, banks now have better appreciation of country risk and many have included country risk in their risk management policies and procedures, including risk limits and stress testing.</p>
22. Market risk	<p>Sound regulations are backed up by good quality supervisory work in terms of on and off-site analysis. The CBRC should be well placed to implement the revised Basel market risk standard that has followed the fundamental review of the trading book. Looking forward, however, the CBRC should continue its path in building its market risk capacity. While there is, at present, only a relatively</p>

Core Principle	Comments
	weak case for banks to develop their trading and market risk activities further, conditions are likely to change over time.
23. Interest rate risk in the banking book	The CBRC has worked to meet the challenges of interest rate liberalization and is currently enhancing its scenario and shock analysis on a pilot basis. Responding to recommendations from the last assessment, the CBRC has enhanced its resource specialization in respect of interest rate risk—there is a specialist team—and routinely analyses data to identify outliers.
24. Liquidity risk	The CBRC approach to liquidity risk supervision is more sophisticated and intense than at its last assessment. As with other related risks—market risk and interest rate risk—the CBRC has developed a pool of specialist resources. All banks with assets of no less than RMB200bn are subject to the LCR and this represents approximately 90 percent of the assets of the banking system. The strengthening of liquidity supervision is particularly welcome given market developments, as lower tier banks are becoming increasingly dependent on wholesale funding and such potential vulnerabilities need to be monitored closely and acted upon at an early moment as necessary.
25. Operational risk	There is a considerable variation in the sophistication of banks' approach to operational risk. As the less complex banks expand their businesses, the challenge for them, as the CBRC is fully aware, is to develop their approach to operational risk in a commensurate manner with their growth.
26. Internal control and audit	CBRC has a strong supervisory focus for banks to maintain a control environment that is commensurate with the risk profile and scale of their business activities. It has put in place requirements for banks to ensure the independence and authority of the head of internal audit and head of compliance, and it pays close attention to the internal control systems and the effectiveness of the three lines of defense.
27. Financial reporting and external audit	<p>Various rules and guidelines have been issued to prescribe the required qualification and independence of external auditors, mandate rotation of external audit firm, and to strengthen the communication between supervisors and the external auditors. Accounting and auditing standards are now substantially in line with international standards.</p> <p>According to CBRC's estimates, listed banks, which account for about 76 percent of total banking system assets, have appointed international accounting firms as their external auditors. The Chinese Institute of Certified Public Accountants (CICPA) conducts audit quality review of the accounting firms, with greater focus on the audit of listed corporates, including listed banks. There continues to be a need to increase oversight of the audit of small-to-medium sized banks.</p> <p>As indicated in EC6, CBRC does not have the direct power to reject or rescind the appointment of an external auditor who is deemed unfit to perform a reliable and independent audit. While CBRC has demonstrated that in practice it was able to indirectly remove the external auditors by recommending the banks to do so, the lack of direct legal power is, nevertheless, not in compliance with Essential Criteria 6.</p>

Core Principle	Comments
28. Disclosure and transparency	<p>The accounting disclosures of banks are in line with international standards. Disclosures by listed banks, which constitute about 76 percent of total banking system, is comprehensive. In addition, CBRC has issued additional information disclosure requirements on banks, and the scope and content of information and the level of details required is commensurate with the risk profile and systemic importance of the banks.</p> <p>Given the size and complexity of the banking sector, there is room for more disclosures on the aggregate statistics and risk indicators for overall banking industry to facilitate a better understanding among market participants, analysts and the public of issues affecting the financial system. For instance, this could entail providing more detailed breakdown of balance sheet structure of banks and their risk profiles including liquidity profile, deposit composition, breakdown of loans, concentrations, etc. This can possibly be done with collaboration between PBC and CBRC.</p>
29. Abuse of financial services	<p>Both regulatory framework and supervisory practices have continued to develop since the last assessment but some gaps still remain. Regulatory standards have been enhanced and policy coordination across institutions has been supported by the AML JMC. The working relationship between the PBC and CBRC is a particular strength. Regulations, though, retain some weaknesses, notably in relation to the treatment of domestic PEPs and the standards and record keeping in relation to identifying ultimate beneficiaries of transactions. Coordination, cooperation and information exchange between the PBC and the CBRC has been lacking in relation to supervisory approaches to individual institutions. The recent decision to conduct joint on-site inspections is very welcome and can be expected to yield many benefits.</p>

Table 2. China: Recommendations to Improve Compliance with the BCPs

Core Principle	Recommendations
1. Responsibilities, objectives and powers	<p>Review the legal framework eliminating from the Commercial Banks Law the reference to developmental objectives.</p> <p>Ensure that all CBRC communication does not mislead banks as to the CBRC's commitment, first and foremost, to safety and soundness.</p> <p>Amend the Banking Supervision Law to explicitly grant CBRC powers to have access to de facto parents and their affiliates.</p>
2. Independence, accountability, resourcing and legal protection for supervisors	<p>Ensure that reasons for dismissal of the Chair of the CBRC must be disclosed publicly.</p> <p>Remove the potential ability for the State Council to over-rule the CBRC's decisions.</p> <p>Widen the CBRC's autonomy over the management of its resources to ensure greater flexibility in numbers and appropriate skillset of staff, salary scales and</p>

Core Principle	Recommendations
	internal organization arrangements, so that staff are available as necessary to meet changing risk profiles within the sector.
3. Cooperation and collaboration	<p>Include into procedures, the need to notify the foreign supervisor in case CBRC is legally compelled to disclose confidential information received from a foreign supervisor.</p> <p>Expand the breadth and depth of data collected from securities and insurance supervisors as needed.</p>
5. Licensing criteria	Review procedures and training as necessary to ensure that CBRC is well equipped to adequately review the ownership structure and governance of the wider group in complex cases in order not to impose undesired risks to the bank and the banking system.
6. Transfer of significant ownership	<p>Amend the legal framework requiring that all de facto changes of control, directly or indirectly up to the ultimate beneficial owner are subject to approval by CBRC thus ensuring that cases of significant influence are subject to CBRC scrutiny and approval;</p> <p>Amend the legal framework to have more explicit and clear powers to have access to information of ultimate beneficial owners and controlling interests;</p> <p>Establish procedures in order to receive periodic information on the names and holdings of all significant shareholders or those that exert controlling influence over a bank;</p> <p>Expressly require all commercial banks to notify CBRC as soon as they become aware of any material information which may negatively affect their suitability as a major shareholder.</p>
7. Major acquisitions	<p>Exercise caution, when authorizing non-banking activities, ensuring that a robust regulatory framework is in place to properly govern such activities, the risks they entail and their implications for the banks, banking groups and the banking system.</p> <p>Review procedures and training as necessary to ensure that CBRC is well equipped to adequately review and assess joint ventures and strategic investments.</p>
8. Supervisory approach	<p>Adopt a more continuous review and updating approach to banks' ratings, ensuring links between ratings and data systems that can facilitate automatic changes to ratings where appropriate.</p> <p>Widen the discretion for use of supervisory judgement in the ratings methodology.</p> <p>Complete the resolvability assessment of domestic systemically-important banks (D-SIBs) when the D-SIB framework has been established.</p>

Core Principle	Recommendations
9. Supervisory techniques and tools	In the course of the continued development of analytical techniques focus on the interaction of individual risks, as well as business strategy and business model analysis.
11. Corrective and sanctioning powers of supervisors	Establish a coordination framework with the Deposit Insurance Fund.
12. Consolidated supervision	<p>Require annual reporting of group ownership structures up to and including natural persons.</p> <p>Conduct a review and mapping of supervisory information to identify what aspects will be of most value to the CBRC from other financial sector regulators and what information the CBRC can provide in relation to groups under CBRC supervision.</p> <p>Coordination and collaboration on cross sectoral regulation of financial activities should be a priority.</p>
13. Home-host relationships	<p>Hold periodic colleges for banks, beyond G-SIBs, which, from a home or host perspective, are considered appropriate.</p> <p>Take a more proactive approach in communicating to home and host supervisory authorities significant findings or supervisory concerns.</p>
14. Corporate governance	<p>To establish a consolidated set of guidelines, bringing in elements of requirements that currently exist in other guidelines and listing rules on corporate governance, confirm consistency with international standards and establish clear minimum standards in implementing a proportionate approach for the smaller and less complex banks. The consolidated CG guidelines should also include establishing:</p> <ul style="list-style-type: none"> - clearer requirements on independence of nominating committee and remuneration committee in respect of non-listed banks. - requirements for risk management committee to be chaired by, and include a majority of, independent directors.
15. Risk management process	<p>Assess whether the banks are effective in adopting enterprise-wide risk approaches and fully identifying, monitoring and managing the risk interactions.</p> <p>Extend the requirement for recovery plan and resolvability assessment to other large banks, in particular those that CBRC assessed to be systemically important in the domestic market.</p> <p>To further develop stress testing capabilities within CBRC and the banks and enhance the robustness of stress testing.</p>
16. Capital adequacy	While continuing focusing efforts on the proper and effective implementation in the five largest banks, a next step should include commensurate efforts toward mid-sized banks, irrespectively if joint stock, city or rural banks.

Core Principle	Recommendations
	Establish a D-SIBs framework.
17. Credit risk	<p>Focus on ensuring that all banks have implemented and complied with the recently issued Comprehensive Risk Management Guidelines, Guidelines on Further Enhancing Credit Risk Management, and the proposed tightening measures on off-balance sheet business activities, and also that comprehensive credit risk management is fully embedded across all banks.</p> <p>Consolidate and develop a comprehensive guidance on credit risk management in line with international standards to ensure that CBRC's supervisory expectations and minimum standards are well understood.</p>
18. Problem assets, provisions, and reserves	<p>Review the current loan classification requirement which permits banks to use good quality collateral to support categorizing loans more than 90 days past due (dpd) as Special Mention, taking reference from BCBS Guidelines on Prudential Treatment of Problem Assets which provide that collateralisation plays no direct role in the categorisation of nonperforming exposures.</p> <p>Review the requirement permitting loans granted to small enterprises to be classified as NPL only when they are more than 180 dpd, to assess whether this practice results in slow downgrading of problem loans and delays the detection of increase in credit risks in this segment.</p>
19. Concentration risk and large exposure limits	<p>In line with moving towards adopting the Basel large exposures framework, review and clarify the application of the criterion for identifying relationships between entities with common local government ownership.</p> <p>- reduce the regulatory limit on a bank's interbank exposures (excluding intraday interbank exposures) to 25 percent of its Tier 1 capital and establish a lower limit of 15 percent of Tier 1 capital on a G-SIB's exposures to another G-SIB</p>
20. Transactions with related parties	<p>Review and bring common ownership of enterprise by local governments into the definition and discipline of related-party transactions.</p> <p>Reduce the limit on aggregate related-party exposures of 50 percent of a bank's capital to a level more consistent with the limits on large exposures.</p>
22. Market risk	<p>Increase on-site oversight of the foreign banks' market risk activity.</p> <p>Further cross-sector benchmark reviews of banks' market risk management should form part of the CBRC's preparation to implement the revised Basel market risk standards.</p>
23. Interest rate risk in the banking book	Use the adoption of the revised Basel standard as a springboard for issuing more extensive guidance to the industry on interest rate risk.
24. Liquidity risk	Ensure close supervision, and impose limits as necessary, on the scale of wholesale funding in banks not subject to the LCR.

Core Principle	Recommendations
	Ensure banks conduct stringent and severe stress tests to consider shocks in relation to features of the market that are becoming more pronounced such as wholesale funding and outflows in WMPs.
25. Operational risk	Promote the development of operational risk standards and awareness within the smaller and less complex banks beyond the perspective of internal controls and IT functions.
27. Financial reporting and external audit	Empower CBRC to reject or rescind the appointment of external auditors who have inadequate expertise or independence, or who do not follow professional standards. Increase audit oversight inspections for audit of small and medium-sized banks.
28. Disclosure and transparency	Consider adopting some of the best practices in other countries to enhance disclosures of aggregate statistics and risk indicators for the overall banking industry, to facilitate a better understanding among market participants, analysts and the public of issues affecting the financial system. For instance, this could entail providing more detailed breakdown of balance sheet structure of banks and their risk profiles including liquidity profile, deposit composition, breakdown of loans, concentrations, etc. This can possibly be done with collaboration between PBC and CBRC.
29. Abuse of financial services	Regulations should be strengthened to ensure that the same treatment is applied to both domestic and foreign PEPs. Requirements should be enhanced to ensure that there are explicit obligations for banks to identify the ultimate beneficiaries of transactions and maintain up to date records that are available for inspection at any time. Coordination, cooperation and information exchange between the PBC and the CBRC should be enhanced and systematized. The CBRC should always be informed of decisions to sanction banks, and the reasons for the decision, at the earliest opportunity. An MoU may be useful but is not essential.

INSURANCE CORE PRINCIPLES

A. Introduction

1. This assessment of insurance regulation in China has been made against the Insurance Core Principles (ICPs) issued by the International Association of Insurance Supervisors (IAIS) in October 2011, as revised up to November 2015. The ICPs apply to all insurers, whether private or government-controlled. Specific principles apply to the supervision of intermediaries. The assessment is based solely on the laws, regulations and other supervisory requirements and practices that were in place at the time of the assessment in December 2016. While this assessment does not reflect new and on-going regulatory initiatives, key proposals for reforms are summarized by way of additional comments in this report. The authorities provided a full and comprehensive self-assessment, supported by anonymous examples of actual supervisory practices and assessments, which enhanced the robustness of the ICP assessment.

B. Overview—Institutional and Macprudential Setting

2. The CIRC is the principal entity responsible for insurance supervision in China. CIRC is a ministerial public service department, which reports to, and carries out administrative functions delegated by, the State Council. CIRC is responsible for supervision of insurance, reinsurance, insurance asset management companies, insurance brokers and agents in China. CIRC is financed by levies on insurers' capital and net retained premiums. CIRC has 36 regional bureaus as well as its head office in Beijing.

3. The supervision of insurance companies in China is largely based on the Insurance Law. Insurers must comply with other acts as well as regulations and rules issued by CIRC. The Insurance Law regulates the organization and conduct of insurance business and prescribes the rights and obligations of organizations and individuals participating in insurance business. China is a member of the IAIS, but is not a signatory of the IAIS Multilateral Memorandum of Understanding (MMoU) on Cooperation and Information Exchange.

Industry Structure and Recent Trends

4. In 2015, the Chinese insurance market was the third largest in the world. Total industry premiums were 3.6 percent of GDP and total assets amounted to RMB 12.3 trillion. Total gross insurance income of RMB 2.4 trillion was recorded in 2015. As of the end of 2015, there were 75 life insurance and 74 nonlife insurance companies in the market, among which 52 were domestic companies and 22 were "foreign invested" companies.

5. Life insurance accounted for 56 percent of gross premiums in 2016, typical of an advanced economy. Participating business accounts for roughly half of the market as it has provided a reasonably consistent and stable profit margin for the insurers and offers the possibility of an enhanced return to the policyholders. Investment-linked insurance is not a mainstream

product in China and only accounts for a miniscule fraction of the premium income of China's life insurance sector.

Table 3. China: Insurance Penetration in Selected Countries, 2015

	Life		Non-Life		Total		Share of World Market	Premium Volume
	Percent of GDP	Per Capita (USD)	Percent of GDP	Per Capita (USD)	Percent of GDP	Per Capita (USD)		
China	1.9	153	1.6	128	3.6	280	8.5	386,500
Japan	8.3	2,717	2.5	836	10.8	3,554	9.9	449,707
India	2.7	43	0.7	11	3.4	55	1.6	71,776
Russia	0.2	15	1.2	102	1.4	117	0.4	16,801

Sources: Axco Global Statistics, SwissRe, and CIRC.

Table 4. China: Premiums Written in 2016

	Life Including Personal Accident and Healthcare	Non-Life	Total
Premium (millions of renminbi)	2,223,461	872,450	3,095,911
Premium (millions of US dollars)	334,633	131,304	465,937
Percent of total market	71.8	28.2	100

Source: Axco Global Statistics.

6. In 2015, motor insurance accounted for over 73 percent of total property and casualty (P&C) premiums. The second largest premium line, commercial property, has seen more modest growth. The underlying reason for China's consistently strong non-life premium growth is the surging number of private cars, which rose by over 20 percent a year between 2003 and 2015. Personal Accident and Healthcare Insurance account for close to 14 percent of premiums written. This type of insurance may be written by both life and non-life insurers.

7. China's life and non-life insurance market are highly concentrated. The top 10 insurance companies account for nearly 76 percent of Gross Premiums Written. With the exception of American International Assurance Company, life insurance business is not open to foreign companies except through joint ventures where the foreign shareholder may have up to 51 percent of the equity. The non-life business is also highly concentrated and dominated by People's Insurance Company of China Property and Casualty Company Limited (33.4 percent), Ping An

Property and Casualty Insurance of China (19.4 percent) and China Pacific Property Insurance Company (11.2 percent).

8. Distribution channels are mostly traditional, with the majority of sales being transacted through agents. In China, the insurance distribution system comprises insurance agents, insurance brokers, direct sales (by insurers), and emerging channels such as the internet. Chinese laws make a clear distinction between insurance agents and insurance brokers: agents act on behalf of insurers, while brokers act on behalf of policyholders. Specifically, insurance agents are institutions or individuals who, in exchange for commissions from insurers, engage in insurance activities on their behalf within the scope so authorized. Among agents are specialized insurance agencies which are exclusively engaged in agency distribution, and ancillary insurance agencies engaged in agency distribution concurrently with other businesses. The *Insurance Law* provides that an individual agent may only sell life insurance products on behalf of one life insurer, while insurance agencies are not subject to this restriction. Insurance brokers, on the other hand, are institutions that provide intermediary services to facilitate prospective policyholders and insurers in concluding the insurance contract. They act in the interest of policyholders and collect fees from them in accordance with the law.

9. The share of the bancassurance channel is growing: it accounts 40 percent in life but is far less significant in non-life. The agents are supported by relatively high levels of commission. The bank channel went into a temporary decline from 2012 as a result of regulatory restrictions and the falling competitiveness of life policy returns relative to other investments, but is now growing again, boosted by the increasing number of banks that have bought shares in their own insurance companies. Insurers are simultaneously increasing both the size and productivity of their agency forces, helped to a large extent by tablet computers which allow illustration, application and payment to be concluded in a single meeting. The fastest growing channels are telemarketing, cross-selling and the mobile internet, which increasingly work together in an "online-to-offline" business model.

10. The compulsory insurance lines in China are motor third party liability, carriers' liability and travel agents' liability. In line with government objectives on the development of liability insurance, local governments also encourage and guide insurance companies to promote liability insurance for environmental pollution, food safety, medical accident, campus safety and other areas, but these are not compulsory. Because the compulsory classes are intended to serve social purposes, insurers are sometimes required to pay deserving claims regardless of their strict policy liability.

