

**MADE IN
CHINA:**

China's Role in Transnational Crime & Illicit Financial Flows



非法资金流动



人口贩运



贩毒



野生动物非法贩运



造假

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GLOBAL FINANCIAL INTEGRITY

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By Channing Mavrellis & John Cassara

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Preface

This report is divided into two sections. The first, authored by Channing Mavrellis, focuses on China's role in four different transnational crimes, while the second, authored by John Cassara, covers the illicit financial flows (IFFs) associated with these criminal activities. Both sections explore the dynamics of the transnational crimes and the related IFFs, discuss the unique factors in China that contribute to them, and evaluate China's response.

As China does not publish official English-language translations of their legislation and regulations, the authors have relied upon machine translation to translate any Chinese-language documents published by the People's Republic of China (PRC or China) as well as any other Chinese-language media.

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Glossary of Terms, Abbreviations, and Acronyms

Acronym/Term	Explanation
Action Plan	National Biodiversity Conservation Strategy and Action Plan (2011-2013)
ADL	Anti-Drug Law
AML	Anti-money laundering
ANPP	Anilino-nphenethylpiperidine
APT	Advanced persistent threat
ATS	Amphetamine-type stimulants
BC	British Columbia
BMPE	Black market peso exchange
BOC	Bank of China
BRI	Belt and Road Initiative
BVI	British Virgin Islands
CA	Canadian, as in CA\$
CCP	Chinese Communist Party
CECC	Congressional-Executive Commission on China
CFT	Countering the financing of terrorism
CIA	Central Intelligence Agency
CITES	Convention on the International Trade in Endangered Species of Wild Fauna and Flora
COMMIT	Coordinated Mekong Ministerial Initiative against Trafficking in the Greater Mekong Sub-region
CNIPA	China National Intellectual Property Administration
CNTC	China National Tobacco Corporation
CTIEC	China Tobacco International Europe Company
CUBS	Chinese underground banking system
<i>Daigu</i>	The purchase of overseas goods by Chinese expats on behalf of consumers in China
DAL	Drug Administration Law
DDC	Drug Distribution Certificate
DEA	Drug Enforcement Administration
Decision	Decision to Comprehensively Prohibit the Illegal Trade of Wild Animals, Eliminate the Bad Habits of Wild Animal Consumption, and Protect the Health and Safety of the People
DMC	Drug Manufacturing Certificate
DMT	Dimethyltryptamine

DPRK	Democratic People's Republic of Korea, or North Korea
DRC	Development Research Center of the State Council
DTO	Drug trafficking organization
EC	European Commission
EIA	Environmental Investigation Agency
EMCDDA	European Monitoring Centre for Drugs and Drug Addiction
EU	European Union
EUIPO	European Union Intellectual Property Office
FATF	Financial Action Task Force
FCTC	Framework Convention on Tobacco Control
<i>Fei-chien</i>	"Flying money," China's informal value transfer system
GDP	Gross domestic product
GFI	Global Financial Integrity
GI	Geographical indicator
GMP	Good manufacturing practices
GOC	Government of China
GSI	Global Slavery Index
GSP	Good Supply Practice for Pharmaceutical Products
GTSEZ	Golden Triangle Special Economic Zone
<i>Guanxi</i>	An overarching social system of rules that govern relationships and social behavior
<i>Hukou</i>	China's national household registration system
ILO	International Labor Organization
IP	Intellectual property
MAPA	Methyl alpha-phenylacetoacetate
MLO	Money laundering organization
NDU	National Defense University
NFGA	National Forestry and Grassland Administration
NMPA	National Medical Products Association (formerly the China Food & Drug Administration)
NNCC	National Narcotics Control Commission
NPC	National People's Congress
NPP	N-phenethyl-4-piperidinone
NPS	New psychoactive substances
OCCRP	Organized Crime and Corruption Reporting Project

OCG	Organized criminal group
OECD	Organization for Economic Co-operation and Development
P2P or P-2-P	Phenyl-2-propanone, also known as phenylacetone
Party	Chinese Communist Party or CCP
PPE	Personal protective equipment
PRC	People's Republic of China, or China
RMB	Chinese renminbi
RTL	Re-education through labor, also known as reform through labor
SOE	State-owned enterprise
STMA	State Tobacco Monopoly Administration
TBML	Trade-based money laundering
TCM	Traditional Chinese medicine
TCO	Transnational criminal organization
TEU	Twenty-foot equivalent
TIP	Trafficking in persons
TOC	Transnational organized crime
TraCCC	Terrorism, Transnational Crime, and Corruption Center (George Mason University)
TZTC	Tian Ze Tobacco Company
UN	United Nations
UNODC	United Nations Office on Drugs and Crime
U.S.	United States
U.S.-China Commission	U.S.-China Economic and Security Review Commission
USTR	U.S. Trade Representative
WPL	Wildlife Protection Law

Introduction

Often when people consider transnational crimes—drug trafficking, human trafficking, environmental crimes, money laundering, etc.—certain assumptions are made in terms of their dynamics. It is typically assumed that these crimes are committed by “traditional” criminals or non-state actors. There is also a general assumption that states, at their core, actively work to craft and enforce policies to effectively address these crimes, and, on the whole, work in-step with the international community to combat transnational crime. Many of these assumptions are based on democratic ideals – that states are founded on democratic principles and have the overall drive to positively impact the international order.

First, nothing precludes state actors from engaging in transnational crime. While it is, unfortunately, quite common for corrupt government actors and regimes to participate in criminal activity, it is uncommon for states, via state policy, to actively or passively facilitate and/or engage in criminal activity themselves.

Second, the overwhelming majority of states try to draft, enact, and implement legislation and regulations that combat transnational crime. Corruption and/or capacity challenges can certainly negatively impact the effectiveness of a government’s response, and there will always be illicit actors that actively try to evade enforcement. However, the vast majority of states do not have policies that explicitly permit criminal activity. Additionally, while it is quite understandable that, by and large, a state would put its own domestic interests above that of other states, most will work to remedy any internal factors that actively and/or passively facilitate transnational crime that occurs elsewhere.

The People’s Republic of China (PRC or China) plays an extremely impactful role as a source, transit and/or demand country in many of the most widespread and serious transnational crimes. The country is unique in that the government itself engages in certain types of criminal activity—specifically forced labor and intellectual property (IP) rights violations. In addition, the country’s political, economic, and social policies have extensive repercussions on the presence and prevalence of these crimes, both domestically and internationally. Furthermore, the country’s willingness to cooperate and act on these crimes within the global context has been relatively limited.

Two important factors to consider when evaluating China’s response to transnational crime are its dynamic, and somewhat forceful, pursuit of development and its authoritarianism. While China has claimed that they have no interest in becoming a global hegemon, there has been no ambiguity about China’s desire to become a geopolitical and economic powerhouse. The country has invested heavily in social and economic development, at home and abroad, and has crafted policies to aggressively support and protect important issues and sectors. At times it has sacrificed potential avenues for improving the efficacy of its fight against different transnational crimes in order to avoid any knock-on impacts that may negatively impact its interests.

China is an authoritarian state, and the Chinese Communist Party (CCP) has significant control over what happens in the country. While there will obviously be actors, such as criminals, criminal organizations, and the corrupt, that compete against Beijing’s interests, the government has a monopoly over a fair amount of what happens in the country and the agency to quickly, and severely, respond to undesired actors, activities, and flows, especially in comparison to democratic states.

An example of this level of extreme control is connected to China's war against opium. When the PRC was founded in 1949, the country was a leading producer of opium for the global market and the drug was consumed on a large scale domestically. However, as Zhang and Chin explain, after Mao took over, "eradication wiped out the largest ever cultivation of poppy in the world, opium dens were shut down, opium manufacturing facilities closed, drug traffickers summarily executed or imprisoned, and drug addicts sent to labor camps. The massive prohibition campaign... was so effective that in less than three years the communist government declared China a drug-free country."¹ They report that, as of 2016, opium cultivation had not returned to the country.²

This paper scrutinizes China's role in four different transnational crimes—drug trafficking, counterfeiting and IP theft, human trafficking and wildlife trafficking—as well as the illicit financial flows (IFFs) associated with these crimes. It explores the dynamics of these crimes as they relate to China both domestically and internationally; the political, economic, social, and cultural drivers and facilitators to these crimes; laws and regulations related to these crimes; and how the Chinese government has responded to these crimes and IFFs. Finally, the paper provides some focused recommendations for China to improve its response to transnational crimes and IFFs as well as for the U.S. to combat these crimes and flows.

1 Sheldon X. Zhang and Ko-lin Chin, "A People's War: China's Struggle to Contain Its Illicit Drug Problem" (Washington, D.C.: The Brookings Institution, 2016), 2. [Retrieved online.](#)

2 Zhang and Chin, 2.

Drug Trafficking

China serves as a major source, transit, and destination for narcotics trafficking, with the annual value of the domestic “drug industry” an estimated US\$82 billion.³ The country has grown into a principle supplier of fentanyl and its analogues as well as precursor chemicals for the production of a variety of drugs including methamphetamine. China’s large, developed chemical and pharmaceutical industries as well as boutique suppliers present major vulnerabilities for the country, which are compounded into weaknesses as there is anemic regulation and oversight. While some of these drugs and precursors remain in-country to satisfy a growing domestic demand, the U.S. Department of State points out that the country’s “numerous coastal cities with high-volume seaports and its vast network of major international airports make China an ideal destination and transit country for illicit drugs.”⁴

China has long been a center for narcotics production and trafficking. However, in recent years the country has also been facing an acceleration in the domestic consumption of illicit drugs. All major drugs have been reported in China, however methamphetamine, ketamine, and heroin are the most common. According to a 2020 report by China’s National Narcotics Control Commission (NNCC), there are 2.14 million drug users in China, however this may not be an accurate picture.⁵ For example, while there were 2.95 million *registered* drug users in China in 2014, a statement by the then NNCC Vice Chair put the actual number at more than 14 million drug users.⁶

Methamphetamine is the most widely consumed drug in China, followed by ketamine and heroin, though the Chinese government has also reported the emergence of new drugs including LSD soaked into blotting paper, synthetic cannabinoids, and pills containing methylphenidate (more commonly known as Ritalin) and DMT (dimethyltryptamine, a psychoactive/hallucinogenic drug).⁷

China as a Destination Country for Drug Trafficking

China borders part of the Golden Crescent of Afghanistan, Pakistan, and Iran, which is the primary source for poppy cultivation and opium/heroin production in the world, via Xinjiang province. However, it receives the majority of its heroin from the Golden Triangle, particularly Myanmar, which is likely due to the fact that Yunnan Province is significantly closer and better connected to China’s major population centers, which lie in the east.