11. The market includes three main insurance pools. The China Residential Earthquake Insurance Pool (CREIP) was created by 45 primary insurers in 2015. The pool is led by People's Insurance Company of China Property and Casualty Company Limited which was appointed as the executive office with responsibility for product design, premium rating and risk diversification. The scheme will cover damage by earthquakes of magnitude 4.7 and above, fire following, tsunami and subsidence or landslide caused by earthquake. The CREIP has developed model products that

guarantee a basic level of protection, have a wide coverage, and are both affordable and appealing, with urban and rural residential houses as the object of insurance.

12. The China Agricultural Reinsurance Pool (CARP) commenced operations in 2015 under the administration of China P&C Re. Although 23 direct insurers are also members of the pool, China Re was expected to write around 80 percent of the pool's estimated premium income of RMB 3.7 billion in 2015. CARP writes around 50 percent of total agricultural reinsurance premiums and will be the main vehicle for agricultural reinsurance in China. The purposes of CARP are: (1) to ensure that agriculture insurance can be ceded at an appropriate price (responding to experience with international reinsurers which stopped accepting business or raised their rates after major natural disasters in China); and (2) to provide reinsurance support to agricultural policies that are encouraged by the government such as price insurance, special crop insurance and fishing insurance, which international reinsurers do not reinsure.

13. Agriculture insurance in China is developed through a combination of government guidance, market-based operations, independent and voluntary participation, and joint promotion by all stakeholders. The State encourages local people's governments to establish a local treasury-supported mechanism for pooling of catastrophe risks covered by agriculture insurance.

14. A total of 29 insurers and reinsurers (including Swiss Re, Lloyd's China, SCOR and Hannover Re) participate in the China Nuclear Insurance Pool (CNIP), which was established in 1999. Because the pool lacks the legal capacity to issue its own policies, risks are written by individual pool members, but all premiums are ceded to the pool and retroceded to members according to their underwriting capacity calculated by the CNIP board each year. The pool is managed by China Re P&C. Pool members' nuclear risk capacity is limited to 5 percent of their total assets. CNIP writes shares of over 300 nuclear plants worldwide and is said to be the third largest nuclear pool in the world in terms of underwriting capacity.

Key Risks and Vulnerabilities

15. Life insurers are principally exposed to market risk arising from the mismatch between assets and liabilities. For many companies, the long duration of their traditional business exposes them, in case of falling interest rates, to losses due to the rising cost of liabilities. Asset and liability management is hampered by the limited availability of longer maturity investments and hedging instruments, including swaps. High-yielding investments are increasingly attractive in such an environment, as is diversification into foreign investments, but they bring credit and liquidity risks as well as placing demands on fund management expertise. A number of life insurers have been reducing the duration of their liabilities by selling high volumes of short and medium term savings products, sometimes using bancassurance and online channels to sell products that are economically equivalent to bank deposits. This is unlikely to be sustainable, not least because of recent CIRC action to require significantly higher insurance content than the minimal amount that has generally been included in such products.

16. For the non-life sector, there are risks associated with the growth of new business lines. As well-established products become less profitable, partly as a result of increased competition following reform of the market, insurers have been launching new product lines, sometimes achieving rapid rates of growth in new business over short periods, for example in credit guarantee insurance. There is a risk that some insurers will not be equipped to manage underwriting risks that differ significantly from their established lines of business. The development of insurance pools will help to mitigate insurers' exposure to loss due to natural catastrophes.

17. There are risks from growth and rapid change in the insurance sector. Premium income has been increasing at over 20 percent per year, spurred in part by liberalization of pricing, with many individual, often newer, companies growing at rates far in excess of the average. Agency-based selling is competing with low cost online and other innovative distribution channels and continued growth is accompanied by high levels of interest from potential new entrants. Insurers need to adapt business models and develop their infrastructure rapidly. There is some pressure to meet demanding targets for the increased penetration of insurance set by the government through the planning process and State Council strategic objectives for the sector. Nonetheless, innovation in relation to more complex products has been relatively limited and some higher risk and harder to manage life products which have been introduced, such as variable annuities, have struggled for market share.

18. There are operational and reputational risks for insurers, as well as direct risks to customers arising from the current limited penetration and lack of understanding of insurance products. Insurance development has been concentrated over many years in savings products (with guarantees) and compulsory insurance (motor third party liability). There is less understanding of protection products and of savings products where the investment risk is shared, wholly or in part, with the policyholder (as in investment-linked and participating policies). With commission-based agency distribution models, there are risks of mis-selling and poor advice, leading to losses for customers and reputational damage and rapid erosion of market share for insurers. The benefits of extensive use of data and the internet, including improved customer screening and better product pricing, are accompanied by risks that private customer information may be compromised as well as vulnerability to cybercrime.

C. Preconditions for Effective Insurance Supervision

Sound and Sustainable Macroeconomic and Financial Sector Policies

19. There is a developed economic policy framework, which is increasingly aimed at reorienting the economy towards demand-led growth, and there is a policy-making infrastructure in place for the financial sector. A sector-based regulatory framework has been in place since the late 1990s, comprising the CBRC, CSRC, and CIRC. All these agencies fall under the leadership of the State Council, which also provides the mechanism for developing and publishing broad strategic plans for economic sectors, including financial services. For insurance, the most recent such plan was set out in August 2014 in the publication "Opinions of the State Council on

Accelerating the Development of a Modern Insurance Service Industry”, which set out an ambitious program for growth and development.

A Well-Developed Public Infrastructure

20. There is an established framework of commercial laws and judicial system. The legislative framework includes company, bankruptcy and contract laws as well as laws on the protection of consumer rights and property. The judicial system comprises investigation and prosecution services, a courts and penal system, people’s mediation, and lawyer and notary services. China scores relatively highly on the World Bank “Doing Business” assessment of enforceability of contracts and the insolvency process.

21. Accounting and auditing standards are aligned with international standards and practices. The Accounting Law, Law on Certified Public Accountants and Accounting Standards for Business Enterprises (ASBE) include both standards and implementation rules and material on the roles of and responsibilities of Chinese Certified Public Accountant (CPA). Issued originally in 2006, ABSEs are in general based closely on International Financial Reporting Standards (IFRS) and the government is committed to continued alignment. The Accounting Regulatory Department of the Ministry of Finance (MoF) is responsible for issuing ASBEs and auditing standards, which since 2010 have also been based on international standards. The use of IFRS is not permitted for domestic reporting, although companies whose securities trade on the Hong Kong Stock Exchange may and in many cases do choose to use them for reporting to Hong Kong investors.

22. China has a pool of independent and experienced accountants and auditors and a growing population of actuaries, as well as developed professional bodies:

- The Chinese Institute of Certified Public Accountants (CICPA), a member of the International Federation of Accountants, is responsible for formulating the codes and rules of practice of certified public accountants and for supervising their implementation. Although a professional body, CICPA operates under the oversight of the MoF and has inspection and disciplinary powers against audit firms and individual auditors.
- The China Association of Actuaries (CAA), founded in 2007, develops the code of ethical practice for actuaries, organizes educational programs and oversees compliance with relevant codes and rules (the one disciplinary case to date resulted in a warning to a member). It has around 900 fully-qualified members (as at late 2016), comprising life and non-life, consulting actuaries and others practicing in auditing firms. The number is growing by around 100 per year, with an increasing proportion obtaining the Chinese qualification, although many existing full members qualified abroad. The CAA is a member of the International Actuarial Association.

23. Audit firms are licensed and oversight of audit work is undertaken by the MoF and the relevant provincial governmental finance departments. Licenses for individual auditors are issued by provincial CPA institutes. The MoF has powers to inspect companies and may require auditors to provide audit documentation of the company under inspection. The CICPA also has

powers, providing a second layer of oversight. Firms that undertake audits of listed entities are further required to be licensed by the CSRC, which has powers to inspect companies listed in China. China is not currently a member of the International Forum of Independent Audit Regulators.

24. Statistics required by insurance businesses are available from government agencies and professional bodies. Economic and financial data are published by the National Bureau of Statistics, the MoF and PBC. The requirements of life insurers for mortality data in relation to insured lives is met by the CAA, which collates data from insurers and publishes a mortality table, in conjunction with the CIRC. The table relates to 2000–2003 data. A new table based on 2010–13 data is under development and will soon be issued by the Mortality Investigation Office of the CAA.

Effective Market Discipline in the Financial Sector

25. Corporate disclosures are governed by the accounting standards and requirements in relation to the issuance of publicly-traded securities. Company Law sets out basic requirements on the preparation by companies registered in China of audited annual financial statements, which must be made publicly available. For listed companies, the requirements of the listing authorities include extensive disclosure provisions.

Mechanisms for Consumer Protection

26. There are arrangements for the protection of insurance policyholders, including through a funded insurance guarantee scheme. The China Insurance Security Fund (CISF), established under the Insurance Law and managed by a state-owned company under regulations jointly issued by CIRC, PBC, and MoF, provides for policyholder compensation in well-defined circumstances of financial stress, including bankruptcy (see the assessment of ICP 12 in this report). Insurance companies are required to contribute to the fund. As of the end of November 2016, the CISF has a balance of RMB 94 billion, which compares with some RMB 14 trillion in insurance sector total assets. There are also mechanisms for resolving policyholders' complaints. There is also access to a complaints mediation function at the Insurance Association of China (IAC) and to the courts.

Financial Markets

27. China has developed financial markets, although there is limited liquidity in longer term financial assets. The longest maturity, actively-traded government bond is only around 10 years and there are few corporate bonds in issue at that length of maturity or longer. Insurers are increasingly able, subject to continuing CIRC investment allocation limits and foreign exchange controls, to invest in long term bonds outside Mainland China. There is an interest rate swap market, but liquidity is relatively low.

D. Summary

Table 5. China: Summary of Observance with the ICPs	
Core Principle	Comments
1. Objectives, Powers and Responsibilities of the Supervisor	Since the FSAP conducted in 2011, CIRC has greatly increased its efforts to ensure a sound regulatory and supervisory environment in China, demonstrating its commitment to turning broad objectives into operational achievements and strengthened supervision. While CIRC focuses in insurance regulation and supervision on the development of safe and healthy insurance markets for the benefit of consumers, the Insurance Law defines two other potentially competing objectives and the detailed mandate and responsibilities of CIRC are defined by the State Council. The priority of policyholder protection in the objectives and mandate of the CIRC needs to be more clearly defined, including in the Insurance Law. Many of the detailed regulatory requirements are either tentative or open to administrative interpretation and take the form of guidance. There is also limited provision for group supervision in primary legislation.
2. Supervisor	The CIRC is in practice operationally independent in the day-to-day exercise of its supervisory functions and is not subject to intervention by the State Council in relation to supervisory decisions (although the State Council can hear appeals against supervisory decisions, it has not done so as yet). However, CIRC relies financially on the regular government budget process for funding and central government human resource processes for staffing, as well as government agreement to its internal structure and organization. CIRC is subject to the overall direction of the State Council in relation to its mandate and functions. CIRC's resources are stretched and will be under increasing pressure from the need to analyze and respond to the developments in licensed companies within the framework of an appropriately interventionist but not yet fully risk-based supervisory system.
3. Information Exchange and Confidentiality Requirements	CIRC has strong and broad based authority to request and exchange information including information on non-regulated related entities and groups. The legislation meets requirements related to dealing with requests quickly, providing information only for a legitimate purpose, ongoing protection of confidentiality, and that information be used only for the purposes specified in the request. CIRC shares information with other authorities as required, under Memorandum of Understanding (MoU) or separate bilateral agreements, where necessary.
4. Licensing	The Insurance Law sets out licensing requirements for insurance and for unlicensed operations. The law clearly states the requirements and covers financial as well as nonfinancial aspects to ensure the implementation of safe and sound operations. During the licensing process, CIRC attaches great importance to the views of overseas

Core Principle	Comments
	regulatory authorities. It requires foreign applicants to provide their supervisors' letter of opinion.
5. Suitability of Persons	CIRC maintains appropriate requirements for the suitability of key personnel. The growth of the insurance market and the demand for highly qualified and experienced management skills should be monitored.
6. Changes in Control and Portfolio Transfers	The legal framework and CIRC's powers ensure that changes in control, broadly defined, are notified to CIRC and that it can prevent changes that could place policyholders at risk. CIRC is well-equipped to address any increase in merger activity in case of industry consolidation.
7. Corporate Governance	CIRC's increased focus on corporate governance in recent years has been reflected in the development of its standards, the introduction of a self-assessment and rating system and increased supervision, including targeted inspections. There are requirements applying to groups. The publication of corporate governance ratings is a potentially powerful tool for improving standards. As in other areas, many of the standards take the form of guidance. The approach is still developing in practice and there is scope to develop the framework for groups and to increase the supervisory focus on the effectiveness of governance, especially at board level, including whether Boards of Directors are instilling appropriate corporate culture. The separation of CIRC's processes for governance from those applying to risk management has facilitated the increased focus on governance, but creates a risk that linkages (and shared areas of weakness) are not identified.
8. Risk Management and Internal Controls	There is an extensive set of standards, although much of them taking the form of guidance. CIRC's approach is being enhanced through the implementation of the Solvency-Aligned Risk Management Requirements and Assessment (SARMRA) framework. Some requirements apply to all, while in other areas CIRC tailors its expectations to the nature, scale and complexity of the insurer. The system is reinforced by the suitability requirements and by reporting to CIRC. There is less coverage of controls or control functions in the group context. There is scope to strengthen requirements on the authority, independence and resourcing of control functions. Standards on outsourcing are limited, reflecting regulatory restrictions, although some outsourcing even of control functions is permitted.
9. Supervisory Review and Reporting	The evolution of Chinese insurance regulation is bringing the market closer to international best practice. Although the CIRC has been working to move to fully risk based supervisory approach using supervisory tools such as China Risk-Oriented Solvency System (C-ROSS) and SARMRA, it is challenged by limited resources and technical capacity in an environment of fast growth in the insurance sector. Prerequisites for effective risk-based supervision are adequate resources, good

Core Principle	Comments
	insurance knowledge and judgment by staff, and strong requirements concerning institutional governance and internal controls. A risk based approach to supervision requires not only changes to supervisory tools, policies and procedures of the organization, but the change of basic supervisory culture.
10. Preventive and Corrective Measures	CIRC has the power to take action against unlicensed activity and the ability to escalate corrective action where a breach has occurred and in the case of solvency breaches can require a plan of corrective action. It can also communicate directly with the board and senior management. It does not have many tools to take preventative action before an administrative breach has occurred, other than through discussion and agreement to inspection/examination findings.
11. Enforcement	The administrative penalty powers include both preventive actions and escalatory actions. Actions may be taken against individuals (e.g., suspension of officers and directors) as well as corporate entities and extend from penalties and suspensions to exercising conservatorship over the insurer in the case of failure to meet solvency requirements. The upcoming major revision of the Insurance Law (started drafting in 2015) will revise and upgrade the relevant provisions, i.e., both the lower and the upper limit of penalties will be upgraded, which has been included in the draft submitted to the State Council.
12. Winding-up and Exit from the Market	The legislative framework provides for a set of circumstances under which CIRC may decide that insurance companies may no longer continue in business as well as legal mechanisms for orderly exit that are likely to deliver a high degree of protection to policyholders. The framework includes a wide range of triggers, including but not limited to inadequate solvency, for CIRC to remove a company's license and criteria for initiating liquidation, although there is no clear point in the framework at which it is no longer permissible for an insurer to continue its business. Policyholders rank high in the order of preference and are eligible, in the case of domestic policyholders, for compensation for losses from the CISF. There is flexibility in practice for CIRC to manage failures, including (with State Council agreement) intervention to recapitalize an insurer using CISF resources, as has occurred in two cases since 2008. The framework has not otherwise been tested in the nearly 20 years of CIRC's existence. Establishing a clear point at which it is no longer permissible for an insurer to continue its business would help to ensure that CIRC is ready (and is seen to be ready) to trigger resolution of a failing insurer without resort to CISF recapitalization, where necessary.
13. Reinsurance and Other Forms of Risk Transfer	CIRC has comprehensive requirements on the reinsurance arrangements of primary insurers, focusing on non-life reinsurance, although the general requirements apply also to life reinsurance. The regulatory approach now relies on risk management requirements, reporting and

Core Principle	Comments
	oversight by CIRC rather than prior approval of individual reinsurance contracts. It is supported by the recently-introduced solvency and related risk management standards (C-ROSS). The introduction of a register system for reinsurers based on credit standing as well as incentives to manage reinsurance credit risk in the solvency framework should ensure that insurers deal only with high quality reinsurers, including foreign companies. CIRC needs to keep its approach and supervisory resources under review as the number of reinsurance companies based in China continues to increase, as CIRC expects.
14. Valuation	There are comprehensive requirements on valuation for solvency purposes which combine the benefits of alignment to accounting standards with requirements to address the specific needs of insurance business. The framework is supported by governance requirements, including required actuarial opinions, risk management requirements and supervisory oversight and enforcement of reserving adequacy. There are also measures, in life insurance, to cap valuation rates. The valuation basis for life insurance is broadly economic, although not fully market consistent. CIRC's objective has been to increase market consistency while avoiding excessive volatility in the valuation and more generally to reflect market conditions and risk management standards in what is not a fully developed financial system. Differences in valuation bases for assets and liabilities, and in particular the treatment of Hold to Maturity investments, mean that the requirements, while comprehensive, are not fully consistent. Simplifications, while appropriate for smaller companies, may lead to inappropriate valuations, including of time value of embedded options and guarantees (TVOG).
15. Investment	CIRC has been significantly liberalizing the requirements on investment of insurance funds and insurers are responding by diversifying from bank deposits and bonds into property, alternative and overseas investments. Across the sector, potentially higher risk investments remain low, although some individual insurers have more aggressive investment strategies and they have been attracting increased CIRC supervisory focus. CIRC has recently moved to tighten investment restrictions in relation to stock market activity by some insurers that has included building controlling interests. CIRC is seeking to balance the benefits of diversification of insurance funds with the need for continuing restrictions, of which there remain many, while expertise in fund management and risk assessment is developing. It is working with insurers and the trade associations in this regard, while also developing the expertise of its own Investment Department. Given the rapid growth of the market, and pressure to accommodate increased use of insurance funds in activities that will support economic growth objectives, CIRC needs to remain vigilant.

Core Principle	Comments
16. Enterprise Risk Management for Solvency Purposes	CIRC has introduced, through the SARMRA framework, an extensive set of risk management requirements, which have already had a significant positive impact on insurer practices. Its integration into the supervisory process and its direct link to overall solvency requirements makes SARMRA likely to become an effective framework for delivering strong Enterprise-Wide Risk Management. The framework is still new and not fully implemented at CIRC or in the processes of insurers. In relation to the ICP expectations, it lacks a full Own Risk and Solvency Assessment (ORSA) requirement (under which insurers would be required to develop their own view, in an integrated manner, of both risk and solvency requirements, which the supervisor can use as an input into its solvency adequacy assessment), even if many of the elements of ORSA are present in the SARMRA framework. While it may be too early for CIRC to require ORSAs at present given the state of development of insurance sector risk management, experience in other countries suggests that an ORSA process can be useful in requiring companies to look at risk and solvency together. Furthermore, by not including explicit requirements on group risk, the SARMRA does not cover all the risks within the scope of the ICP.
17. Capital Adequacy	The new C-ROSS solvency framework is a major step towards a risk-based approach. The combination of Pillar 1 with a Pillar 2 qualitative and quantitative framework, including additional solvency requirements for individual insurers under the SARMRA process, goes beyond the approach of many other countries in linking solvency requirements to the overall supervisory approach. It is likely to incentivize sound risk and capital management. While it excludes an internal model approach, the framework relies on extensive CIRC interventions and is resource-intensive for it to manage. There is also a risk at this early stage that elements of the approach are not embedded by insurers or understood by those using the output. The IRR ratings in particular may be hard to evaluate. The framework is not comprehensive: operational risks are excluded from Pillar 1 requirements, even where quantifiable, although there are data constraints in China. The relatively high requirements on credit risk for offshore reinsurers (where not collateralized), regardless of credit rating, raise concerns that aspects of the framework may not be fully risk-based. The requirements for equity risk appear low. While CIRC policy and practice is clearly to enforce the requirements fully, it will be helpful to clarify its approach to solvency control levels and to ensure the insurance sector is aware of its approach.
18. Intermediaries	Against the background of an increasingly competitive market, with rebating and inducements for policyholders, the incidence of insurance misrepresentation is increasing. The abolition of statutory qualification requirements for insurance agents with effect from 2015 has led to an explosion in the number of people engaged in the business, particularly in life agency. Insurance distribution is not simply about pushing product to achieve a specific growth rate. Policyholders' needs have to be understood and assessed, options identified and appropriate advice

Core Principle	Comments
	<p>given on which insurance companies and products to select. For insurance companies, it is in distribution that relationships and trust are built with agents, brokers, and customers, opportunities identified and created, and products and services sold. Although CIRC has a database, there is a room for improvement to have a more efficient computer system, for example with automated computer runs to check on compliance with each of main requirements (the list of non-compliant firms could not be produced upon request).</p>
19. Conduct of Business	<p>CIRC is continuously regulating the distribution network to encourage innovation, motivate lower premiums, better service and more responsive insurance products while restructuring/redesigning the new solvency regime. These two tasks require a well-planned/ designed road map, highly technical staff and adequate resources. The insurance dispute settlement mechanism has played an important role in timely resolving of conflicts and disputes. CIRC has introduced good rules about problems such as exaggerating the insurance coverage or the returns from insurance products, guaranteeing returns on insurance products with volatile performance and important insurance clauses such as fees and charges in universal insurance or investment-linked insurance. While there are many good requirements in the law, additional provisions are necessary to ensure products sold to purchasers are appropriate to their needs, that any potential conflict of interest are disclosed, and that public information is available to support consumer decisions and the fair treatment of consumers.</p>
20. Public Disclosure	<p>CIRC sets out detailed disclosure requirements of its own, rather than relying on the publication of audited financial statements, although in practice the information to be disclosed is closely aligned and many disclosures are driven by accounting standards. There is not complete coverage of the ICP requirements as disclosures at the insurance group level (and for reinsurers) are limited. Some disclosure requirements, such as technical provisions, claims, corporate governance and Enterprise Risk Management are relatively limited. The implementation of C-ROSS is greatly improving the disclosure of information on solvency. The full impact and effectiveness of these disclosures is yet to be felt and there may be challenges in understanding the basis of the IRR and SARMRA ratings in the early days. However, initial indications are that disclosures are being closely watched, including by brokers and agents.</p>
21. Countering Fraud in Insurance	<p>CIRC focuses on three dimensions of fraud: false insurance companies, false policies specifically in life insurance and false claims. In 2015 and 2016, CIRC has dedicated resources in the inspection department and in the regional insurance bureau available to support efforts against insurance fraud.</p>

Core Principle	Comments
22. Anti-Money Laundering and Combating the Financing of Terrorism	Since the 2010 FSAP, CIRC has conducted effective work, including cooperating with PBC in Anti-Money Laundering (AML), promulgating new AML rules and making AML a part of the risk indicator assessment system of C-ROSS. CIRC enforces regulation and classification-based supervision according to industry characteristics, leverages its understanding about insurance operations and focuses on the research and practice of AML standards in the context of industry characteristics, complementing the role of PBC. CIRC has allocated regulatory resources in a reasonable manner, focusing on the regulation of systemically important companies, companies with high money laundering (ML) risks and high-risk products and regions.
23. Group-wide Supervision	CIRC has established a framework of measures and guidelines that establish comprehensive groupwide supervision of insurance groups. The framework is being applied in practice to all groups and has enabled CIRC to apply a wide range of regulatory standards, including on solvency and capital management, governance, risk management, intra-group transactions (IGT) and disclosure, to insurance groups as well as to carry out oversight of groupwide risks.
24. Macroprudential Surveillance and Insurance Supervision	CIRC uses the extensive data reported by insurers as well as other information and targeted stress tests to monitor the insurance market for significant trends. It draws on macroeconomic data and analysis to identify risks to the sector. The focus is mainly domestic, reflecting the limited international dimension to the insurance sector. CIRC also monitors for systemic risk in insurance products, taking into account the predominance of traditional, and otherwise standard, products in the market and the influence of distribution channels such as bancassurance. While CIRC is already applying enhanced supervision of the G-SII, the framework for macroprudential regulation will be much strengthened next year with the planned introduction of requirements for D-SIIs.
25. Supervisory Cooperation and Coordination	CIRC has been increasing cooperation with other regulators, through the new Joint Ministerial Conference (JMC) arrangements and mainly bilateral arrangements with foreign regulators. Its approach reflects the limited internationalization in practice of the Chinese market to date. There is scope for closer cooperation with the CSRC, to reflect the CIRC's responsibilities for asset management and the importance of insurers as investors in capital markets. In relation to international cooperation, there is scope to update and extend the scope of bilateral supervisory cooperation arrangements and to incorporate supervisory recognition of foreign regulatory regimes, taking into account the recent significant development of the Chinese regime, in areas such as C-ROSS.
26. Cross-border Cooperation and Coordination on Crisis Management	CIRC has powers and processes for addressing an insurance company crisis, including recovery and resolution plans (RRPs) for the one G-SII for which it has groupwide responsibility. Crisis preparedness has been tested, but only by experience of a domestic company in stress. Crisis management planning has not been a focus of cross-border supervisory

Core Principle	Comments
	work, reflecting the limited internationalization of the market, although CIRC has the ability to share relevant information with foreign supervisors. Most focus on crisis management preparedness has been on the G-SII group, which is also the most significant cross-sectoral group. There is a need to ensure that other insurers, some of which may have more significant cross-border operations than the G-SII, are subject to appropriate crisis management preparedness requirements, and that processes are available to manage a cross-border crisis in practice.

E. Recommendations

Table 6. China: Recommendations to Improve Observance of the ICPs	
Core Principle	Recommendations
1. Objectives, Powers and Responsibilities of the Supervisor	<ul style="list-style-type: none"> In the context of the next regular review of the Insurance Law, the authorities review the objectives of the law, with a view to giving CIRC an express mandate to promote the maintenance of a fair, safe and stable insurance sector for the benefit and protection of policyholders (or similar language) to the exclusion of other objectives, functions and responsibilities except to the extent that they are consistent with this primary objective.
2. Supervisor	<ul style="list-style-type: none"> The authorities, in the context of the next review of the Insurance Law, make changes to the law to equip CIRC with the formal and financial independence it will need effectively to administer an increasingly complex regulatory framework, including scope to set its own budget and recruit staff, subject to appropriate accountability.
3. Information Exchange and Confidentiality Requirements	<ul style="list-style-type: none"> CIRC should complete its network of MoUs with key regulators including relevant US states directly, where necessary. CIRC should publish its MoUs, where agreed, and accelerate the process to join the IAIS MMoU.
4. Licensing	<ul style="list-style-type: none"> CIRC should consider making increased use of inputs from foreign supervisors as an alternative proof of compliance on some key licensing criteria.
5. Suitability of Persons	<ul style="list-style-type: none"> CIRC should increase its emphasis over time on competence assessment, in relation to the role of the individual, taking account of the scale and nature of the company's business.
7. Corporate Governance	<ul style="list-style-type: none"> CIRC should develop further its expectations on corporate governance of groups, recognizing the existing significance and likely increasing importance of groups, including financial conglomerates, and drawing on recent IAIS work in this area, as applicable.

Core Principle	Recommendations
	<ul style="list-style-type: none"> • CIRC should develop a set of binding requirements in due course to strengthen existing mainly guidance-based material. • CIRC should develop its supervisory approach over time (recognizing the priority of embedding C-ROSS/SARMRA) to equip supervisors to assess the effectiveness of governance more fully, and to integrate the assessment of corporate governance within the C-ROSS process more completely.
8. Risk Management and Internal Controls	<ul style="list-style-type: none"> • CIRC should continue to strengthen its expectations of control functions (other than internal audit) in relation to independence and resourcing and the scope of their responsibilities. • CIRC should review the need for more guidance or other material on group level risk management and develop standards on outsourcing that would apply to any outsourced activities. • CIRC should develop a set of binding requirements in due course to strengthen existing mainly guidance-based material on risk management, etc.
9. Supervisory Review and Reporting	<ul style="list-style-type: none"> • CIRC should develop stronger centralized oversight of the supervision of groups, by a system of lead supervision with adequate staffing to ensure close and continuous oversight of significant groups and able to see the group wide risks and respond accordingly. • CIRC to develop its supervisory framework to include more emphasis on a risk-based supervisory plan to bring together all the issues and actions on an insurer, including market conduct. This is particularly important in an increasingly competitive market with an expanding number of companies.
11. Enforcement	<ul style="list-style-type: none"> • CIRC should review the general level of penalties to ensure that they are an effective deterrent.
12. Winding-up and Exit from the Market	<ul style="list-style-type: none"> • CIRC should ensure that the regulatory framework specifies a clear point at which it is no longer permissible for an insurer to continue its business, for example where the insurer falls below its minimum capital requirement. • CIRC should whether, given policyholder compensation is available via the mechanism of CISF (although it is not an ICP requirement), the level of protection should be increased to 100 percent in case of compulsory lines of insurance (motor third party liability).
13. Reinsurance and Other Forms of Risk Transfer	<ul style="list-style-type: none"> • Although facultative reinsurance contracts have to be signed before they become effective, CIRC should strengthen requirements on the documentation of reinsurance arrangements to ensure that documentation is signed promptly as far as possible. • CIRC reviews its approach to life reinsurance, recognizing the significant recent growth in use of reinsurance by primary insurers,

Core Principle	Recommendations
	partly in response to the introduction of the new solvency requirements (C-ROSS).
14. Valuation	<ul style="list-style-type: none"> • CIRC should establish an objective and a plan for improving the consistency of valuation requirements across assets and liabilities and longer term, for moving valuation to a more market consistent basis, while continuing to take into account the characteristics of Chinese markets. • CIRC should develop, maybe as part of the plan, elements of the framework where large insurers (for example, Class I under C-ROSS) or those with proven financial controls, to use more sophisticated techniques, such as stochastic valuation of TVOG. • CIRC, in cooperation with other authorities, should complete the implementation of an approach to reserving for catastrophe risk.
15. Investment	<ul style="list-style-type: none"> • CIRC should review its approach, including the balance between regulatory limits and supervisory activity, to higher risk investments including equities, taking account of the 30 percent limit on equity investments that is high for many forms of insurance business and the recent experience with stock market activity of some insurers.
16. Enterprise Risk Management for Solvency Purposes	<ul style="list-style-type: none"> • CIRC should develop an approach to the inclusion of group risks explicitly in the SARMRA framework. • CIRC should extend the SARMRA framework in due course to require insurers to develop ORSAs: these would ideally be prepared as integrated documents setting out the insurer's own view of risk and the related solvency needs; they should be agreed by the Board and submitted to CIRC as required as an input into the SAMRA assessment. • CIRC should consider, after the completion of the first year of SARMRA assessments, how to make the process more risk-based, for example moving to regularly more frequent assessments of Class I or larger insurers and less frequent reviews of smaller companies, at least those with strong SARMRA performance.
17. Capital Adequacy	<ul style="list-style-type: none"> • CIRC should review its approach to intervention in terms of the ICP framework providing for two solvency control levels prescribed capital requirement and minimum capital requirement, establish levels for intervention and publish its approach. • CIRC should review the treatment in the solvency requirements of credit risk on offshore reinsurers and equity risk (in the light of market volatility in recent years).
18. Intermediaries	<ul style="list-style-type: none"> • CIRC should review the level of resources that it currently applies to market conduct and intermediaries in the light of the increasingly competitive market. • CIRC should consider establishing stronger requirements on agents to disclose commissions and potential conflicts of interest.

Core Principle	Recommendations
19. Conduct of Business	<ul style="list-style-type: none"> • CIRC should consider developing a five year road map for the distribution network and market conduct focusing on: (a) clear and simple guidance on the needs of the policyholder and advice during selling life and non-life products which takes into account the interests of the policyholders; (b) Clear information at the first business contact; the agency and/or broker should have to inform the customer about their status (e.g., broker or tied agent), so that the customer is aware of a potential conflict of interests; (c) Informing policyholders about the costs of concluding life and health insurance products; (d) a standard claims management system to be able to handle claims in a timely and fair manner; and (e) on-going advice to the policyholders.
20. Public Disclosure	<ul style="list-style-type: none"> • CIRC should review and update the core requirements on disclosure to reflect the full range of ICP requirements, as appropriate in the context of the Chinese insurance market, including in relation to technical provisions and claims, and complete their planned work to align them with C-ROSS required disclosures. • CIRC should extend the disclosure requirements applying to reinsurers and insurance groups. • CIRC should continue to give guidance (and require insurers to do so) on the interpretation of the new disclosures under Pillar 3 of the C-ROSS framework to maximize their usefulness to stakeholders.
23. Group-wide Supervision	<ul style="list-style-type: none"> • The revised insurance legislation being developed by CIRC for submission to the State Council and People's Congress should include more explicit powers in relation to groupwide supervision so as to ensure that CIRC can continue to exercise effective groupwide oversight.
24. Macroprudential Surveillance and Insurance Supervision	<ul style="list-style-type: none"> • CIRC should finalize, as planned, the regime for D-SIIs.
25. Supervisory Cooperation and Coordination	<ul style="list-style-type: none"> • CIRC should continue to deepen supervisory cooperation within the JMC framework and bilaterally, including with the CSRC in relation to areas of shared interest. • CIRC should establish a framework for assessing the equivalence of foreign regulators (particularly in relation to their consolidated supervision), where significant in relation to foreign-funded insurers, and in case of future expansion of domestic insurers outside China. • CIRC should review, update and extend its network of MoUs with foreign regulators to incorporate provisions on supervisory cooperation to supplement provisions on exchange of information (see also ICP3).
26. Cross-border Cooperation and	<ul style="list-style-type: none"> • In addition to completing its planned development of its D-SII framework, which captures cross-border business, CIRC should review the scope of its crisis management planning for all insurers

Core Principle	Recommendations
Coordination on Crisis Management	<p>with foreign operations to ensure that there is adequate focus on crisis preparedness in supervisory work.</p> <ul style="list-style-type: none"> • CIRC should develop a framework for crisis simulation involving an insurance group, to test how it would react in case of a crisis. While more useful for a banking crisis, an exercise simulating how CIRC, CISF, etc. would deal with a crisis at a major insurance group would be useful in testing how communications would work, whether adequate information was available, and whether the authorities had the right tools to deal with the crisis.

F. Authorities' Responses to the Assessment

28. China Insurance Regulatory Commission (CIRC) welcomes the opportunity to take part in the second China FSAP and have a full assessment of ICP observance. We appreciate the fruitful work of the assessment that would have been impossible without the hard work of the assessors and the good communication and cooperation between the assessment team and CIRC.

29. After first China FSAP, much progress has been made to modernize and strengthen insurance regulation and supervision in China. Since then, Insurance Core Principles (ICPs) have also gone through amendments and the current version, as amended by the IAIS in 2015, is much more rigorous and comprehensive than the one used for the first China FSAP in 2011. CIRC is pleased with the general findings of the assessment indicating that China has been undertaking far-reaching reforms and modernization since the 2011 FSAP; and that the Chinese regulatory system has a good level of compliance with the Insurance Core Principles.

30. The report recognizes that CIRC has focused its work on improving corporate governance, enforcing sound market conduct and reshaping the solvency standards into a modern, risk-based approach; that CIRC's regulatory framework includes extensive requirements on these three pillars of regulation; and that all these requirements are applied appropriately.

31. The report identifies areas for development and gives many constructive recommendations as to how CIRC can further improve its regulatory system such as through a stronger system of lead supervision, enhanced collaboration with other supervisors and recognition of foreign supervisors, further development of crisis preparedness and market conduct work, planning for the next stage of China Risk Oriented Solvency System(C-ROSS), as well as making changes of legislative framework.

32. Many of the proposed changes are already in progress. The regulatory framework for Domestic Systemically Important Insurers was under steady construction when the on-site mission took place and the solvency regulation recognition work with EU and Hong Kong is in process. As for C-ROSS, a task force has been established to discuss the next step.

33. It is important to note that the Chinese insurance industry has a relatively short history. At the time of the assessment, China is an emerging insurance market with insurance penetration and density both below world average despite its size and fast growth in recent years. CIRC's regulation system is designed based on this fact. Therefore, some areas that seem partially compliant with ICP such as enterprise risk management are specially designed to reflect the current risk management level of the insurance industry. This approach to reflect Chinese characteristics has been proved to be useful and successful in practice.

34. We appreciate the recommendations of the assessors, which will have increasing value as the Chinese insurance industry continues to grow and to mature. CIRC looks forward to continuing dialogue with the IMF and World Bank as it considers the recommendations.

IOSCO

A. Executive Summary

1. The authorities' vision of ensuring that the capital markets support China's transformation towards a more market-oriented economy has driven capital markets development and—as the authorities recognize—the regulation and supervision of the markets. In some areas, the specific characteristics of the market combined with the vision of capital markets development have prompted the China Securities Regulatory Commission (CSRC), as the main regulator of the securities markets, to adopt different approaches to the regulation and supervision of the market than those adopted in other large markets. At times, such an approach has encountered challenges and the balance between market development and stability has been difficult to strike. Moving to more market-based solutions should allow the markets to work more efficiently but this should be done in a carefully-sequenced way.