Yunnan Province serves as a revolving door for drug trafficking flows. China views it as a critical entry point into the country for methamphetamine, heroin, ketamine and other narcotics, and the

3 It is important to note that the estimate is from 2015. Shannon Tiezzi, “China’s Growing Drug Problem,” *The Diplomat*, May 28, 2015. [Retrieved online.](#)

4 U.S. Department of State, *International Narcotics Control Strategy Report, Volume I: Drug and Chemical Controls, 2021* (Washington, D.C.: Bureau of International Narcotics and Law Enforcement Affairs, U.S. Department of State, 2021), 110. [Retrieved online.](#)

5 National Narcotics Control Commission, “Drug Situation in China (2019)” (Beijing: National Narcotics Control Commission, 2020), 3. [Retrieved online.](#)

6 See later in the chapter for a discussion of China’s drug user registration. “Drug Users Exceed 14m in China,” *China Daily*, May 11, 2015. [Retrieved online.](#)

7 National Narcotics Control Commission, “Drug Situation in China (2019),” 4.

government has stated that it believes Myanmar is the primary source of drugs seized in the country due to “chemical analyses of seized drugs”.⁸ However, the province also represents a crucial exit point for precursor chemicals entering the Golden Triangle from China. The United Nations Office on Drugs and Crime (UNODC) reports that the “vast majority” of recent precursor chemical seizures reported by Myanmar, which is overwhelmingly the largest source of methamphetamine production in East and Southeast Asia, is connected to transnational criminal organizations (TCOs) operating in the China border area.⁹

The NNCC also reported increasing flows of cannabis and cocaine entering the country, pointing to North America as the source of the cannabis and South America as the source of cocaine.¹⁰ They attribute the increased cannabis smuggling to the movement to decriminalize/legalize cannabis in Europe and the U.S. and its influence on “foreign employees, international students, overseas returnees, and entertainment professionals” who “[collude] through the Internet to purchase and abuse marijuana and related products from abroad by international parcel, or trafficking secretly through airlines.”¹¹ In regards to cocaine, the World Drug Report 2021 notes that Mexico is an important transit point, as Mexican authorities reported that “8 per cent of the cocaine in 2019 had been destined for China.”¹²

China as a Source Country for Drug Trafficking

China had formerly been the world’s largest producer of opium, connected in part to its losses in the Opium Wars in the 19th century; however, following the Chinese Communist Revolution and the founding of the People’s Republic of China in 1949, the government swiftly moved to implement a repressive albeit effective prohibition campaign targeting growers, manufacturers, purveyors, and users.¹³ Much of this was undone by the open-door policy China established in 1978, which ushered in a new era of interaction, particularly economic, with the rest of the world; narcotics found their way into the country with the increased flows of trade, capital, and people.

The principle drugs produced in China are amphetamine-type stimulants (ATS), new psychoactive substances (NPS) and other synthetic drugs, including fentanyl, as well as the precursor chemicals needed to manufacture these drugs. Unsurprisingly, the production of these drugs and precursor chemicals is strongly linked to the country’s developed and dynamic chemical and pharmaceutical industries, which are among the largest in the world by value.

For methamphetamine, ketamine, and similar lab-produced drugs, there is not a clear picture of how

8 Zhang and Chin, “A People’s War,” 4.

9 United Nations Office on Drugs and Crime, *Synthetic Drugs in East and Southeast Asia: Latest Developments and Challenges* (Vienna: United Nations Office on Drugs and Crime, 2020), 15. [Retrieved online.](#)

10 National Narcotics Control Commission, “Drug Situation in China (2019),” 1–2, 5.

11 National Narcotics Control Commission, 5.

12 United Nations Office on Drugs and Crime, *World Drug Report 2021; Drug Market Trends: Cocaine and Amphetamine-Type Stimulants* (Vienna: United Nations Office on Drugs and Crime, 2021), 27. [Retrieved online.](#)

13 The Permanent Mission of the PRC to the UN in Vienna highlights how, following “the founding of the People’s Republic of China (PRC) in 1949, the Chinese government led the Chinese people in a momentous struggle against drugs. In a short period of three years, China wiped out the scourge of opium, which had scourged China for a century, thus performing a miracle acknowledged by the whole world.” “Narcotics Control in China,” Permanent Mission of the People’s Republic of China to the United Nations and Other International Organizations in Vienna, June 2, 2004. [Retrieved online.](#)

much of China's internal demand is satisfied by external providers (i.e. outside of China, principally from the Golden Triangle) and how much is satisfied from internal production.