2. The regulatory framework and supervisory program for the securities markets is largely compliant with the International Organization of Securities Commissions (IOSCO) Principles. Since 2010, when the previous assessment was conducted, the authorities have implemented several initiatives aimed at protecting China's very large retail investor population. On the CSRC side, this includes strengthening the suitability requirements for intermediaries, investors' ability to exercise their rights, and its investor education program. The CSRC has also expanded authorized activities for some categories of securities intermediaries with the objective of developing an investment banking culture to help capital markets serve the real economy better. At the same time, the prudential and capital requirements applicable to some participants have been reviewed and strengthened. During the last three years, the CSRC has strengthened its tools to monitor systemic risk. Following the market volatility of 2015 it has taken actions to curb excess leverage in the market, with some of these actions undertaken jointly with other public authorities. Finally, during the last year the CSRC has also taken a stronger stance on enforcement. By the same token, the CBRC has strengthened the regulatory framework for WMPs in several key aspects, including, for example, by introducing stronger distribution and sales rules, requiring full segregation and separate accounting for each WMP, and imposing stricter rules on eligible investments.

3. Some innovative approaches taken by the CSRC could serve as a reference for other jurisdictions. The see-through system for clients' accounts, the creation of the China Investor Services Corporation, which can represent investors in court, and the efforts to develop a multilayer mediation system are only a few of the investor protection initiatives that could be followed by emerging markets regulators. As for systemic risk monitoring, the creation of the Capital Markets Statistics and Monitoring Center, the development of the Central Regulatory Information Platform, and the implementation of a universal identification number for investors across the securities and futures markets are leading practices.

4. However, at the regulatory and supervisory level the authorities face some challenges that require attention. First, the financial authorities should implement the existing agreements aimed at harmonizing the regulation of activities and products currently subject to more than one regulatory regime and supervisory authority. Priority should be given to the development of harmonized regulations for asset management services, as differences in key operational aspects provide room for regulatory arbitrage, which in turn may have an impact on investor protection and affect the ability of the authorities to monitor systemic risk. Under the JMC, the People's Bank of China (PBC), the CSRC, the CBRC, and the CIRC have reached a consensus to strengthen the regulation of WMPs and are currently working on the development of uniform regulatory rules for the same type of WMPs. Such harmonized framework should address weaknesses identified through this assessment in the areas of disclosure, custody, bankruptcy remoteness and valuation, as appropriate. In addition, coordination arrangements should continue to be enhanced to help ensure that such harmonized regimes are administered in a consistent fashion. By the same token, the authorities should implement agreements reached in the JMC for Bonds concerning the bond markets that aim at harmonizing regulations, and enhancing coordination mechanisms including enforcement actions. In tandem, the authorities should continue working on the harmonization of the regulations for credit rating services, for which a draft regulation has been submitted for consultation. Finally, in the medium term, the authorities should also consider the development of harmonized regulations for asset-backed securities within the framework of the *Securities Law*.

5. Second, addressing the resource challenges faced by the CSRC should allow it to step up its supervisory and enforcement program as the market continues to grow. The staff quota system and salary scale to which the CSRC—along with the other financial regulatory commissions—is bound are limiting its ability to keep up with a market that is growing in complexity and at a very fast pace. While improvements in off-site monitoring and the use of big data can help, the current market structure characterized by a large presence of retail non-sophisticated investors trading in the market, requires a much more intensive approach to supervision than may be required in other large jurisdictions. In this regard, in general it is important that the coverage of the monitoring programs for all participants be kept under review, including that of auditors, given their role in the system. Thus, additional resources are needed to ensure that the CSRC can deliver a sufficiently robust program of supervision and enforcement. In addition, consideration should be given to providing the CSRC with greater autonomy to decide on the number of staff and to have a separate salary scale from that applicable to the civil service, as is the case in other jurisdictions.

6. Third, the enforcement strategy should continue to be enhanced, and the powers to impose appropriate sanctions strengthened so that the CSRC and the criminal authorities can implement an enforcement program that provides confidence to investors. There is evidence that the CSRC is moving towards using administrative measures and sanctions in a more vigorous way, including through the imposition of larger monetary penalties and bans on the full range of market participants, from issuers to intermediaries and including gatekeepers such as sponsors and auditing firms. To ensure it has a lasting effect on market behavior, this approach should be continued and further strengthened. To assist this effort, gaps and inconsistencies in the descriptions of misconduct should be eliminated and the level of fines and penalties available increased for both administrative sanctions and criminal offenses, as appropriate, including in the latter case the terms of imprisonment. In addition, criminal sanctions, in particular imprisonment, need to be used more vigorously to punish the most egregious violations and send clear deterrence messages to the market.

7. From a systemic risk monitoring perspective, the authorities should continue strengthening mechanisms to ensure they have a holistic view of securities markets and their interconnectedness with the rest of the financial sector. As mentioned above, the CSRC has made impressive progress to improve its tools and processes for systemic risk identification and monitoring. Such efforts should continue with a view to ensuring that the CSRC has effective tools and expertise to monitor all markets under its remit. Given the existence of multiple regulators for key products and markets, it is critical that the current cross-sectoral mechanisms to share information, identify and monitor systemic risk continue to be strengthened. In particular, as agreed by the authorities, data sharing on asset management should continue to be expanded and efforts to standardize data be given full priority. The authorities should also explore whether a more continuous and systemic mechanism to jointly monitor risks stemming from the bond markets is needed.

8. Further, it is critical that all authorities responsible for the regulation and supervision of key components of the securities markets remain continuously alert to the need to make adjustments to regulation and supervisory practices in a timely fashion. In the case of China, the pace of growth means that practices that today are considered appropriate might be inadequate in a short period of time. Thus, even in areas where the system has been considered fully aligned with the Principles, the authorities are encouraged to keep a critical eye.

9. Looking forward, many of the challenges ahead will continue to require a careful balancing of the developmental and stability mandates, which in turn would have an impact on regulation and supervision. In the case of China, many of the challenges ahead stem from the authorities' vision to further develop the markets and the potential approaches to do so in a manner that delivers more market-based solutions, while ensuring investors' protection and financial stability. For example, to further strengthen the role of disclosure in the public markets and the private exercise of rights, work would be required on several fronts, including initiatives to (i) strengthen corporate governance of issuers as a key step to improve the quality of their financial disclosure, (ii) ensure that different gatekeepers comply with their responsibilities, (iii) enhance investors' ability to exercise their rights, and (iv) foster greater participation of institutional investors

in the markets—some of which are not covered by the IOSCO Principles. Further, from a broader perspective, a key challenge for the CSRC and the Chinese authorities is to ensure that the multi-tiered market is implemented in a way that it does not adversely affect investors' confidence in the capital markets as a whole. To this end, the CSRC should keep the National Equities Exchange and Quotation Corporation (NEEQ) and the securities companies that operate in it under close monitoring. In addition, as planned by the authorities, standards should be implemented to facilitate the regional trading platforms to develop safely and operate as an effective way to bring local financing to local businesses. In the long run, the authorities should consider the development of a common framework that encompasses all non-exchange trading platforms, while allowing for differences in the role that the CSRC would play in their oversight. Similarly, further development of the futures markets would require consideration of the potential need for a more sophisticated business model for futures intermediaries and how best to foster the confident participation in the market by end users. This will require the CSRC to assess whether changes are needed in the regulatory framework as well as education programs and continued close monitoring of market activity and risk management practices. Finally, because of the importance of the audit process for the reliability of financial information across the financial sector, it is critical that the authorities unite their efforts to ensure high quality audits and a well-regulated profession. The creation of a single, independent oversight body might be an option to achieve this objective.

B. Introduction

10. An assessment of the level of implementation of the IOSCO Objectives and Principles of Securities Regulation (IOSCO Principles) was conducted in the People's Republic of China from November 29 to December 21, 2016 and February 21 to March 1, 2017. The assessment was made as part of the IMF-WB FSAP by Ana Fiorella Carvajal, IMF staff on assignment with the World Bank, and Malcolm Rodgers and Thomas Yee, external experts working for the IMF-WB. The previous IOSCO assessment for China was conducted in 2010.

C. Information and Methodology used for Assessment

11. The assessment was made on the basis of the IOSCO Principles approved in 2010 and the Assessment Methodology adopted in 2011. As has been the standard practice, Principle 38 was not assessed due to the existence of a separate standard for financial market infrastructure. The IOSCO Assessment Methodology requires that assessors not only look at the legal and regulatory framework in place, but also at how it has been implemented in practice. Among other things, such a judgment involves a review of the inspection programs for different types of supervised entities, the cycle, scope and quality of inspections, as well as how the relevant authorities follow up on findings, including by using enforcement actions.

12. The assessment was based on several sources. These comprise (i) a self-assessment and additional written responses prepared by the authorities; (ii) reviews of the relevant legislation and regulations; (iii) meetings with CSRC management team and staff, (iv) and meetings with public officials, including representatives from the PBC, the CBRC, the CIRC, the National Development and Reform Commission (NDRC), the MoF, and the Ministry of Public Security; and meetings with

exchanges, industry associations, the China Securities Depository and Clearing Corporation (CSDC), the Securities Investor Protection Fund (SIPF), and a sample of listed companies, securities companies, fund management companies, future companies, banks, insurance companies, auditors, credit rating agencies, consultancy firms, and law firms.

D. Institutional and Market Structure—Overview

Regulatory Structure

13. The regulation and supervision of the financial sector in China is set broadly along sectoral lines, whereby the securities industry is mainly regulated by the China Securities Regulatory Commission (CSRC); while the banking industry and the trust company industry is regulated by the CBRC and the insurance industry by the CIRC. The CSRC was established in October 1992 as a ministry-level government agency directly under the State Council (SC), to which it is accountable. The main governing body of the CSRC is the Chairman, whose position has Ministerial rank. He is currently supported by four Vice-Chairmen and two Assistant Chairmen. The Chairman has responsibilities for all matters; while each Vice-Chairmen and Assistant Chairman has responsibilities to oversee day-to-day operations of specific departments. The executive team is appointed by the State Council (SC).

14. The SC plays a key role providing strategic direction to the CSRC. The regulation and supervision of the capital markets is driven by a capital markets development strategy aimed at ensuring that the capital markets play a larger role in financing the real economy. This strategy emanates from the National People's Congress (NPC) annual meetings and is transformed into actionable points via opinions of the SC. The most relevant opinions are the Opinion on Further Enhancing the Protection of Small Investors' Rights and Interests from 2013 and the Opinion on the Healthy Development of the Capital Markets from 2014. CSRC strategic priorities are driven by such opinions. That said, the CSRC has the opportunity to influence such opinions, as their development is subject to consultation with all relevant stakeholders including the CSRC.

15. In general, the mandate of the CSRC covers the regulation and supervision of the securities and futures markets. Such responsibilities are mainly established by law (the Securities Law and the Securities Investment Fund Law); and complemented by regulations and decisions of the SC. Pursuant to the legal and regulatory framework the CSRC authorizes the public offering of securities and funds, licenses all categories of intermediaries with the exception of private securities investment fund managers (which are only subject to registration with the Asset Management Association of China (AMAC)), licenses futures markets (while the licensing of equity markets falls to the SC acting on the recommendation of the CSRC), and licenses information service providers, including credit rating agencies and auditors that provide services in the securities and futures markets. It has rulemaking powers over all such categories of participants (including private fund managers), and exercises day-to-day supervision of their operations. It also has investigative and administrative enforcement authority in connection with the laws and regulations that it administers and as a result can impose administrative measures on regulated entities and administrative sanctions, including money penalties, on both regulated entities and persons who are in breach of

such laws and regulations. Criminal enforcement is a responsibility of the criminal authorities, although the CSRC and the Securities Crime Investigations Bureau of the Ministry of Public Security play a key role in assisting the investigation of criminal offenses.

16. However, certain activities and products are subject to the regulation and supervision of more than one regulatory authority. Agreements between the relevant agencies have already been reached to harmonize regulation and strengthen coordination and cooperation arrangements in most of these areas, which include:

- The provision of asset management services.
- The offering, placement and trading of bonds.
- The offering, placement and trading of asset backed securities (ABS).
- The provision of credit rating services.

17. To exercise its responsibilities, the CSRC's central office in Beijing is complemented by its 38 regional offices. In general, the CSRC central office is responsible for (i) preparing market development plans; (ii) formulating, amending and revising regulations and rules concerning the securities and futures markets; (iii) carrying out the approval function in key matters such as public offerings and licenses of intermediaries; (iv) guiding and coordinating efforts on risk prevention and mitigation; (v) coordinating supervisory actions, (vi) organizing investigations and enforcement activities in relation to cases involving misconducts or material violations of securities and futures laws; and (vii) coordinating and planning investor protection initiatives. The CSRC regional offices are the frontline supervisors of their respective jurisdictions, and as such are responsible for the supervision of entities and activities under their jurisdiction, along with the investigation of misconduct, and the corresponding enforcement actions, and the implementation of investor protection initiatives, including investor education. There are different mechanisms through which coordination takes place, including annual statewide meetings to discuss supervisory and enforcement priorities.

18. The CSRC is supported by 19 affiliated institutions, which include the stock and futures exchanges as well as industry associations including the Securities Association of China (SAC), the China Futures Association (CFA) and AMAC. Both the exchanges and the industry associations exercise self-regulatory functions assigned to them by Law. The exchanges have listing authority and as such have a key role in the monitoring of listed companies' compliance with listing obligations including disclosure obligations; they also have an important role in member regulation and market surveillance with a view to ensuring orderly trading and supporting the identification of unfair trading practices. Membership in the industry associations is mandatory for specific categories of intermediaries: securities companies must be members of SAC; futures companies of the CFA and private securities investment fund managers of AMAC. The industry associations have two main roles: the development and administration of a system for the qualification of practitioners (individual persons that exercise specific functions in the securities and futures industry) and the development and monitoring of rules for the industry, which in practice have come to provide additional granularity to CSRC regulations. Notwithstanding the existence of the industry

associations, the CSRC has the licensing authority over all intermediaries, and has developed supervisory programs for all categories of intermediaries; thus the programs of the industry associations complement CSRC programs. The only case where there is a difference in approach relates to the managers of private securities investment funds and the private funds themselves, whereby they are not subject to licensing by the CSRC nor approval of the funds by the CSRC, but only to registration with AMAC. That said, the CSRC has regulatory powers over them and in practice it has its own supervisory program to oversee their operations.

E. Market Structure

Cash Markets

Equity Markets

- 19. The Chinese authorities are pursuing a strategy of building a multi-tiered equity market to ensure access to capital for a wide range of business enterprises.** In practice, they have been actively involved in the establishment of the different types of markets and trading platforms described below.
- 20. At the top are the Shanghai and Shenzhen Stock Exchanges.** The Shanghai Stock Exchange (SSE) has only one board, and caters mainly to blue chip State Owned Enterprise (SOEs). The Shenzhen Stock Exchange has three levels: the main board, the SME board and the Growth Enterprise Board (GEB), also known as ChiNext. The GEB is considered a second board, catering to innovative growth enterprises. Listing requirements are scaled, with the GEB having the least stringent financial and performance requirements. The Shenzhen Stock Exchange has mainly catered to private (non SOEs) companies. Companies that have publicly offered shares can be listed on any of these boards. As of the end of 2015, there were 2,827 companies listed on the two exchanges, for a total market capitalization of RMB 53.2 trillion which is equivalent to 78.5 percent of China's GDP.
- 21. Arrangements have been established to allow cross-border trading in shares between the Chinese Mainland and Hong Kong.** Before 17 November 2014, foreign investors only had exposure to Chinese equities via Chinese listings on the Hong Kong Stock Exchange. Only institutional investors were given access to the Shanghai and Shenzhen stock exchanges via the Qualified Foreign Institutional Investor (QFII) and RMB Qualified Foreign Institutional Investor (RQFII) programs. Onshore retail investors could only own investments outside of China through onshore Qualified Domestic Institutional Investor (QDII) products. These barriers came down with the implementation of Shanghai-Hong Kong Stock Connect (Stock Connect). Stock Connect allows direct mutual market access between the Shanghai and Hong Kong exchanges using their local brokers and clearing houses, within certain volume caps. A similar arrangement between the Shenzhen Stock Exchange and the Hong Kong Stock Exchange commenced operations in December 2016, except that there are no total volume caps for it. Trading through these mechanisms is jointly supervised by the exchanges and regulators in each of the jurisdictions.
- 22. Secondary market trading has grown significantly since the previous assessment.** There was a very significant increase in market trading in 2015, accompanied by large swings in market

prices. As noted below, concerning trading in the secondary markets, the level of direct participation by retail investors is very high by international standards and participation by institutional investors remains small compared to other large markets. This is one factor that likely contributed to high levels of market volatility, for example in 2015, as retail investors tend to react in large numbers to information or market rumors, and the market discipline that could be provided by institutional investors is largely absent.

23. In accordance with the Securities Law and under the approval of the SC, the National Equities Exchange and Quotations (NEEQ), also known as the “New Third Board”, was established in 2013 as a national trading venue to cater to innovative, entrepreneurial and growth micro, small and medium enterprises. It is a national platform for the transfer and trading of securities subject to the regulation of the CSRC. Companies in NEEQ may have more than 200 investors (the threshold for a public offering), however they are only allowed to sell their shares to qualified investors, which are experienced investors with at least RMB 5 million in financial assets. Trading in NEEQ is also restricted to qualified investors. Companies in NEEQ are subject to a set of disclosure requirements and corporate governance requirements in light of their nature as non-listed “public” companies. Compliance by issuers with such requirements is monitored by the NEEQ. There are no financial indicators that NEEQ companies must comply with. In practice, at the time of the assessment the percentage of companies that exceeded 200 investors was not material. As of the end of 2016, 10,163 companies were listed on NEEQ, and market capitalization was approximately RMB 4.1 trillion. The NEEQ's annual turnover was RMB 814 million in 2013, RMB 13,036 million in 2014, and RMB 191,062 million in 2015 and RMB 191,229 million in 2016 respectively.

24. In addition to the nationally regulated markets, there are 40 regional “trading platforms” that operate as OTC markets to raise capital, and that are restricted to qualified investors. Regional equity platforms are established mainly in accordance with the Decision of the SC on Rectifying Various Trading Venues to Effectively Prevent Financial Risks (Guo Fa, 2011 No. 38), the Opinions of the General Office of the SC on Implementing Efforts to Rectify Various Trading Venues (Guo Ban Fa, 2012 No. 37) and the Notice of the General Office of the SC on Regulating the Development of Regional Equity Markets (Guo Ban Fa, 2017 No.11, the “Notice”). Pursuant to these instruments each regional platform should only trade companies located in the region. Companies trading on these platforms cannot engage in a public offering of securities; they are only allowed to sell their securities to qualified investors through a private placement. Thus, as per the definition of public offering, they cannot have more than 200 shareholders. Secondary market trading also is restricted to qualified investors. As per recent guidance issued by the SC such investors must be institutional investors or individuals with more than 500,000 RMB in financial assets. Trading mechanisms vary; but pursuant to the SC instruments no trading platform may establish a market-making system or provide a continuous auction or electronic matching capability, and a lapse of 5 days must take place between the moment that an investor buys a securities and the moment in which he/she sells it. At the end of 2016, there were about 17,400 companies listed in these platforms. In 2016, companies raised RMB 287.1 billion through various financing activities on the system.