China's large, developed pharmaceutical and chemical industries present major vulnerabilities for the country, with a reported 5,000 pharmaceutical companies and more than 160,000 chemical companies that produce, among other things, active pharmaceutical ingredients and chemicals that can be used in the processing or manufacture of illegal narcotics including cocaine, methamphetamine, fentanyl, and more.¹⁴

Research by the RAND Corporation found that, while ephedrine and pseudoephedrine had previously been preferred methamphetamine precursors, there has been a decline in the seizures of both drugs which has been "mirrored by increases in seizures of P-2-P."¹⁵ This can be seen in UNODC reports, which notes that P2P "designer precursors", which frequently are imported from China, are relatively easy to obtain in Western Europe, and "may have favoured the expansion of clandestine methamphetamine manufacture in the subregion in recent years."¹⁶ Similarly, the Drug Enforcement Administration (DEA) states that more than 99 percent of the methamphetamine analyzed in the U.S. by the first half of 2019 was produced by Mexican TCOs "mainly out of non-controlled precursors of P-2-P, typically imported from China."¹⁷

According to the NNCC, in 2019 the "large-scale manufacturing of drugs shrank substantially" and "illegal diversion of drug precursors was rectified."¹⁸ The latter part of the statement, that the government has "rectified" precursor diversion, likely refers to the May 2019 decision to control all fentanyl-like substances. However, the NNCC also reports that production has shifted to scattered small-scale manufacturing, including in family workshops and minivans.¹⁹

One challenge for combating drug trafficking is the apparent ease with which drug trafficking organizations (DTOs) are able to identify and substitute other uncontrolled precursor chemicals needed to produce fentanyl (or other narcotics, for that matter), a nod to the sophistication of some of the criminal operations. The ability to swap precursors relatively quickly means that countries are typically reactive in controlling (i.e. strictly regulating and monitoring) precursor chemicals. With China's considerable chemical and pharmaceutical industries, Chinese DTOs have a priceless resource they can turn to in order to stay one step ahead of law enforcement and regulations. The UNODC states that "transnational [OCGs] in China continue to circumvent existing domestic and legal frameworks using non-scheduled precursor chemicals."²⁰

14 U.S. Department of State, *INCSR Vol. I, 2021*, 50; Sean O'Connor, "Meth Precursor Chemicals from China: Implications for the United States," Staff Research Report (Washington, DC: U.S.-China Economic and Security Review Commission, July 18, 2016), 8. [Retrieved online.](#)

15 "P-2-P" (also written as P2P) refers to the chemical phenyl-2-propanone, also known as phenylacetone. Bryce Pardo, Beau Kilmer, and Wenjing Huang, *Contemporary Asian Drug Policy: Insights and Opportunities for Change* (Santa Monica, CA: RAND Corporation, 2019), 24. [Retrieved online.](#)

16 United Nations Office on Drugs and Crime, *WDR 2021; Cocaine and ATS*, 49.

17 United Nations Office on Drugs and Crime, 54–55; Drug Enforcement Administration, *2020 National Drug Threat Assessment* (Washington, D.C.: Drug Enforcement Administration, 2021), 21. [Retrieved online.](#)

18 National Narcotics Control Commission, "Drug Situation in China (2019)," 1.

19 National Narcotics Control Commission, 6.

20 United Nations Office on Drugs and Crime, *Synthetic Drugs in East and Southeast Asia*, 39.

Boutique dealers often tweak the formulas of their drugs to stay ahead of bans, or disregard them entirely. The Shanghai-based Zheng DTO, which was run by Fujing Zheng and his father Guanghua Zheng, operated its own labs and sold its synthetic narcotics, including fentanyl, “on websites posted in 35 languages, from Arabic and English to Icelandic and Uzbek.”²¹ The Zhengs ran an agile, sophisticated operation for more than a decade: their labs manufactured more than 250 different drugs, which were shipped to at least 25 countries, and they would quickly modify the formulas of these drugs—creating an analogue—in order to get around China’s narcotics controls.²²

DTOs in China

Drug trafficking in China is largely controlled by Chinese organizations, which also operate internationally, though Mexican and Southeast Asian DTOs have also been reported in the country.²³ In regards to trafficking outside of China, Mexican DTOs have accessed precursor chemicals directly from manufacturers in China as well as working with foreign DTOs to secure the same goods. For example, in 2016 the *Small Wars Journal* reported that Chinese triads were “becoming the preeminent supplier of precursor chemicals to Mexican criminal enterprises;” similarly, in 2014 the *South China Morning Post* detailed how the 14K and Sun Yee On triads were supplying the Sinaloa cartel with methamphetamine precursors.²⁴

The attributes of Chinese DTOs can differ from group to group, with research as well as news reports providing varying pictures. While all are profit-motivated, determining factors that seem to influence group dynamics include the drug(s) involved, whether trafficking is domestic/regional or international, and whether the group solely traffics drugs or if they are also involved in the production and direct sale to consumers.