25. There is also an inter-institutional quotation system administered by SAC. The China Securities Internet System Co., Ltd. (CSIS) is a financial institution established on February 27, 2013 with the approval of CSRC and administered by SAC in accordance with market-based principles. CSIS is licensed to (i) provide quotation, offering, and transfer services for non-publicly offered products; (ii) facilitate, through building business alliances, the exchange of information and the interconnection of trading networks in the private market such as the OTC market of securities companies and regional equity markets; (iii) provide the depository, clearing, settlement, and third-party collateral management services in respect of non-publicly offered products; and (iv) provide services relating to the monitoring and statistical analysis of the private market, and develop, promote, study, investigate, and advise on the private market and its operations. CSIS is a well-functioning company with growing membership and business operations.

Bond Markets

26. There is a multilayered system for the bond markets, comprised of the exchange and the interbank bond market. Before 1997, the securities exchange was the main market for bonds. After 1997, with the approval of the SC, the inter-bank bond market was established and regulated by PBC. It is an over-the-counter (OTC) market, positioned as a market for institutional investors, which term includes various types of financial institutions, legal entities, and their financial products.

27. The bond markets have experienced considerable growth during the last years; however, of the two markets, the interbank bond market is by far the larger. In 2016, roughly 90 percent of the new issuance of bonds was originated and traded in this market. As of December 2016, the inter-bank bond market consisted of debt instruments worth more than RMB 56.3 trillion.

28. The ABS markets are incipient. Currently ABS can only be offered to qualified investors. As of end 2016, outstanding ABS issued by banking financial institutions in the interbank bond market stood at RMB 487.8 billion; while outstanding ABS issued on the exchanges reached RMB 541.9 billion, up by 233 percent year on year.

29. The local government bond market has experienced rapid growth. By the end of 2016, the outstanding volume was around RMB 10 trillion, which is close to the size of the treasury bond market. There are guidelines of MoF pertaining to the issuance of local government bonds by way of a public offering. Those guidelines require initial as well as ongoing disclosure. As per current guidelines, such documents are filed with the MoF. Only the local government bonds listed in the exchange market could be offered to retail investors. This segment of the market remains small.

30. Banks can offer a limited number of bond products over the counter. However, they cannot be offered to retail investors, only to high net worth individuals.

Futures Markets

31. There are three commodities futures exchanges and one financial futures exchange in the Chinese Mainland. The Shanghai Futures Exchange, the Dalian Commodity Exchange and the Zhengzhou Commodity Exchange trade only in commodity-based futures contracts. They are all mutualized exchanges. As of end 2015, there were 46 commodity futures contracts traded on the markets covering commodities such as gold, oil, copper, aluminum, zinc, steel, rubber, rice, corn, soybeans and sugar. The China Financial Futures Exchange (CFFEX), which is owned by the other commodity futures exchanges and the two stock exchanges, trades only financial futures contracts. As at the end of 2015, three stock index futures and two Treasury bond futures traded on the CFFEX. Separately, there is one Exchange-Traded Fund (ETF) options contract traded on the Shanghai Stock Exchange.

32. Trading in futures contracts has seen significant growth in recent years. In the commodities markets, the Chinese futures markets have now become the global reference point for the pricing of some commodities. Market growth has been most striking in the financial futures market operated by CFFEX, and there is market demand for an increasing range of new products. As in the equity markets, there is a high level of retail participation in futures trading and this may in part account for market volatility that is sometimes high by international standards.

Cross Trading

33. There is no cross-listing of securities or futures traded on regulated financial markets, and products trade on only one market. An exception to this is bonds traded on one or other of the stock exchanges and on the interbank bond market, including government and local government bonds, and bonds issued by financial institutions and enterprise bonds. In practice, trading of bonds on the public markets accounts for a relatively small percentage of overall bond trading.

Investors in the Exchanges

34. An important feature of China's securities and futures markets is the degree of retail investors' participation in secondary market trading, and a relatively lower level of institutional participation compared to many other jurisdictions. Retail investors with less than RMB 500,000 account for well over 90 percent of trading accounts on the stock exchanges, about 80 percent of trading activity and 35 percent of market value. Similarly, in futures markets, retail accounts (accounts held by natural persons) were over 95 percent of the total as of February 3, 2017. In futures markets, retail trading accounts for about 79 percent of trading (68 percent in June 2015), and 50 percent of open interest. In 2015, there were almost 215 million stock accounts held by over 99 million investors; and 1.268 million futures accounts held by 1.075 million futures investors.

35. There is limited participation of foreign institutional investors. As of the end of June 2016, there were 297 QFIIs, with a combined QFII quota of USD 81.2 billion and QFII assets of RMB 561,103 billion; there are 207 RQFIIs, with a combined RQFII quota of RMB 507,968 billion and RQFII assets of RMB 149,865 billion.

Asset Management Services

Fund Management Companies

36. At the end of June 2016, fund management companies in China were managing 3,115 mutual funds (MFs) that were offered to the public (retail investors), with assets under management (AUM) of RMB 8.0 trillion. While growing, the collective investment scheme (CIS) industry is still relatively small and underdeveloped in terms of the type of products that are offered to the public. The bulk of the assets are in open-end funds; and in particular in money market funds (MMFs). Bond funds, including MMFs, experienced considerable growth in recent years, particularly following the volatility on the equity markets that lowered investors' risk appetite. MFs suffered important redemption pressures in late 2016 as a result of the stress situation experienced in the bond markets.

37. Retail investors have an important participation in CIS. As of the end of June 2016, individual investors accounted for 99.96 percent of the total number of active accounts in open-end funds, and institutional investors accounted for only 0.04 percent. Individual investors and institutional investors accounted for 46 percent and 54 percent respectively of the net value of holdings.

38. In addition to CIS, fund management companies are authorized to manage assets for individual clients. As of June 2016, the total AUM of fund management companies and subsidiaries that provide asset management services for specific clients was RMB 15.3 trillion.

Fund Management Companies Managing Private Funds

39. There are a significant number of private funds; but only a few could be considered hedge funds (HFs). Under the current legal and regulatory framework there is not an official definition of HF. Managers of private securities investment funds and the private funds themselves are required to register with AMAC. As of the end of December 2016, AMAC had a total of 17,433 private fund managers on its register and was keeping records on 46,505 private funds with a combined paid-in AUM of RMB 7.9 trillion. A breakdown of such funds is provided below. In practice, as per conversations with authorities and market participants, very few of such funds would meet the characteristics commonly associated with a HF (in terms of their investment strategies, use of derivatives and/or use of leverage), and they are not yet important in terms of their size. Overall about 90 percent of the investors in these funds are natural persons (high net worth individuals).

Banks and Trust Companies

40. Banks offer asset management services to all types of investors. A key component is WMPs, some of which constitute CIS offered to the public (retail investors). At the end of June 2016, there were 454 banking institutions offering WMPs. There were a total of 68,961 products and the total value of WMPs was RMB 26.3 trillion. Of these WMPs those that involve a guarantee of the principal (and in some cases also of return) accounted for 23.2 percent of total value. These products are on the balance sheets of the issuing banks and are not CIS. Of the remainder, some products are

offered only to high net worth individuals, institutional or private banking clients. Collective products which involve managing a pool of assets for retail clients amounted approximately to RMB 8 trillion in AUM.

41. Trust companies offer asset management services, in particular trust plans, but to qualified investors only. The collective money trust products provided by trust companies are offered only to qualified investors including institutional investors and natural persons who meet the relevant criteria.¹ A collective money trust product may not have more than 50 individual investors whose investment is smaller than RMB 3 million. There is no limit regarding the number of investors whose investment exceeds that amount. As per conversations with authorities and market participants, at the time of the assessment they did not have the characteristics commonly associated with HFs. First, current regulations do not allow trust companies to engage in debt businesses other than interbank borrowing (subject to credit limits). In addition, their investment strategies did not involve complex techniques or use of derivatives. As at December 2016 there were 68 trust companies licensed by the CBRC with assets of about RMB 7.3 trillion. Less than 40 percent of trust assets are held by collective trust products.

Insurance Companies and Insurance Asset Management Companies

42. Insurance companies offer certain products that have some characteristics of a CIS, but that provide a protection component. In particular, they offer unit-linked insurance products. However, pursuant to CIRC regulations they must have an important protection component (the sum insured must be at least 120 percent, 140 percent or 160 percent of the premium paid or account value depending on the age profile). Unit-linked insurance products are on balance-sheet items, thus are under the regulation of the new C-ROSS solvency framework.

43. Insurance asset management companies manage asset management plans; which constitute CIS but can only be offered to institutional investors. In practice, they are mainly used by insurance companies to manage their insurance funds. As a result, at the time of the assessment, they did not meet the characteristics commonly associated with HFs. The balance of their insurance AUM amounted to approximately RMB 13.5 trillion as of December 2016.

Intermediaries

Specialized Securities Intermediaries

44. There are four types of specialized licenses to carry out securities market activities: securities companies, futures companies, fund management companies and securities and futures investment consultancy firms. Under the current regulatory framework, securities

¹ Pursuant to the Rules for Collective Money Trust Products an eligible investor refers to a person who satisfies any of the following criteria as is able to identify, judge and undertake the risks associated with a trust plan: (i) a natural person or institutional investors whose minimum investment in a trust plan is at least RMB 1 million; a natural person whose aggregate individual or family financial assets exceed RMB 1 million at the time of subscription or a (ii) a natural person whose annual income exceeds RMB 200,000 in the recent three years or who earns with his/her spouse over RMB 300,000 annually in the recent three years.

companies are the only type of intermediary that is authorized to engage in “principal” business, including proprietary trading, margin trading and securities financing; they can provide these services both in the regulated and the OTC markets. That said, overall the regulatory approach to intermediaries is evolving. While in the past each category of intermediary was only allowed to conduct a set of specific activities associated with the corresponding license, increasingly they are being allowed to provide additional services either via an expansion of authorized activities for such license or through subsidiaries. All this in line with a strategy of the authorities to create an investment banking culture that can propel the capital markets to serve the real economy better. Securities intermediaries require the approval of the CSRC to establish subsidiaries overseas.

45. As of end June 2016, there were the following number of intermediaries: 127 securities companies (including 2 in a preparatory stage); 117 mutual fund managers; 149 futures companies and 84 securities investment consultancy businesses that hold only a securities investment consultancy license (i.e. they are not securities companies or futures companies). Except for securities investment consultancy service, these companies do not engage in other securities activities such as brokerage, underwriting, sponsorship, and margin trading.

46. At present, China does not allow foreign authorized/registered/licensed securities companies, fund management companies and futures companies to directly participate in the domestic market. Foreign investors, however, may hold stakes in domestic securities companies, fund management companies and futures companies in accordance with the *Law on Securities Investment Funds*, the *Rules for Establishment of Securities Companies with Foreign Investment*, the *Measures for the Administration of Futures Companies*, among other relevant laws and regulations. As of the end of June 2016, 11 of the 127 securities companies; 44 of the 104 fund management companies and 2 of the 149 futures companies were joint ventures with foreign investors.

Other Intermediaries that can Provide Securities Markets Activities

47. Banks can undertake a range of securities markets activities. The main activities are (i) the provision of asset management services (individual and collective portfolio management and advisory services) to both retail investors and high net worth individuals, for which they are subject to the regulation and supervision of the CBRC; (ii) market making and trading of bonds in the interbank bond markets, for which they are mainly under the regulation and supervision of the PBC and self-regulation of National Association of Financial Market Institutional Investors (NAFMII) and the regulation and supervision of the CBRC; (iii) distribution of funds, for which they are subject to the regulation and supervision of the CSRC and the CBRC; and (iv) custody services for which they require license by both the CBRC and CSRC. In addition, as discussed below, there currently is a pilot program to allow banks to establish a fund management company as its subsidiary to undertake fund management activities under the regulation and supervision of the CSRC and consolidated supervision of the CBRC. Banks are not allowed to invest in equity.

48. Trust companies can provide asset management services. In addition to collective trust plans, trust companies can provide individual and collective portfolio management and advisory

services, but only to qualified investors as defined above. In these activities, they are subject to the regulation and supervision of the CBRC.

49. Insurance asset management companies can provide asset management services but exclusively to institutional investors. As indicated earlier, in practice the asset management plans of these companies are used by insurance companies to manage their insurance funds; and by a few other institutional investors (banks, annuity companies) to get long-term products. These plans are subject to the regulation and supervision of the CIRC.

Information Services Providers

50. Credit rating agencies (CRAs) are required to fulfill filing requirements with the PBC which is their lead regulator. In addition, CRAs are required to be licensed or recognized by the regulatory authority of the market in which the company rated will issue the securities. In practice, there is significant overlap in the lists of recognized CRAs. As of June 2016, there were 7 CRAs licensed by the CSRC to engage in securities markets services.

51. Auditors providing their services in relation to the securities and futures market are required to obtain approval from the CSRC and the MoF. The MoF is the competent authority for certified public accountants (CPAs). All auditors that want to provide services in the securities and/or the futures markets must obtain a license that is issued jointly by the CSRC and the MoF. In addition, they are subject to the ongoing supervision of the CSRC. As of end 2016 there were 40 audit firms authorized to conduct securities service business in China.

F. Preconditions for Effective Securities Regulation

52. Some of the preconditions for effective securities market regulation are in place, although challenges remain in a few areas.

- Overall the Company Law is considered sound; however, it still allows the use of unregistered stock (essentially bearer shares); and companies are not required to maintain a record of the names of the holders of an unregistered stock. This poses challenges to the verification of ownership of companies. In March 2014 the State Administration for Industry and Commerce (SAIC) established an Enterprise Information Disclosure Regime (EIDR), which created a database that provides access to information on all businesses and companies, including business registration, chattel mortgage, equity pledge, administrative penalties, and annual reports. This problem does not apply to companies listed on the exchanges and the NEEQ. Shares of these companies are dematerialized, registered and deposited at CSDC. As a result, ownership information is not only up-to-date but also available at the ultimate investor level, because China adopts a direct holding system and beneficiary ownership is limited to a few programs including the Stock Connect.
- The Enterprise Bankruptcy Law contains restructuring procedures to be guided by the courts.
- The role of the judicial system in effective resolution of disputes is still a challenge. The exercise of private rights is still evolving, and the Judiciary has yet to develop more expertise in

securities markets matters. However, the CSRC has taken an active role in developing mechanisms aimed at enhancing the ability of investors to exercise their rights. In particular, the Investor Services Corporation (CSISC), created in 2014, can provide support for small and medium size investors in bringing civil lawsuits against violators; although class actions suits are not permitted. As of the time of the assessment the CSISC had already taken such role in three lawsuits. In addition, a pilot program has been implemented whereby the CSISC has bought a small package of shares (100 shares) from a number of listed companies, which in turn allows it to exercise rights as a shareholder. In this way, it is seeking to educate shareholders as to the way to exercise their rights and to indirectly influence governance practices of listed companies. In addition, the CSRC jointly with the Supreme People's Court have taken steps to enhance the use of mediation services as an alternative mechanism to solve disputes. To enhance the binding effect of mediation, according to the laws and regulation as well as the notice jointly issued by the CSRC and the Supreme People's Court, the mediation agreements reached through notarization, arbitration and the judicial system, can apply for compulsory enforcement by the people's court.

- The accounting and auditing standards have been recognized by the international standard setting body as converged with those international standards. All CPAs are subject to the oversight of the MoF and auditors that provide services in the securities and futures markets to approval of CRSC and the MoF. That said, the quality of financial disclosure by issuers and of auditing work remains an issue of concern.

G. Scope of Assessment

53. The way the assessors have applied the IOSCO Principles and Methodology vis-à-vis the market and regulatory structure is summarized below.

- Regarding the Principles for the regulator, enforcement and cooperation the assessment has relied on the framework for the CSRC given its position as the main regulator and supervisor of the securities and futures markets, except when the scope of a particular principle demanded a broader approach. That has been the case of Principles 1, 6, and 12. In all other cases, the participation of other authorities in the regulation or the supervision of a specific component of the securities and/or futures markets has been assessed under the corresponding sectoral principles.
- Regarding the Principles for issuers, the assessment focuses on issuers whose securities are offered to retail investors or that are traded in platforms open to retail investors given the focus of the IOSCO Methodology. As a result, companies in NEEQ and the regional platforms were outside of the scope of the assessment given that they can only offer their securities to qualified investors, and the platforms in which they trade are restricted also to qualified investors – although the assessors recognized the differences in nature and regulation between the companies quoted in NEEQ and in the regional trading platforms. For the same reason, issuers that raise funding in the interbank bond market were outside of the scope of the assessment, as they can only be offered to institutional investors and trading is also restricted to such type of

investors. Local governments can also issue bonds by way of a public offering; however, given the size of this market at the time of the assessment, their regime was not covered.

- Regarding the Principle for credit rating agencies, the Principle covers rating services in the securities markets as a whole. That said, the assessment relied mainly in a review of the regulation and supervisory program of CRAs subject to CSRC supervision, due to the important level of overlap among the lists of authorized CRAs by the different authorities.
- Regarding the first four Principles for collective investment schemes (CIS), the assessment has covered the regime applicable to all products with the character of CIS offered to retail investors, which is in keeping with the Methodology. As a result, the regime for non-guaranteed WMPs offered by banks to retail investors has been covered in Principles 24-27, along with the regime for traditional MFs. Conversely, the regime applicable to trust plans offered by trust companies and the regime applicable to asset management plans managed by insurance asset management companies were outside of the scope of the assessment given that such plans are only offered to qualified and institutional investors respectively. Unit-linked insurance products were also outside of the assessment due to the fact that they have a significant protection (i.e., insurance) component and as a result they cannot be fully assimilated with CIS.
- Concerning the Principle for Hedge Funds (HFs), the assessment focuses on the regime for private investment securities funds and their managers because out of all the CIS currently offered to investors, only a subset of these funds seem to meet the characteristics commonly associated with HFs.
- Regarding the Principles for intermediaries, the focus has been on the provision of investment services. As a result, the regime applicable to banks in the provision of asset management services has been covered in these Principles, in addition to the regime applicable to CSRC intermediaries. However, the regime for banks has only been assessed under Principle 31 given that the Basel Core Principles assessment covers licensing, capital and resolution issues. The regime applicable to trust companies was outside of the scope of the assessment given that the bulk of their activities comprises the management and distribution of private funds that do not meet the characteristics commonly associated with HFs.
- Regarding the Principles for secondary markets, the focus has been on regulated markets and in particular on the exchange markets. However, the assessors recognize the “hybrid” nature of the NEEQ market; and as a result details regarding its regulation and supervision have been included in the assessment. The regional trading platforms were outside of the scope of the assessment given their relative importance at the time of the assessment, the fact that companies on them cannot do a public offering of securities, that secondary market trading is restricted to qualified investors, and the nature of trading mechanisms. On bond markets, the interbank bond market was outside of the scope of the assessment given that such platform is a wholesale OTC market. Given the above, the NEEQ and NAFMII were not covered in the Principles for Self-Regulatory Organizations (SROs).