In a paper from The Brookings Institution, which principally looked at methamphetamine and heroin, Zhang and Chin reported that Chinese DTOs are “loosely affiliated individuals with little hierarchical structure” and consisting of “low-key entrepreneurs who are doing everything possible to avoid detection by and confrontation with the police or each other. Making money quietly is their motto.”²⁵ On the other hand, according to C4ADS, those Chinese companies and networks that illicitly produce, market, and/or traffic fentanyl can be described as: overt, by openly advertising online; adaptive, as they are quick to respond to drug scheduling, and; diversified, producing a wide variety of goods.²⁶

Tse Chi Lop, a Chinese-born Canadian, was the kingpin behind one of Asia’s largest drug trafficking organizations until he was arrested in January 2021. By aligning five of Asia’s triad groups—14K,

21 Del Quentin Wilber, “Fentanyl Smuggled from China Is Killing Thousands of Americans,” *Los Angeles Times*, October 19, 2018, sec. Politics. [Retrieved online.](#)

22 “Two Chinese Nationals Charged with Operating Global Opioid and Drug Manufacturing Conspiracy Resulting in Deaths,” U.S. Department of Justice, August 22, 2018. [Retrieved online.](#)

23 U.S. Department of State, *INCSR Vol. I*, 2021, 110.

24 Roger J. Chin, “Assessing New Frontiers: Methamphetamines and the Emerging China-Mexico Connection,” *Small Wars Journal* (blog), January 15, 2016. [Retrieved online.](#); “Hong Kong Triads Supply Meth Ingredients to Mexican Drug Cartels,” *South China Morning Post*, January 12, 2014. [Retrieved online.](#)

25 Zhang and Chin, “A People’s War,” 11.

26 Michael Lohmuller, Nicole Cook, and Logan Pauley, *Lethal Exchange: Synthetic Drug Networks in the Digital Era* (Washington, D.C.: C4ADS, 2020), 5. [Retrieved online.](#)

Wo Shing Wo, Sun Yee On, Big Circle Gang, and Bamboo Union—he was able to create a criminal syndicate dubbed “The Company” (also known as “Sam Gor”) that specialized in the trafficking of methamphetamine but also heroin and ketamine in the Asia Pacific. The syndicate “supplies a bigger, more dispersed drug market and collaborates with a more diverse range of local crime groups” than other OCGs and the results of this collaboration can be evidenced by an estimated US\$8 billion to US\$17.7 billion annual profit from its methamphetamine trade.²⁷

With the increased diversion of fentanyl and fentanyl precursors going from China to Mexico instead of directly to the U.S., the importance of Mexican DTOs in the fentanyl trade has grown as has their relationship with Chinese DTOs and chemical and pharmaceutical manufacturers. A paper from the National Defense University (NDU) points out that, around 2013, Mexican cartels began adding fentanyl to their heroin, potentially in response to reduced poppy cultivation leading to decreased heroin yield.²⁸ This produced a more potent product at a cheaper price, which garnered the appreciation of both users as well as traffickers. Drug producers and traffickers have maneuvered this substitution into an intentional addition, not just for heroin but also cocaine and prescription pills.

While all the above examples involve “traditional” DTOs, research by the Terrorism, Transnational Crime, and Corruption Center (TraCCC) on the online sale of fentanyl on open-web, Chinese-hosted platforms determined that “40 percent of websites advertising illicit fentanyl were tied to officially registered Chinese companies, contradicting frequently expressed statements that illegal fentanyl is produced primarily by rogue producers in China, and organized crime.”²⁹ Besides fentanyl, the European Monitoring Centre for Drugs and Drug Addiction (EMCDDA) and Europol reported that NPS was “sold openly by chemical and pharmaceutical companies” in China.³⁰

These findings are important because they contradict frequently expressed statements that illegal fentanyl and its precursors are produced primarily by rogue suppliers in China. As an authoritarian state, China, and the CCP, have tremendous control over its citizens’ access to the internet, routinely blocking, censoring, and taking down sites that do not meet its approval. China could easily do the same with companies advertising fentanyl and other dangerous and illegal drugs, however they have not done this to any serious degree. Their efforts to combat the online sale of drugs and precursors have by and large focused on pressuring online marketplaces and similar e-commerce platforms to better police the listings on their sites.

The direct involvement of “legitimate” companies is also a problem in the supply of precursor chemicals. The UNODC detailed that, despite the impacts of the COVID-19 pandemic on international supply chains, the “illicit supply chains of precursor chemicals for the manufacture of illicit drugs in the Golden Triangle are not expected to be disrupted for the foreseeable future, as sourcing of chemicals largely involves direct diversion from industry and trafficking, not diversion from licit trade channels.”³¹ This suggests that DTOs work directly with chemical and pharmaceutical companies to obtain precursors. However, it is unclear if these companies know they are supplying DTOs.

27 Ben Bauchau, “The Hunt for Asia’s El Chapo,” Reuters, October 14, 2019. [Retrieved online.](#)

28 Chloe Gilroy, “Great Power Competition and Counternarcotics in the Western Hemisphere,” Perry Center Occasional Paper (Washington, D.C.: National Defense University, September 2020), 14. [Retrieved online.](#)

29 Louise Shelley, “Fentanyl, COVID-19, and Public Health,” *World Medical & Health Policy* 12, no. 4 (2020): 392.

30 European Monitoring Centre for Drugs and Drug Addiction and Europol, *EU Drug Markets Report 2019* (Luxembourg: EMCDDA; Europol, 2019), 18. [Retrieved online.](#)

31 United Nations Office on Drugs and Crime, *Synthetic Drugs in East and Southeast Asia*, xiii.

Impacts of Chinese Narcotics and Precursor Chemicals Worldwide

The flows of narcotics and precursor chemicals out of China are destined for many countries around the world. Some are close by, such as drug-producing countries in the Golden Triangle like Myanmar, as noted above. Others are much further, such as fentanyl and its precursors that are trafficked to the U.S. and Mexico, as well as “finished” products such as NPS and methamphetamine that are trafficked to European and Australian markets.

A DEA estimate from circa 2015 had China supplying 80 percent of the precursor chemicals used by Mexican DTOs to produce methamphetamine, with Mexican-produced methamphetamine supplying 90 percent of the U.S. market.³² Criminal activity connecting China and Latin America is not a new phenomenon, but rather, as explained by R. Evan Ellis, a “natural artifact of the expansion of human and commercial contacts between Latin America and Asia” that has been evolving for decades, but for which “Latin America may be frighteningly unprepared.”³³ While activities such as human trafficking, migrant smuggling and extortion by Chinese TCOs may be largely confined to ethnic Chinese communities in Latin America, Chinese TCOs often collaborate with Latin American TCOs, in particular Mexican DTOs, on the supply of drugs as well as precursor chemicals; this is also true of the inverse supply of cocaine from Latin America to Asia.

The DEA’s *2020 National Drug Threat Assessment* reported that the supply of fentanyl coming into the U.S. directly from China has “decreased substantially,” while the supply from Mexican DTOs has increased. This has been linked in part to the significant rise in fentanyl being produced by Mexican DTOs that have been importing fentanyl precursors, primarily from China.³⁴

It is interesting to note that China disputes such claims, stating that assertions such as “Chinese fentanyl precursors flow into the United States via Mexico” are “highly irresponsible and utterly false” and the Chinese government has yet to find “any scheduled precursor chemicals trafficked to Mexico, or received any notification from the Mexican side about seizing scheduled chemicals originating from China.”³⁵

The decrease of fentanyl directly from China entering the U.S. could be attributed to China’s placement of the fentanyl and fentanyl-related drugs on its controlled narcotics list as well as increased enforcement/interdiction in China. However, it is also as possible that Mexican DTOs sought to carve out a larger share of the market, and its profits, by synthesizing their own fentanyl from Chinese-imported precursors, just as they previously took greater ownership of the manufacture and/or supply of cocaine and methamphetamine.

Regardless of whether the fentanyl is produced in China or in Mexico with Chinese precursors, the potency of the drug remains high, often with purity levels above 90 percent.³⁶ For fiscal year 2021, U.S. Customs and Border Protection seized 11,201 pounds of fentanyl (approx. 5,081 kilograms), an

32 O’Connor, “Meth Precursor Chemicals from China.”

33 R. Evan Ellis, “Chinese Organized Crime in Latin America,” *PRISM* 4, no. 1 (2014): 65.

34 Drug Enforcement Administration, *2020 National Drug Threat Assessment*, 14.

35 “Remarks by the Spokesperson of the Chinese Embassy in the United States on the Fentanyl Issue,” Embassy of the People’s Republic of China in the United States of America, September 2, 2021. [Retrieved online.](#)

36 Drug Enforcement Administration, *2018 National Drug Threat Assessment* (Washington, D.C.: Drug Enforcement Administration, 2019), 24. [Retrieved online.](#)

increase of nearly 134 percent from 2020;³⁷ this amount of fentanyl has the capability of killing every American nearly eight times over.³⁸

SPOTLIGHT ON...

COVID-19 AND FENTANYL

Wuhan is at the heart of two global crises: the production of fentanyl and its precursors as well as the source of COVID-19. When the pandemic hit, factories in Wuhan were shuttered in January 2020, which also meant that the production of fentanyl precursors halted. While monitoring Chinese websites selling fentanyl, TraCCC detailed that “online advertisements for illegal fentanyl in February 2020 reported that there was no supply or shipment available, although contact could be made with suppliers for the time when production and shipment would resume.”¹ According to the *Los Angeles Times*, the production of fentanyl as well as methamphetamine by Mexican DTOs also ground to a halt as they weren’t able to access the necessary precursor chemicals, precursors that are typically produced in Wuhan.² When lockdown ended in April 2021, producers, supply chains and DTOs rebounded.

1 Louise Shelley, “Fentanyl, COVID-19, and Public Health,” *World Medical & Health Policy* 12, no. 4 (2020): 394.

2 Kate Linthicum, “Coronavirus Chokes the Drug Trade - from Wuhan, through Mexico and onto U.S. Streets,” *Los Angeles Times*, April 24, 2020. [Retrieved online.](#)

During the time that China was directly supplying the majority of the U.S. market, a U.S. Senate investigation found that Chinese websites were “brazenly” marketing fentanyl openly, responding to inquiries and conducting business in a professional, efficient manner.³⁹ Although much of the fentanyl entering the U.S. now comes from/through Mexico compared to a few years ago, the fentanyl that still enters the U.S. directly from China primarily arrives in small amounts via international mail and parcel packages—a pseudo death by a thousand cuts; yet, with fentanyl, even one nick can be fatal.⁴⁰

To combat smuggling via mail, China and the U.S. have a bilateral agreement whereby the U.S. Postal Service receives advanced electronic data on U.S.-bound packages from China Post, China’s postal service, which has been viewed by the U.S. as helping in interdicting the flow of fentanyl.⁴¹ China reports that “the postal and parcel industry is mandated to take specific measures aimed at combating the trafficking of fentanyl substances and other scheduled chemicals, such as asking for real names

37 “Drug Seizure Statistics,” U.S. Customs and Border Protection, October 15, 2021. [Retrieved online.](#)

38 Based on a lethal dose of 2mg and a U.S. population of 332,475,723 (as of July 1, 2021) “Facts about Fentanyl,” Drug Enforcement Administration, accessed October 27, 2021. [Retrieved online.](#); “U.S. and World Population Clock,” U.S. Census Bureau, accessed October 27, 2021. [Retrieved online.](#)

39 U.S. Congress, Senate, Permanent Subcommittee on Investigations, *Combatting the Opioid Crisis: Exploiting Vulnerabilities in International Mail*, p. 28-29, 34.