54. That said, it is critical that the authorities keep a holistic view of the markets. In this regard, the assessors note the growing importance in China of the private offering regime for capital

raising including through the use of electronic platforms, and of OTC markets for the trading of equities and bonds as part of a multilayer strategy for capital markets development. Further, many of the activities and markets mentioned above are developing rapidly and their nature evolving. Thus, it is key that their supervisory efforts extend beyond the products and markets covered in detail by this assessment.

H. Main Findings

55. Principles for the regulator. The CSRC has a broad mandate to regulate and supervise the securities markets. It operates with a high degree of operational (day-to-day) independence, although under the strong strategic direction of the SC. Certain activities, products and markets, in particular asset management services and the bond markets, are subject to the regulation and supervision of more than one regulatory authority. However, the authorities are already working toward the implementation of harmonized regulations and to strengthen coordination and cooperation arrangements, as appropriate. During the last three years the CSRC has significantly enhanced the tools and processes to identify and monitor systemic risk and the authorities have been working to improve cross-sectoral mechanisms for risk-identification, monitoring and management; although additional steps need to be taken. CSRC resources have not kept pace with market growth nor with its expanding mandate and the salaries it pays are not competitive with industry salaries. This poses a challenge to CSRC's ability to deliver the type of intense supervisory and enforcement program that a market structure characterized by a large presence of retail investors requires.

56. Principles for self-regulation. Market institutions such as the exchanges and industry associations have SRO functions assigned to them by the legislation. All SROs have developed their own supervisory programs; although resources seem limited, particularly in the case of the industry associations. Coordination mechanisms are being developed that seek to avoid duplication and strengthen the complementarity of the SRO programs with CSRC's own supervisory program. The CSRC exercises oversight over the exchanges and industry associations through a combination of tools that include participation in the rulemaking process, reporting obligations, and participation in the appointment of key personnel (in the case of the exchanges) and appointment of representatives in key organs (in the case of the industry associations). Increasingly inspections are also being used.

57. Principles for enforcement. The CSRC has broad supervisory powers over regulated entities. It has broad investigative powers over both regulated entities and third parties, and can impose a series of administrative measures and administrative sanctions on them. It also has the power to refer matters to the criminal authorities and an office has been established to enhance coordination on criminal matters. In practice, the CSRC has implemented a monitoring and inspection program that covers issuers, all types of intermediaries and gatekeepers; although the coverage of such programs should be kept under review. Particularly in recent years it has also taken a more vigorous approach to enforcement, including by imposing stronger penalties and bars on different types of participants. However, this more vigorous approach still needs time to take hold. Criminal enforcement is weak and is yet to have a clear deterrent role in the market, although steps

have recently been taken by the criminal authorities to enhance their ability to pursue these crimes. Similarly, more severe penalties are starting to be applied. In both cases, deficiencies in the legal framework, including the low level of sanctions that can be imposed for some misconduct, pose limitations to the ability of the authorities to implement an effective enforcement program. The CSRC has implemented several initiatives aimed at empowering investors so that they can more effectively exercise their private rights of actions.

58. Principles for cooperation. The CSRC has the legal authority and capacity to share information and cooperate with other authorities domestically and internationally. At the international level, it is a signatory to many Memoranda of Understanding (MOUs), including the IOSCO Multilateral MOU (MMOU) and a number of bilateral MOUs with its international counterparts, and has a record of active cooperation. It does not require the permission of any outside authority to share or obtain information, nor does it require an independent interest in the matter to assist. At the domestic level, mechanisms have been developed for coordination and cooperation at policy level and the CSRC has demonstrated that it cooperates with other financial authorities.

59. Principles for issuers. The current regime for the issuance of securities to the public subjects them to initial disclosure (via a prospectus) as well as periodic and ongoing disclosure obligations that are in line with international practices. Publicly offered equities must be listed on an exchange. The financial statements in all such documents must be prepared in accordance to Accounting Standards for Business Enterprises (ASBE) that have substantially converged with IFRS. The regulatory regime applicable to equity issuers provides safeguards to ensure that holders of securities are treated fairly and equitably; in particular, it requires shareholders' approval of major transactions, and information obligations exist that seek to ensure that shareholders can take informed decisions. As part of such framework, changes of control transactions are subject to full disclosure. Prompt notification of holdings by substantial shareholders and insiders is also required. The exchanges have developed programs to monitor listed issuers' compliance with their disclosure obligations. The CSRC also has a program of review of annual reports, which focuses on compliance with accounting standards. In addition, a program of on-site inspections is also in place. The programs are all risk-based. NDRC has also implemented a program of on-site inspections.

60. Principles for auditors, credit rating agencies, and other information service providers. The MoF is the competent authority for CPAs. In addition, audit firms that provide audit services for the securities and futures markets must obtain a securities services license jointly issued by the CSRC and the MoF. These firms are also subject to the CSRC's ongoing supervision, which it conducts mainly through on-site inspections. However due to limitations in resources the use of comprehensive inspections is limited. The PBC is the lead regulator for CRAs and all firms must fulfill the record filing procedure regulated by it. In addition, they must obtain a license or recognition from the regulatory authority of the market in which the companies rated will issue securities. Pursuant to CSRC regulations CRAs are required to observe governance rules that address the quality and integrity of the rating process, independence and the avoidance of conflicts of interest. CSRC has a robust supervisory program over CRAs, which includes on-site inspections of all CRAs.

Securities analysts are subject to rules aimed at mitigating potential conflict of interest, including via disclosure, and are inspected as part of the regular program of intermediaries' supervision.

61. Principles for collective investment schemes. The management of funds that are offered to the public can only be done by fund management companies and other entities authorized by the CSRC. In all cases licensing requirements are robust. Funds are subject to initial disclosure obligations (via a prospectus) and also to periodic and ongoing disclosure obligations that are in line with international practices. Fund assets must be held by a separate custodian; however, it can belong to the same group as the fund manager. There are legal provisions that clearly separate the assets of the funds from the assets of the fund manager and the custodian, thus protecting the assets in the event of their insolvency. Fund assets must be valued according to ASBE. Under the condition that the Net Asset Value (NAV) can fairly reflect the portfolio value of the fund, MMFs are allowed to use amortized cost and keep a stable NAV. In extreme market conditions, liquidity risks may arise when investors redeem a large amount of MMF in a short time. The CSRC has a supervisory program in place that includes both off-site monitoring and on-site inspections that are carried under a risk-based approach. Private securities investment funds (including HFIs) must register with AMAC. They are subject to reporting and an on-site inspection program that appears to be commensurate to the risk they currently pose. Some WMPs offered by banks are retail CIS. Banks offering these WMPs are subject to organizational requirements and reporting obligations. Assets of these WMPs must be held by a custodian but self-custody is permitted, and there is legal uncertainty about bankruptcy protection. WMPs must be issued under a prospectus but the requirements are at a high level of generality, and banks are allowed to quote expected returns in the prospectus and marketing material. Assets of a WMP must be valued according to ASBE and thus at fair value. The current regulatory framework for these products does not contain specific provisions setting out minimum standards for subscription and redemption pricing, pricing errors or suspension or deferral of redemption.

62. Principles for market intermediaries. Securities companies, fund management companies and futures companies are subject to licensing by the CSRC. Licensing requirements are robust. Capital requirements need to be adjusted based on the activities and risks undertaken on an ongoing basis; and an early warning system is in place, where reporting takes place within 3 days. There are robust requirements for the protection of investors' assets both in the securities and futures markets and investor compensation schemes come into play in the event of the insolvency of an intermediary. Conduct obligations apply, including information and suitability requirements towards clients. All intermediaries are required to conduct annual evaluations of their internal controls, and an external auditor must also issue an opinion about the adequacy of such controls. The CSRC monitors compliance with all such obligations via a supervisory program of off-site monitoring and on-site inspections that are carried under a risk-based approach. In recent years, particular attention is being paid to issues related to internal controls, as well as suitability and information obligations. A framework to deal with the failure of firms is in place, which has been tested particularly after the failures that took place in the early 2000s. Banks providing asset management services and products are required to have internal control and supervision systems,

and strong suitability rules apply. The CBRC carries out inspections of banks that provide these services, under a risk-based approach.

63. Principles for secondary markets. The constitution of equity and futures exchanges is subject to the approval of the SC, upon recommendation of the CSRC, in the case of equity exchanges and approval of the CSRC in the case of futures exchanges. Robust requirements exist aimed at ensuring fair access and reliability of the systems, including on the latter the requirement of annual IT evaluations. Exchanges are the frontline supervisors for purposes of real time surveillance. They also have a critical role in ex-post monitoring supporting the CSRC in the identification of unfair trading practices. To this end all exchanges have developed automated systems, with alert triggers and a reasonable level of resources has been dedicated to the investigation of such alerts. In addition, mechanisms for cross-market surveillance (between the equities and the futures markets) have been established as well as cross-border with Stock Connect. Pre and post-trade transparency obligations apply to all exchanges, although for one exchange fewer bid/offer details are provided pre-trade than in the other markets. Current mechanisms to address volatility involve price limits; and in the futures markets they involve also the use of margins, transactions fees and position limits. In addition, as appropriate the exchanges can suspend trading. However, the current market structure, and in particularly the large and active presence of retail investors, poses challenges to the management of volatility. Clearing and settlement in both the securities and futures markets is conducted via central counterparties (CCPs), which have developed mechanisms to manage clearing and settlement risks, and the level of settlement failures is very low. All exchanges have mechanisms in place to deal with the default of an intermediary, including clear procedures and a default waterfall. Only covered short-selling is allowed and disclosure obligations apply.

I. Authorities' Response to the Assessment

64. The CSRC is highly committed to the FSAP exercise and views the IOSCO Principles assessment as an opportunity to fully examine and strengthen the regulation of China's capital markets in line with international standards. We appreciate the comprehensive and thorough review of the regulatory framework and practices in China's securities and futures markets by the assessment team, and applauds their professionalism and dedication shown throughout the process.

65. Since China's first FSAP in 2009, the CSRC has placed high importance and taken real actions on the recommendations made in the assessment reports, achieving significant progress in many areas identified for action. Specifically, the CSRC has continued to develop China's multi-tiered capital markets to support national development strategies and the real economy; enhanced communication and coordination on financial regulatory policies under the Joint-Ministerial Conference (JMC) spearheaded by the PBC; strengthened the regulation of listed companies and intermediaries by raising quality standards for listed companies and requirements for intermediaries in regard to risk management and internal control; improved the mechanism for risk monitoring, surveillance and contingency response in capital markets; fought forcefully against violations and misconduct to provide effective protection for investors' legitimate rights and

interests; steadily expanded two-way opening-up of China's capital markets; and established a database on the integrity record of market participants and promoted the use of information technology in regulation.

66. This year's assessment report objectively depicts the current stage of development of China's securities and futures markets, acknowledges that the regulatory framework is largely compliant with the IOSCO Principles, and recognizes the authorities' efforts to mitigate risks, deepen reforms, and promote development in the context of China's capital markets since the first FSAP. In particular, the report points out that China's innovative approaches to investor protection and market surveillance could serve as a reference for other jurisdictions. In the meantime, the report also notes some specific challenges faced by China's capital markets at the current stage.

67. The report gives recommendations to increase regulatory resources, strengthen regulatory coordination and information sharing, improve governance practices of listed companies, strengthen regulators' investigation and enforcement powers, increase the intensity of supervision on capital market gatekeepers, consider creating an independent authority for audit oversight, bolster the risk management function of the futures market, explore differentiated regulation of hedge funds. Such recommendations are very much in line with the authorities' philosophy of pursuing law-based, comprehensive, and strict regulation, and will be of great value to the authorities when strengthening the legal and regulatory framework of China's capital markets.

68. The continued deepening of financial markets in recent years and the wide use of cross-sector and cross-market financial instruments have given rise to a higher likelihood of intertwined and magnified financial risks, presenting new challenges to and higher requirements for the regulators. Regarding some specific issues discussed in the assessment report, the CSRC would like to further clarify its views. **With respect to harmonized regulation of like products,** under the leadership of the PBC, financial regulators have reached important consensus on harmonizing regulation of asset management products and services and are developing unified regulatory rules. The CSRC will, under the guidance of the Financial Stability and Development Commission (FSDC) of the State Council, continue to enhance regulatory coordination with other regulators in order to eliminate supervisory shortfalls, prevent financial risks, and safeguard national financial security and the sound development of the capital markets. **With respect to the use of criminal enforcement,** over the past few years, the CSRC has strengthened cooperation with judicial authorities to impose stricter criminal sanctions against securities crimes. Synergies are created through coordinated administrative and criminal investigations to ensure timely information sharing between securities regulators and public security authorities. Moreover, the police force has established specialized offices targeted on criminal offenses in the securities and futures markets. The CSRC will act upon recommendations in the report and continue to assist China's legislature to expand the scope of applicability and increase the level of sanctions of the *Criminal Law* with regard to securities crimes. **With respect to information disclosure by listed companies,** the CSRC has employed a disclosure-focused supervisory regime and steadily raised the transparency of listed companies. As the next step, the CSRC will analyze the specific

recommendations in the report on expanding the coverage of periodic report review, shortening deadlines for submitting annual reports and extending the notice period for *ad hoc* shareholder meetings in light of China's situation. **With respect to preventing conflicts of interest**, the *Securities Law* prohibits the CSRC staff from holding or trading stocks. In practice, the CSRC has set out even more stringent requirements, e.g., disallowing the staff to open securities accounts, thus eliminating the possibility for them to hold, let alone trade bonds on the stock exchanges. In addition, the CSRC has issued specific rules to regulate the trading of securities investment funds by its staff. Such rules have proved effective in maintaining high standards of integrity and preventing conflicts of interest for the staff.

69. The CSRC believes that recommendations and action points proposed in the report will not only facilitate future plans of the regulators, but also foster consensus among regulators, legislators and other stakeholders to create a positive environment for the reform and development of the capital markets. Pressing ahead with reforms would require efforts of the CSRC as well as support from many external authorities. Going forward, the CSRC will pay special attention to drawing on the comments and recommendations and apply international standards to the particular circumstances in China and its capital markets. The CSRC will, sticking to the market-oriented and law-based reform path with a global vision, accelerate the formation of multi-tiered capital markets that feature full range of financing functions, sound underlying structures, effective regulatory regime and adequate investor protection, thereby enabling the markets to better support China's real economy and become more resilient to financial risks.

Table 7. China: Summary Implementation of the IOSCO Principles—Detailed Assessment

Core Principle	Comments
1. The responsibilities of the Regulator should be clear and objectively stated.	The CSRC is the main regulator of the securities and futures markets. Its mandate derives mainly from the Securities Law, the Fund Law and the Regulations for the Administration of Futures Trading. Other authorities have specific competencies over certain sub-segments of the markets, and as a result in some cases a plurality of regulatory authorities have jurisdiction over an activity, a market or a product. In particular that is the case for the provision of asset management services, and the bond markets including asset backed securities and the provision of credit rating services which are subject to the regulation and supervision of more than one authority. On the former, CSRC, CBRC and CIRC have regulatory responsibilities depending on the entity involved in the provision of the services. On the latter, under the authorization of the Law on the People's Bank of China, the PBC is the regulatory authority in the interbank bond market, while the CSRC regulates and supervises the exchange market and the NDRC has authority over the enterprise bond market. In some cases, the differences in the regimes could have an impact on investor protection, market liquidity and/or financial stability. Particularly regarding asset management services and bond markets the authorities have reached agreements to work towards the harmonization of regulations, and there is already a unified draft regulation for the provision of credit rating services. In addition, the authorities have been working to strengthen coordination and cooperation arrangements. Recent improvements have also been

Core Principle	Comments
	made to the regulatory framework for the regional equity trading platforms, which are subject to day to day regulation and supervision by the provincial authorities, with a stronger role being provided to the CSRC. Mechanisms exist for coordination and cooperation among the financial regulatory authorities, including the Financial Crisis Response Group (FCRG) at the systemic risk level, and the JMC and the JMC for Bonds led by the PBC under authorization of the SC both of which are aimed at improving regulatory coordination of cross-sectoral issues.
2. The Regulator should be operationally independent and accountable in the exercise of its functions and powers.	CSRC's strategic priorities are driven by the NPC and SC to which it is accountable. In its day-to-day operations, the CSRC operates without the need for approval from any authority and the legal framework provides adequate protection to staff against legal suits resulting from the discharge of their functions. However certain features of the legal framework might pose challenges to its operational independence. In particular, the budget has not kept pace with market growth, regulatory demands or mandate changes and thus is no longer adequate. Other issues that might give rise to concerns are the review of decisions of the CSRC by the SC and the framework for the dismissal of the executive team; however, in both cases other provisions in the legal framework help to mitigate such concerns. The CSRC is subject to high standards of transparency and procedural fairness, including the need to provide reasons for its decisions and to provide an opportunity to the parties affected by a decision to be heard. Its decisions are subject to judicial review. Strong confidentiality provisions apply to commercially sensitive information.
3. The Regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.	In general, the CSRC has broad powers to regulate and supervise the securities and futures markets. Such powers include rulemaking, licensing, supervision including carrying on-site inspections, investigations and enforcement. However, the legal and regulatory framework for administrative sanctions has deficiencies; the main one being the low level of fines that can be imposed for some misconduct. The CSRC has taken steps to provide more facilities for smaller investors so that they can exercise more actively their private rights including strengthening of alternative resolution schemes and the creation of the CSISC that can represent investors in civil suits. CSRC budget has not kept up with market growth, or with its expanding mandate. In addition, the salaries that it can pay are not competitive with the industry and this has affected its ability to hire and retain staff. Altogether these factors can affect CSRC's ability to deliver its supervisory and enforcement program in a rapidly growing market. The CSRC places a high priority on investor protection initiatives, including those related to investor education, where several innovative initiatives have been implemented.
4. The Regulator should adopt clear and consistent regulatory processes.	The CSRC has adopted a transparent process for rulemaking, which includes consultation with the market and the public; the latter mainly via simultaneous publication of rulemaking proposals on the website for the Legislative Affairs Office of the SC in addition to the CSRC website. The criteria to decide on licenses and to impose sanctions are established by law and regulations which are all publicly available through the CSRC