40 U.S. Congress, Senate, Permanent Subcommittee on Investigations, *Combatting the Opioid Crisis: Exploiting Vulnerabilities in International Mail*, 115th Cong., 2nd sess., 2018, 17. [Retrieved online.](#)

41 Liana W. Rosen and Susan V. Lawrence, “China Primer: Illicit Fentanyl and China’s Role,” In Focus (Washington, D.C.: Congressional Research Service, January 29, 2021), 2. [Retrieved online.](#)

of senders and receivers, checking the parcel contents, using security screening equipment for security checks, and strengthening inspection on cross-border parcels to certain destinations such as the United States.”⁴²

In addition to parcel mail, an investigation by the Wilson Center and *InSight Crime* reported that Chinese TCOs often ship drugs and contraband through shipping containers that are intentionally mislabeled, however even without the mislabeling it can be “difficult to track the origin of precursor chemicals or clandestinely-produced fentanyl because of the intricate network of freight forwarding companies commonly employed by criminal groups to conceal the origin of the product.”⁴³

China also serves as an important source country for precursor chemicals as well as NPS trafficked into Europe. Though synthetic opioids have not presented as serious a problem for Europe as they have for the U.S., the EMCDDA and Europol reported that the majority of synthetic opioids available in Europe come from China, or are produced in Europe from precursors originating in China. Those synthetics from China can either be ready for sale, or may be cut (i.e., diluted with another substance(s) to increase yield) and then packaged for sale.⁴⁴

Like many countries in the world, China’s fight against international drug trafficking is hampered by the massive scale of global trade. Four of the five busiest container ports in the world are located in China, with a total of 119.1 million TEU, or the equivalent of 119.1 million 20-foot shipping containers, moving through the ports each year.⁴⁵ A senior official in Guangdong Province, which hosts China’s fourth largest and the world’s fifth largest container port in Guangzhou, reported that they “have neither the manpower nor the equipment to inspect the millions of containers” that move through the province.⁴⁶

Chinese Policy Response to Drug Trafficking

There are two areas at play when it comes to the Chinese government’s policy response to the trafficking of drugs and their precursors. The first area involves the criminalization of the manufacture, smuggling, trafficking, and transportation of narcotic drugs.⁴⁷ The second area involves the regulation of the pharmaceutical and chemical sectors, which are responsible for the manufacture of legal pharmaceutical/chemical substances that can serve as narcotic drugs or are used as precursor chemicals in the production of narcotic drugs.

The Criminal Law of the People’s Republic of China (“Criminal Law”) criminalizes the smuggling, trafficking, transportation, and manufacture of narcotic drugs as well the transportation and sale of

42 “Remarks by the Spokesperson.”

43 Steven Dudley et al., *Mexico’s Role in the Deadly Rise of Fentanyl* (Washington, D.C.: Wilson Center; InSight Crime, 2019), 9. [Retrieved online.](#)

44 European Monitoring Centre for Drugs and Drug Addiction and Europol, *EU Drug Markets Report 2019*, 115.

45 TEU stands for “twenty-foot equivalent” and is a standardized unit of measurement used to describe cargo volumes for containers, with one TEU representing one 20 foot x 8 foot x 8 foot intermodal shipping container. See “What Are the Five Top Ports in China?,” Port Technology, February 20, 2020. [Available online.](#)

46 Zhang and Chin, “A People’s War,” 12.

47 Article 357 notes that the term “narcotic drugs” means “opium, heroin, methylaniline(ice), morphine, marijuana, cocaine and other narcotic and psychotropic substances that can make people addicted to their use and are controlled under State regulations.” “Criminal Law of the People’s Republic of China” (1979). [Retrieved online.](#)

precursor chemicals. In addition, the Anti-Drug Law of the People's Republic of China (ADL) seeks to “[prevent] and [punish] criminal offences related to narcotic drugs, protecting the health of citizens both in body and in mind and maintaining social order.”⁴⁸ The primary organization responsible for implementing China's anti-drug laws is the NNCC, which was established in 1990 under the Ministry of Public Security and is comprised of more than 25 different agencies.