Core Principle	Comments
	website. There are robust requirements aimed at ensuring procedural fairness. There is a tradition of use of pilots for the implementation of regulations that could have significant impact in the market. Starting in 2015, pilots have been undertaken under a set of rules or self-regulatory standards which provides certainty to the market regarding the scope and conditions of the pilot; thus mitigating concerns of their potential to give rise to unlevelled playing field.
5. The staff of the Regulator should observe the highest professional standards, including appropriate standards of confidentiality.	CSRC staff is subject to high ethical standards, including the prohibition on occupying positions in regulated entities; the obligation to recuse in cases of conflict, the prohibition on accepting gains; and cooling-off periods. Staff is prohibited from holding shares and futures; but they can hold and own bonds and mutual funds. For midlevel staff and up, annual disclosure of holdings is required. Staff is also subject to confidentiality provisions. Breaches of these obligations carry disciplinary consequences and, depending on the case, administrative penalties and even criminal penalties (in the case of disclosure of inside information). There is evidence that the CSRC has actively acted against corruption.
6. The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate.	The CSRC has developed a series of tools to identify and manage systemic risk including (i) a set of indicators for intermediaries, for market infrastructure, for the market and macroeconomic indicators; (ii) a contingency response mechanism for the stock market; and (iii) stress testing, all of which complement the regular mechanisms to monitor the markets, market infrastructure and intermediaries. A steering group on stock market risk monitoring and response was set up, which meets on a quarterly basis to assess the risk profile of the market, identify potential risk and make corresponding recommendations. In tandem, the CSRC is stepping up its ability to collect and use data to monitor risks, mainly via (i) the creation of the Capital Markets Statistics and Monitoring Center in charge of data collection, analysis and risk identification and, (ii) the development of the Central Regulatory Information Platform, which is an integrated system for the aggregation and sharing of information. The platform will significantly increase the level of digital monitoring and smart monitoring of risks. The authorities have been strengthening cross-sectoral mechanisms to share information, identify and monitor systemic risk. In particular, they are working to enhance data sharing on asset management and standardizing data. They are also working towards enhanced data sharing regarding bond markets.
7. The Regulator should have or contribute to a process to review the perimeter of regulation regularly.	There are several sources of emerging risk identification, from referrals by the SC to the regular processes in place to supervise regulated entities. The steering group on stock market risks serves also as a regular forum for discussion of major potential risks. When issues identified are within the jurisdiction of the CSRC, they are tackled through rulemaking, supervision and/or enforcement actions. There is evidence of continuous enhancements to the rules and regulations, triggered by findings from such supervisory activities and/or referrals; as well as of changes in the organizational structure to give appropriate response to new challenges. In the case of new issues or issues involving a plurality of authorities, they are

Core Principle	Comments
	brought for discussion at JMC level and then reported to the SC. There is also evidence that such mechanism has been used. The CSRC has participated actively in the review of the Securities Law and the development of a Futures Law; in both cases drafts are currently under consideration.
8. The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed.	There are rules in place that require intermediaries to establish controls to address conflict of interest. In addition, specific prohibitions apply for particular sets of intermediaries aimed at prohibiting specific activities that might pose substantial risk of conflict. Compliance with these rules is monitored through the regular supervisory programs of the CSRC. In the case of issuers, misalignment of incentives is mainly managed through disclosure obligations, which are monitored by both the exchanges and the CSRC through their off-site monitoring programs. In addition, the CSRC has an on-site inspection program for issuers. In the case of securitization, the current regulatory regimes by PBC, CSRC and CBRC only allow their placement to qualified investors, and general disclosure obligations apply.
9. Where the regulatory system makes use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, such SROs should be subject to the oversight of the Regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.	Market institutions such as the exchanges and industry associations for securities companies, futures companies and asset managers have SRO functions assigned to them by the legislation. Exchanges are responsible for the supervision of their markets, market participants, and listed companies—the last only for equity exchanges. Membership in an industry association is mandatory for all relevant intermediaries, and associations make rules that are binding on their members. In practice, all SROs have developed off-site and onsite inspections programs to carry out their supervision responsibilities, although the resources assigned appear limited, particularly at industry associations. The programs are run independently from the CSRC programs; however, mechanisms for coordination are being developed. The CSRC exercises oversight over the exchanges and industry associations through a combination of tools that include participation in the rulemaking process, reporting obligations, participation in the appointment of key personnel (in the case of the exchanges) and appointment of representatives in key organs (in the case of the industry associations). Increasingly inspections are also being used.
10. The Regulator should have comprehensive inspection, investigation and surveillance powers.	The CSRC has the authority to inspect regulated entities and to require from them any information that it needs concerning their operations. Recordkeeping obligations exist for all intermediaries, which in general extend for 20 years.
11. The Regulator should have comprehensive enforcement powers.	The CSRC has the authority to investigate violations of the laws and regulations under its jurisdiction. To this end, it can request explanations and information from any entity or person involved in the event under investigation. There are specific provisions that require banks to cooperate with the CSRC and provide it with information concerning banking records. The CSRC has the obligation to report violations that may constitute a crime to the criminal authorities. This is done through the Enforcement Bureau. The CSRC has the authority to impose regulatory measures on

Core Principle	Comments
	regulated entities; and administrative sanctions on regulated entities and third parties that violate the laws and regulations for the securities and futures markets. Administrative sanctions include confiscation of illegal gains, money penalties and market bans. However, the legal framework for administrative sanctions has deficiencies; the main one being the low levels of fines that can be imposed for some misconduct.
12. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.	The CSRC has implemented a supervisory program that reasonably covers all intermediaries under its remit, gatekeepers and other regulated entities, through off-site monitoring and on-site inspections; however, the coverage of the programs should be kept under review. The CSRC is moving towards using administrative measures and sanctions in a more vigorous way, including through the imposition of larger monetary penalties and bans on a full range of market participants. However, this more vigorous approach towards enforcement still needs time to take hold. More importantly, the use of criminal enforcement and in particular actual imprisonment has been limited. This can significantly limit the deterrence effect that enforcement is intended to achieve. The criminal authorities have taken recent steps to strengthen their ability to pursue these types of cases via the creation of centralized teams and larger prison sentences are starting to be applied.
13. The Regulator should have authority to share both public and nonpublic information with domestic and foreign counterparts.	The CSRC has the obligation to establish mechanisms for sharing regulatory and supervisory information with other domestic financial regulatory authorities. It also has the power to establish arrangements with foreign securities and futures regulators for supervisory cooperation in relation to cross-border matters. The CSRC is not required to obtain any external approval to establish such mechanisms or arrangements nor is it limited in the type of information that it can share. The CSRC is able to share both public and non-public information on all the areas mentioned in the IOSCO methodology and it is not required to have an independent interest in the matter to provide cooperation.
14. Regulators should establish information sharing mechanisms that set out when and how they will share both public and nonpublic information with their domestic and foreign counterparts.	There are mechanisms in place for cooperation at both the domestic and international level. At the domestic level, coordination and cooperation on systemic issues takes place via the FCRG, and on policy issues via the JMC and the JMC for bonds. There is also a MoU between the CBRC, CIRC and CSRC that establish principles for cooperation and exchange of information among the Commissions. At the international level the CSRC is signatory to the IOSCO MMoU, as well as a significant number of bilateral MoUs with foreign securities and futures regulators. The CSRC actively responds to and increasingly makes requests for information and assistance from foreign regulators.
15. The regulatory system should allow for assistance to be provided to foreign Regulators who need to make inquiries in the discharge of their functions and exercise of their powers.	The CSRC is able to collect information that is not already in its files on behalf of foreign regulators as required by the IOSCO Principles and the IOSCO MMoU. It can use all its investigative powers to this end. There is evidence that the CSRC has used its powers to cooperate with foreign regulators.

Core Principle	Comments
16. There should be full, accurate and timely disclosure of financial results, risk and other information that is material to investors' decisions.	Companies can issue securities to the public either via the regulatory regime of the CSRC or, in the case of enterprise bonds, the regulatory regime of the NDRC. In both cases a merit approval system is in place and issuers must submit a prospectus for the review of the respective authority. Companies can also issue securities in the interbank bond market, but in such case their offering is restricted to qualified investors. Companies that offer securities to the public are subject to periodic and ongoing obligations including publication of annual and semi-annual reports, and the prompt disclosure of material events. Equity issuers also have to issue quarterly reports. Companies that issue securities to the public under the CSRC framework are required to be listed. Enterprise bond issuers can choose whether to list on the exchanges or trade in the interbank bond market, and the requirements of the respective trading venue apply to them. In the case of listed issuers, monitoring of ongoing obligations is conducted mainly via off-site monitoring by the exchanges. In addition, the CSRC has a program of review of annual reports aimed at assessing compliance with accounting standards and some regional offices conduct their own reviews of annual reports. A program of on-site inspections is also in place at both the CSRC and NDRC.
17. Holders of securities in a company should be treated in a fair and equitable manner.	The regulatory regime provides safeguards to ensure that holders of securities are treated fairly and equitably. In particular, the legal and regulatory framework requires shareholders' approval of major transactions and information obligations are in place to ensure that shareholders can take informed decisions. The Takeover Measures provide a framework for changes in control transactions to be conducted fairly and with full disclosure. To this end, a tender offer report must be submitted to the CSRC and published. In case of partial offers, a pro-rata principle applies. Prompt notification of holdings by substantial shareholders and insiders is required. Compliance with these requirements is mainly monitored by the exchanges.
18. Accounting standards used by issuers to prepare financial statements should be of a high and internationally acceptable quality.	Financial statements required to be included in prospectuses and in the periodic reports of public issuers must be prepared according to the ASBE. ASBE have substantially converged with the IFRS. Current mechanisms to supervise compliance with accounting standards include the review of financial statements by the CSRC and the complementary review of periodic reports by the exchanges.
19. Auditors should be subject to adequate levels of oversight.	The MoF is the competent authority for CPAs. In addition, audit firms that provide audit services for the securities and futures market must obtain a securities services license jointly issued by the CSRC and the MoF, met licensing requirements on an ongoing basis and remain subject to the CSRC's ongoing supervision, which it exercises primarily through on-site inspections. On-site inspections include comprehensive and targeted inspections. Comprehensive inspections are limited. Targeted inspections are used by the CSRC to ensure that the majority of audit firms are subject to some level of inspection once every three years.

Core Principle	Comments
20. Auditors should be independent of the issuing entity that they audit.	Independence requirements for audit firms have converged with the international standards. Supervision of auditors' compliance with such requirements involves monitoring by the firm itself, the audit committees of listed companies and the supervisory program of the CSRC. In addition, the MoF performs the supervisory function on the industry while the Chinese Institute of Certified Public Accountants (CICPA) is the industry SRO.
21. Audit standards should be of a high and internationally acceptable quality.	The Chinese standards of auditing have fully converged with the International Standards of Auditing (ISA). Supervision of audit firm's compliance with the standards of auditing involves monitoring by the firm itself and the CSRC's program of on-site inspection of the audit firms licensed to provide securities services. In addition, the MoF performs the supervisory function on the auditing industry while the CICPA is the industry SRO.
22. Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision.	The PBC is the lead regulatory agency for the provision of credit rating services. All firms that want to provide this type of service must fulfill the record filing procedures regulated by the PBC. In addition, a firm must obtain a license or recognition from the regulatory authority of the market in which the companies rated will issue the securities. In practice, there is significant overlap in the CRAs authorized by the different regulators to provide services for these markets. CRAs that want to obtain a CSRC license are subject to governance requirements that address the quality and integrity of the rating process, independence and the avoidance of conflicts of interest, and responsibilities to the investing public and rated entities. Ongoing supervision includes off-site monitoring through periodic reporting requirements and on-site inspections. In practice the CSRC has conducted on-site inspections on all CRAs.
23. Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.	The provision of securities and futures research reports falls under the definition of engaging in the business of providing securities and futures investment consultancy and therefore is subject to license. Securities and futures companies and their staff who provide research reports are also required to obtain CSRC's approval. Securities analysts are subject to specific requirements mainly aimed at addressing potential conflicts of interest, including by requiring disclosure by the firms of their holdings and other type of conflicts, and by establishing rules applicable to the analysts themselves. As most firms providing securities research are securities companies, ongoing supervision of compliance is conducted as part of the supervisory program for securities companies.
24. The regulatory system should set standards for the eligibility, governance, organization and operational conduct of those who wish to market or operate a CIS.	Pursuant to the Funds Law, the management of funds that are offered to the public can only be done by fund management companies and other entities authorized by the CSRC. In all cases licensing requirements include capital requirements, and organizational requirements. An on-site inspection is conducted as part of the licensing process. Fund management companies are subject to reporting requirements that include quarterly, semi-annual and annual reports. In addition, the CSRC conducts onsite inspections to verify compliance with their obligations, under a risk-based approach. Inspections are mainly carried out by the CSRC regional offices, with an active role from CSRC central office via the definition of themes for

Core Principle	Comments
	<p>annual inspections. In practice during the last years, all fund managers have been subject to some level of annual on-site inspection. Distributors of funds are also subject to licensing by the CSRC, periodic reporting and on-site inspections. Fund managers are subject to record keeping obligations. They are required to place the interest of investors first. There are rules in place to manage conflict of interest, including those arisen from the possibility given to fund managers to do some of the trading for the funds they manage (rent seats). Delegation is permitted, but the manager retains responsibility.</p> <p>Banks can offer WMPs to retail investors, some of which products substantively are CIS. In the provision of such activity, banks are subject to strong organizational requirements. They are also subject to reporting obligations that include monthly, quarterly and annual reports. The CBRC conducts on-site inspection of banks' compliance with obligations relating to the provision of WMPs, under a risk-based approach. Banks are also subject to record keeping obligations. They are subject to rules on conflict of interest. Delegation is also permitted, but the banks retains responsibility.</p>
<p>25. The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.</p>	<p>Pursuant to the Funds Law, funds under the CSRC are established via a contract, and do not have separate legal personality. Funds must have a custodian, which is in charge of the safekeeping of assets as well as of monitoring fund managers' compliance with their obligations. Custodians need to be separate entities, but can be associated with the fund management company. There are explicit provisions in the Fund Law that establish a strict separation of the assets of the fund from the assets of the fund management company and the custodian, and thus protect investors in the event of a bankruptcy of the fund management company and the custodian.</p> <p>Pursuant to CBRC regulations, WMPs under the CBRC are also established via a contract and do not have legal personality. Regulations of the CBRC and the MoF require strict segregation and separate accounting for each WMP. WMPs assets must be held by a custodian bank, but a bank that is a licensed custodian can hold assets of that bank's WMPs. There have not been cases of banks' insolvencies leading to questions concerning WMPs' protection; as a result, there is legal uncertainty regarding the treatment of WMP assets in the event of insolvency of the bank.</p>
<p>26. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a CIS for a particular investor and the value of the investor's interest in the scheme.</p>	<p>Funds under the jurisdiction of the CSRC are required to submit a prospectus for the approval of the CSRC ahead of the offering. Specific legal and regulatory provisions govern the content of the prospectus, which is in line with international standards. In addition, funds are required to provide prompt quarterly, semi-annual and annual reports to investors. They are also subject to prompt material events disclosure. Changes must be notified to investors, and some require their approval. There are specific rules concerning advertisements that prohibit funds from promising returns, misleading investors or using expected returns in their prospectus and their advertisement material.</p>

Core Principle	Comments
	<p>Banks must submit a series of disclosure and sales information to the CBRC 10 days before starting to offer a WMP. For new types of products prior approval is required. A prospectus is part of the documentation to be submitted, along with a risk statement. However, the regulatory requirements for the content of this disclosure are high level. WMPs are required to provide monthly reports to investors, and a report upon liquidation. Changes in the scope of investment and in fees must be disclosed to investors before they are implemented. There are rules concerning advertisements that prohibit banks from promising returns and, more generally, from misleading investors; however, banks can include expected returns in their prospectuses and market material.</p>
<p>27. Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a CIS.</p>	<p>Funds under CSRC jurisdiction are required to prepare their financial statements in accordance with ASBE. There is specific guidance for the valuation of assets where market price is not available. Open-end funds must disclose the NAV per unit daily, while closed end funds must disclose it at least weekly. There are specific rules regarding pricing errors and the fund unit holders can ask for compensation from fund manager and fund custodian for losses caused by such errors. The regulatory regime prescribes specific circumstances under which redemptions can be suspended; in all such cases the fund manager is required to report the suspension to the CSRC. Money market funds are authorized to value their assets at amortized cost and keep a stable NAV, although specific conditions must be met. However, current regulations still allow for significant credit and market risks at these funds that could also impact a fund's ability to meet redemption obligations. The CSRC recently released a new rule for the liquidity risk management of open-ended securities investment funds. The rule, effective October 1, proposes revisions to the valuation methods of MMFs and liquidity management tools under circumstances of substantial redemptions.</p> <p>WMPs are required to prepare their financial statements according to ASBE. All WMPs, including those that operate like MMFs, must value their assets and participations at fair value. The current regulations do not contain specific provisions on minimum standards for subscription and redemption pricing, pricing errors, or on the possibility of suspensions or deferrals of redemption. However, banks are required to establish internal rules and controls for their WMPs; these issues need to be covered by the rules and the corresponding disclosures made to investors via the sales documents.</p>
<p>28. Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight.</p>	<p>There is currently no definition of HF in the jurisdiction. At the time of the assessment, the number of private funds that might be considered a HF was not significant. Such funds are covered by the regulations on private funds. Pursuant to this regime fund managers that manage private securities investment funds, and the private funds themselves, are subject to registration with AMAC. AMAC's rules require fund managers to comply with internal control requirements and as part of the registration process, it requires a legal opinion on the company meeting such requirements. Private funds report every quarter. AMAC has also promulgated rules on leverage. The CSRC and AMAC conduct on-site inspections on HF</p>

Core Principle	Comments
	managers. While the program is limited, at present it appears to be commensurate to the risks that HFs seem to pose to the system.
29. Regulation should provide for minimum entry standards for market intermediaries.	Securities companies, futures companies, fund management companies and investment consultancy firms are all subject to licensing by the CSRC. For all but investment consultancy firms that only provide advice, the requirements include minimum and ongoing capital requirements, as well as robust organizational requirements. On-site inspections are conducted as part of the licensing process. Major changes need to be approved by the CSRC. The CSRC keeps a registry of licensed entities, which is also available to the public.
30. There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.	Securities companies, fund management companies and futures companies are subject to minimum and ongoing capital requirements. The main requirement is a net capital rule, which has an imbedded leverage ratio. In addition, securities companies are subject to two liquidity ratios. All firms must report their capital on a monthly basis (and securities companies must calculate it on a daily basis). They must also provide early warning reports when capital or certain risk indicators fall below trigger points. For securities companies these reports are due within three days, while for futures companies they are due within the same day of reaching the threshold. Equity in subsidiaries is fully deducted. A more comprehensive framework to address risks from outside the regulated entity is being piloted in a selected number of securities companies.
31. Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters.	<p>Securities companies, fund management companies and futures companies are required to have in place robust internal controls and risk management requirements. In addition, they are required to have a compliance function. All intermediaries are required to prepare and submit to the CSRC an annual report on internal controls, which needs to be assessed by the external auditing firm. All intermediaries are subject to a unified system of suitability requirements in the offering and distribution of products and information obligations towards their clients. They are also required to set up mechanisms to deal with complaints. All these obligations are mainly monitored through a program of on-site inspections, which is risk-based. Inspections are carried out primarily by the CSRC regional offices, with an active role from CSRC central office via the definition of themes for annual inspections.</p> <p>Banks providing wealth management services that involve securities are required to have strong internal controls and risk management systems. There are detailed rules for internal supervision (compliance) and the board and senior management must directly oversee these arrangements. There are strong suitability requirements for banks distributing WMPs to their clients, and clients must be given statements of account and quarterly financial reports. Banks must also establish procedures for dealing with client complaints. Compliance with these obligations is monitored by on-site inspections carried out by the CBRC, which are risk-based.</p>
32. There should be a procedure for dealing with the	An early warning system is in place to monitor the capital of securities intermediaries. The CSRC has plans in place and sufficient tools at its

Core Principle	Comments
failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.	disposal to deal with distressed firms. There are specific rules to deal with the failure of a securities intermediary, which have been tested. There are mechanisms in place in both the securities and futures markets to protect clients' assets in the event of the failure of an intermediary. For securities markets, ownership of securities is registered directly at the investors' level in the CSDC, while cash must be kept in individualized accounts on the name of the investor at deposit banks. In case of losses, the Securities Investor Protection Fund (SIPF) has rules that protect the cash of investors. For futures markets, margins are deposited in individualized accounts in the name of the investor, thus ensuring full portability and the Futures Investor Protection Fund (FIPF) is available to meet client margin losses.
33. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.	The constitution of equity and futures markets is subject to the approval of the SC, upon a recommendation of the CSRC, in the case of equity markets and the CSRC in the case of futures markets. In all cases the authorization is conditioned on meeting a set of organizational, risk management and technological requirements. Exchanges are required to submit annual independent evaluations of their IT systems. There are no circuit breakers, but other measures are in place to deal with volatility such as price limits and, for futures markets, also the possibility of increasing margins, as well as position limits. In addition, exchanges can suspend trading.
34. There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.	The exchanges are the front line supervisors of the markets. They have automated surveillance systems that allow them to conduct real time surveillance for purpose of ensuring orderly trading. They also conduct ex-post monitoring to support CSRC in the identification of unfair trading practices. To this end all the exchanges have established market surveillance teams to follow up on leads. The CSRC has established a program for the supervision of the exchanges that includes the approval of their rules and new products, reporting requirements, on-site inspections and approval of the appointment of key personnel.
35. Regulation should promote transparency of trading.	Exchanges are subject to pre-and post-trade transparency requirements. As for pre-trade transparency, most –but not all--exchanges display at least the five best bids and offers. Neither iceberg orders nor dark orders are permitted. Under the current framework, all transactions must be conducted on the exchanges. Block trades can be negotiated off the market, but must be reported to and confirmed by the exchanges.
36. Regulation should be designed to detect and deter manipulation and other unfair trading practices.	The exchanges have automated surveillance systems designed to identify unfair trading practices. In general, they have assigned sufficient resources to the investigation of such practices. If cases are complex, and/or involve the violation of laws then they are transmitted to the CSRC for their follow up. Mechanisms have been established for cross-market supervision, in particular there is a dedicated data feed to share information. Mechanisms have also been established for cross-market surveillance with Stock Connect. There is evidence that the CSRC is taking a stronger stance in connection with enforcement cases including those related to unfair trading practices such as insider trading and market abuse. In addition, it is also referring a significant amount of clues to the criminal authorities. While

Core Principle	Comments
	criminal judgments exist, in general criminal enforcement is still weak, although the criminal authorities have taken recent steps to strengthen their ability to pursue these types of cases via the creation of centralized teams and larger prison sentences are starting to be applied. These actions require time to take hold.
37. Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.	All exchanges have CCPs. The CSDC is the CCP for all the equity exchanges, while the futures exchanges themselves act as the CCPs for their markets. All exchanges have established mechanisms to address clearing and settlement risks, and the risks of large exposures. In the case of the equity markets, the main requirements are access criteria for clearing members, settlement margins, collateral requirements, a guarantee fund and a risk reserve fund. Large holdings can be directly monitored by the exchanges and the CSRC as each client is required to have a single identification number. In the case of futures markets, the main requirements also include access criteria for clearing members, margin requirements, mark to market of positions on a daily basis, position limits, a guarantee fund and a risk reserve fund. A large positions' report has also been implemented. There are clear mechanisms to deal with the default of a clearing member. Only covered short selling is allowed, and is subject to disclosure obligations.

Table 8. China: Recommended Action Plan to Improve Implementation of the IOSCO Principles

Core Principle	Recommendations
<p>1. The responsibilities of the Regulator should be clear and objectively stated.</p> <p>(Cross linkages to Principles 8, 16, 24-27, 28, 31 and 33.)</p>	<ul style="list-style-type: none"> The authorities should implement the agreements reached in the JMC aimed at developing harmonized regulations for asset management services, while allowing for differentiation based on the type of products, the type of investors to which they are offered and the systemic importance of the products. In this context, there could potentially be three different "sets" of regulations: (i) one for CIS offered to retail investors, which should be developed based on the requirements imposed by the IOSCO Principles and Methodology. In this context, the authorities are encouraged to consider the application of disclosure and conduct obligations of CIS to insurance products that have an investment component such as unit-linked products, (ii) one for CIS offered to non-retail; in this case the regulations should be flexible enough to allow different investment strategies and structures, while ensuring that the authorities are able to monitor their potential systemic implications and impose prudential requirements if and when necessary for purposes of ensuring financial stability, including in the case of HFs as required by the IOSCO Principles and Methodology; and (iii) finally a set of regulations for other asset management services (individual and portfolio management and advisory services).

Core Principle	Recommendations
	<ul style="list-style-type: none"> • In tandem, coordination and cooperation arrangements should continue to be strengthened to ensure consistent administration of these regulations. • The authorities should continue to actively implement the agreements reached in the JMC for Bonds aimed at (i) unifying the issuance criteria and disclosure requirements gradually in accordance with the principle that like products should be subject to unified regulatory rules; (ii) establishing appropriate mechanisms for coordination, (iii) promoting cross-market issuance and (iv) engaging the CSRC in cross-market enforcement. • The authorities should continue working towards the implementation of a single regulatory regime for CRAs, via the draft regulation currently under consultation. The authorities should ensure that such draft meets the requirements set forth in the IOSCO Principles and Methodology. • In the medium term, the authorities should work toward the development of harmonized regulations for ABS. In this context, and in anticipation of the expected changes to the IOSCO Methodology, the authorities are encouraged to consider the following issues: (i) the need for strong disclosure obligations, not just at the moment of issuance but over the life cycle of the underlying assets, potentially supported by the development of standardized disclosure templates, and (ii) the need for retention requirements. • The CSRC along with relevant authorities should continue working towards the implementation of a stronger framework for the regulation and supervision of the regional equity trading platforms. The CSRC should give priority to the development and implementation of the corresponding code of conduct and to the establishment of adequate mechanism for the oversight of these platforms, supported by strong reporting requirements by the trading platforms to the CSRC. • In the long run, the authorities are encouraged to consider the development of a unified regulatory framework for all non-exchange trading platforms. Such a framework would establish operational criteria applicable to all platforms, while allowing for differentiation between types of platforms and the role of the CSRC in their supervision based on criteria including their size and importance as well as the type of investors that have access to them. • The CSRC should develop regulations for equity crowdfunding. More generally, the authorities are encouraged to review whether any gaps in the regulation of online financing remain. • In anticipation of changes to the Methodology, the authorities are encouraged to consider whether there is a need to further strengthen the framework for OTC derivatives transactions. • The authorities are encouraged to finalize the drafts for a new Securities Law and a Futures Law.

Core Principle	Recommendations
	<ul style="list-style-type: none"> The CSRC and CBRC are encouraged to consider whether current rules and regulations could be consolidated into fewer number of normative documents thus enhancing clarity and certainty of the framework that applies to specific activities.
<p>2,3</p> <p>2. The Regulator should be operationally independent and accountable in the exercise of its functions and powers; and</p> <p>3. The Regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.</p>	<ul style="list-style-type: none"> The authorities should consider providing the CSRC with greater autonomy to decide on the number of staff and to have a separate salary scale to allow is to hire and retain qualified personnel. The authorities should consider transferring the responsibility for approval of equity exchanges and markets more generally to the CSRC.
<p>3, 11, 36</p> <p>3. The Regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.</p> <p>11. The Regulator should have comprehensive enforcement powers.</p> <p>36. Regulation should be designed to detect and deter manipulation and other unfair trading practices.</p>	<ul style="list-style-type: none"> The authorities should prioritize the review of the legal and regulatory regime for administrative sanctions to increase the level of penalties that can be applied where the current levels are too low and to ensure that the same misconduct across the securities and futures market is subject to the same level of penalties. The CSRC is encouraged to work actively with the criminal authorities to ensure that the sanctions that can be applied in criminal cases (including terms of imprisonment) provide sufficient deterrent effect.
<p>4. The Regulator should adopt clear and consistent regulatory processes.</p>	<ul style="list-style-type: none"> The CSRC is encouraged to monitor the implementation of pilot programs with a view to ensuring that the potential for unlevelled playing field does not arise in practice. In addition, the CSRC is encouraged to consider whether additional transparency can be brought to the selection process.
<p>5. The staff of the Regulator should observe the highest professional standards, including appropriate standards of confidentiality.</p>	<ul style="list-style-type: none"> The CSRC should implement a system of prompt notification of any change in holdings of securities by its staff.
<p>6. The Regulator should have or contribute to a process to monitor, mitigate and manage</p>	<ul style="list-style-type: none"> The CSRC should continue to enhance the tools used to monitor all the markets under its supervision.

Core Principle	Recommendations
systemic risk, appropriate to its mandate.	<ul style="list-style-type: none"> • In addition, the CSRC is encouraged to consider expanding the mandate of the stock market crisis group so that it becomes the regular venue to discuss all emerging and systemic risks on a periodic basis. • If it has not done so, the CSRC should incorporate market intelligence meetings to the tools available for systemic risk identification. • The authorities should continue to strengthen current cross-sectoral mechanisms to share information, and monitor risks. In particular, data sharing on asset management should continue to be expanded, and efforts to standardize data be given full priority. The authorities should also explore the implementation of improvements in the mechanisms to jointly monitor risks stemming from the bond markets. • More generally, the authorities are encouraged to consider further strengthening of the institutional framework for systemic risk identification.
7. The Regulator should have or contribute to a process to review the perimeter of regulation regularly.	<ul style="list-style-type: none"> • The CSRC is encouraged to consider the development of a more structured framework for the identification of emerging risks that considers their impact and probability as first step to determine the actions to take. In tandem, a risk registry could be implemented.
8. The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed.	<ul style="list-style-type: none"> • The CSRC is encouraged to continue paying attention to governance practices in listed companies as they are key to the protection of minority shareholders. • The CSRC is encouraged to intensify the monitoring of the OTC equity markets. • The CSRC is encouraged to monitor compensation arrangements for intermediaries and how they may affect the products offered to clients, including in the context of MFs. • In anticipation of the changes to the Methodology, the authorities are encouraged to review the framework for securitization and consider the need for consistent regulations that impose (i) stronger disclosure obligations, not just at the moment of issuance but over the life cycle of the security and its underlying assets, potentially supported by the development of standardized disclosure templates, and (ii) retention requirements on the issuer/promoter.
9. Where the regulatory system makes use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, such SROs should be subject to the oversight of the Regulator and should observe standards of fairness and confidentiality when	<ul style="list-style-type: none"> • The CSRC should keep the resources of SROs under review to ensure that sufficient resources are devoted to their regulatory functions, including on-site inspections. • The CSRC should review whether comprehensive inspections of SROs are needed. • The CSRC is encouraged to require the SROs to appoint independent members in their decision-making bodies, including their disciplinary bodies.

Core Principle	Recommendations
exercising powers and delegated responsibilities.	
10. The Regulator should have comprehensive inspection, investigation and surveillance powers.	<ul style="list-style-type: none"> The authorities are encouraged to eliminate the legal authority of corporations to issue unregistered stock.
11. The Regulator should have comprehensive enforcement powers.	<ul style="list-style-type: none"> The authorities are encouraged to (i) consider changes to the legal framework in order to explicitly provide the CSRC with stronger legal backing to request testimony from third parties, and to request telephone and internet service provider (ISP) records, along with the tools to make this power effective, (ii) to review whether there is a need to strengthen the powers to freeze assets and (iii) to ensure that all these powers can be used to assist foreign regulators. The CSRC is encouraged to continue working with other authorities to address any remaining challenges that might prevent investors from effectively exercising their rights in courts if they choose to do so. In this context, a class action system could be explored, along with a change in the burden of proof. The CSRC is encouraged to continue working with other authorities to implement the multilayer system of mediation.
12. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.	<ul style="list-style-type: none"> The criminal authorities should give priority to securities markets offenses to ensure that criminal enforcement provides an effective deterrent. The CSRC should keep its enforcement strategy under monitoring to ensure that it is making appropriate use of its powers to impose administrative sanctions (monetary penalties and bans), including for breaches of business conduct obligations such as suitability rules.
12, 16, 24, 31	<ul style="list-style-type: none"> The CSRC should keep the intensity of its programs for issuer monitoring and intermediary supervision under review and calibrate their intensity as needed. The CSRC should continue to enhance its theme identification framework potentially by linking it to a more structured framework for emerging risk identification as well as its current risk monitoring framework for securities companies, and to develop a similar type of framework for futures companies and fund management companies.
14, 15 14. Regulators should establish information sharing mechanisms that set out when and how they will share both public and nonpublic information with their	<ul style="list-style-type: none"> The CSRC is encouraged to shorten the time required to answer requests for foreign assistance, particularly in cases where collection of information is required.

Core Principle	Recommendations
<p>domestic and foreign counterparts; and</p> <p>15. The regulatory system should allow for assistance to be provided to foreign Regulators who need to make inquiries in the discharge of their functions and exercise of their powers.</p>	
<p>16. There should be full, accurate and timely disclosure of financial results, risk and other information that is material to investors' decisions.</p>	<ul style="list-style-type: none"> • The CSRC is encouraged to shorten the deadlines for submission of annual financial statements at least in connection with larger companies. • The CSRC is encouraged to consider a package of measures aimed at further strengthening the role of disclosure on investment decisions including initiatives to (i) strengthen corporate governance of issuers as a key step to improve the quality of their financial disclosure, (ii) ensure that gatekeepers comply with their responsibilities, (iii) enhance investors' ability to exercise their rights and (v) foster additional participation of institutional investors into the market.
<p>17. Holders of securities in a company should be treated in a fair and equitable manner.</p>	<ul style="list-style-type: none"> • The CSRC is encouraged to consider requiring issuers to provide a longer period of notice of shareholder meetings for important matters requiring a two-third's majority.
<p>19. Auditors should be subject to adequate levels of oversight.</p>	<ul style="list-style-type: none"> • The CSRC should expand the use of comprehensive inspections for the supervision of auditors. • The authorities should explore the creation of an independent body for the oversight of auditors in the financial sector.
<p>23. Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.</p>	<ul style="list-style-type: none"> • The CSRC is encouraged to review whether adjustments are needed to the current rules for futures analysts. • The CSRC is encouraged to review the current guidelines for securities analysis in order to provide more guidance on specific conflict situations where public disclosure should be made; this would promote consistency in firms' disclosure practices.
<p>24. The regulatory system should set standards for the eligibility, governance, organization and operational conduct of those who wish to market or operate a CIS.</p>	<ul style="list-style-type: none"> • Both CSRC and CBRC should keep the intensity of their supervision of CIS under review and ensure appropriate use of the full range of enforcement actions.
<p>25. The regulatory system should provide for rules governing the legal form and structure of collective</p>	<ul style="list-style-type: none"> • The CSRC and the CBRC should consider requiring fully independent custodians. Alternatively, at a minimum, they should introduce additional measures to protect investors and their assets when self-custody or

Core Principle	Recommendations
investment schemes and the segregation and protection of client assets.	<p>related party custodians are used, including but not limited to, enhanced reporting and supervision.</p> <ul style="list-style-type: none"> The CBRC and relevant authorities should consider introducing specific provisions to ensure that WMP assets are protected if the bank that issues the WMP becomes insolvent.
26. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a CIS for a particular investor and the value of the investor's interest in the scheme.	<ul style="list-style-type: none"> The CSRC should require an updated or replacement prospectus if there are significant changes in a fund's circumstances. The CSRC is encouraged to consider requiring funds to provide investors with a simplified information document in addition to the detailed prospectus. The CBRC should prohibit the use of expected return information in non-guaranteed collective WMPs offered to retail investors. The CBRC should require WMP offer documents to contain disclosure about the methodology for valuing assets, redemption and pricing of interests, custodial arrangements and financial information about the WMP. More generally the CBRC should review whether more comprehensive guidance should be given in relation to the content of the prospectus and how to keep it up-to-date. Finally, the CBRC should review whether a more comprehensive regime for material events disclosure is needed.
27. Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a CIS.	<ul style="list-style-type: none"> The CSRC should monitor the implementation of the new framework for MMFs to assess sufficiency of changes. The CBRC should establish minimum standards for subscription and redemption pricing, pricing errors, a WMP's right to suspend or defer redemptions, and obligations to report suspensions or deferrals of redemptions to the CBRC.
28. Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight.	<ul style="list-style-type: none"> The CSRC, in coordination with AMAC should continue to monitor the HF industry to ensure that it develops in a healthy manner. If large, potentially systemically important, funds emerge, it may be necessary to take a differentiated approach to the regulation of such funds. In such an approach, the CSRC along with relevant authorities might consider a transfer of the registration of such managers and funds to the CSRC, as well as additional reporting obligations and more intense on-site supervision. Other authorities should continue to monitor non-retail asset management activity to ensure that the potential for systemic risk is identified and managed.
30, 31 30. There should be initial and ongoing capital and other prudential requirements for market intermediaries that	<ul style="list-style-type: none"> The CSRC is encouraged to consider implementing a more prompt notification requirement for deficiencies in capital in securities companies.

Core Principle	Recommendations
<p>reflect the risks that the intermediaries undertake; and</p> <p>31. Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters.</p>	
<p>31. Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters.</p>	<ul style="list-style-type: none"> Both CSRC and CBRC should keep the intensity of their supervision of intermediaries under review and ensure appropriate use of the full range of enforcement actions.
<p>33. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.</p>	<ul style="list-style-type: none"> The CSRC is encouraged to enhance the monitoring of the NEEQ market.
<p>33, 37</p> <p>33. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight; and</p> <p>37. Regulation should aim to ensure the proper management of large</p>	<ul style="list-style-type: none"> As part of the Principles for Financial Market Infrastructure (PFMI) assessment on the CCPs, the CSRC is encouraged to review whether intraday margin is needed for clearing members and if so, whether a recalibration of initial margins is warranted.

Core Principle	Recommendations
exposures, default risk and market disruption.	
35. Regulation should promote transparency of trading.	<ul style="list-style-type: none"><li data-bbox="591 342 1382 430">• The CSRC should review current transparency requirements for the exchanges and ensure that an appropriate level of pre-trade transparency applies to all of them.