As many of the drug trafficking challenges in China involve the production and export of precursor chemicals, it is this second area, regarding the regulation of the pharmaceutical and chemical sectors, where there has been the greatest scrutiny. An important law in regards to pharmaceutical manufacturing is the Drug Administration Law of the People's Republic of China (DAL), which was originally adopted in 1984 and most recently revised in 2019. The DAL applies to “activities involving drug development, manufacturing, distribution, and use, and drug regulation” in China.⁴⁹ Regulatory responsibilities are divided between the drug regulatory departments of the central government and provincial governments. In addition, there are multiple national government agencies that are involved “in promulgating and enforcing production and export requirements for pharmaceuticals or chemicals.”⁵⁰

Among other activities, the DAL outlines the processes by which companies can manufacture and distribute drug products. For the former, a company must obtain a Drug Manufacturing Certificate (DMC), which is issued by each provincial drug regulatory department. Similarly, those companies engaged in the wholesale or retail sale of drugs must obtain a Drug Distribution Certificate (DDC) from the same provincial drug authorities. The RAND Corporation reports that the Chinese government has made efforts over the last decade “to adopt better enforcement and production guidelines, including good manufacturing practices (GMP). The GMP standards cover the most-basic aspects of manufacturing, including sanitary working conditions, product testing and tracking, and record-keeping.”⁵¹

In addition, China adopted “Good Supply Practice for Pharmaceutical Products” (GSP) in 2000, which was amended in 2016, which aims to “[strengthen] the quality management of drug distribution, [regulate] drug distribution, and [ensure] the safety and effectiveness of drugs for human beings.” The GSP requires enterprises to “[examine] the legality of the... purchasers,” however it is unclear to what lengths the company must go to ascertain and verify the authenticity of the buyer so as to ensure that the pharmaceuticals are destined for legitimate use rather narcotics production or illicit trade.⁵²

The penalty for manufacturing and/or distributing drugs without a DMC or DDC includes the closure of the operation, the seizure of the produced/sold drugs and related proceeds, and a fine of ten to twenty times the value of the drugs. However, if “the circumstances are serious, an order shall be given to suspend production or business operations for rectification, until revocation of drug approval documents, Drug Manufacturing Certificate, Drug Distribution Certificate, and Pharmaceutical

48 “Anti-Drug Law of the People's Republic of China” (2007). [Retrieved online.](#)

49 “Drug Administration Law of the People's Republic of China” (1984). [Retrieved online.](#)

50 Pardo, Kilmer, and Huang, *Contemporary Asian Drug Policy*, 60.

51 Pardo, Kilmer, and Huang, 59–60.

52 “Good Supply Practice for Pharmaceutical Products (2016 Amendment),” Law Info China, July 13, 2016. [Retrieved online.](#)

Preparation Certificate for Medical Institution.”⁵³

Because China’s chemical and pharmaceutical sectors grew rapidly, in large part due to privatization, the growth “has outpaced the capacity and design of China’s regulatory regime,” resulting in “regulatory gaps and bureaucratic fragmentation [which] continue to hamper China’s ability to oversee [these industries].”⁵⁴ A clear example of this was a now-closed loophole whereby the Chinese State Food and Drug Administration (now the National Medical Products Association or NMPA), which does regulate pharmaceutical companies, did not have jurisdiction over chemical companies that manufacture pharmaceutical components, leaving them in a jurisdictional void without oversight.⁵⁵

This loophole was technically closed in 2014 when the State Administration of Work Safety published the Guidelines for Standardization of Enterprises’ Management of Non-Pharmaceutical Precursor Chemicals (Notice 70 of 2014), which required chemical companies producing non-pharmaceutical precursor chemicals to create stronger safeguards including implementing “a liability system, record-keeping, precursor chemical management, purchasing, production and storage, sales, training and annual reporting to work safety administrations.”⁵⁶

However, it appears that at least three weaknesses exist in these guidelines. First, companies are encouraged via “incentive schemes” to “[internally prosecute] behavior in violation of regulations;” and second, companies are to report “severe cases” to “local authorities of public security and work safety.”⁵⁷ It is unclear why the government would encourage a company to handle illicit behavior internally rather than report such instances to government authorities, as such guidance would seem likely to reinforce a culture of non-reporting and create a serious lack of transparency.

Additionally, if cases are “severe” enough to be reported externally, due to previously noted issues of local corruption and bureaucracy hampering government oversight, it seems that a national-level authority would be the best agency to receive such reports. Finally, unless clarified in the Guidelines, it is unclear what would constitute a “severe” case, leaving a large gray area in which companies could choose to not report instances of serious wrongdoing.

Weak oversight of the chemical manufacturing sector has also led to challenges including an increase in “unlicensed or ‘semi-legitimate’ chemical manufacturers or distributors,” the use of “shell facilities,” as well as the production and sale of chemicals beyond manufacturers’ legal limits.⁵⁸ This has been reported by the NNCC, which noted that criminals in China are able to take advantage of the weakly regulated chemical sector, registering “ready-made” or “fly-by-night” chemical companies in order to receive the operating license certificates necessary to obtain and then traffic drug precursors.

53 Drug Administration Law of the People’s Republic of China.

54 Bryce Pardo, “Evolution of the U.S. Overdose Crisis: Understanding China’s Role in the Production and Supply of Synthetic Opioids: Testimony before the Subcommittee on Africa, Global Health, Global Human Rights, and International Organizations,” § Committee on Foreign Affairs (2018). [Retrieved online.](#)

55 Walt Bogdanich, “Chinese Chemicals Flow Unchecked onto World Drug Market,” *The New York Times*, October 31, 2007, sec. World. [Retrieved online.](#)

56 Jane Zhou, “SAWS Issued Guidelines to Standardize Enterprises’ Management of Non-Pharmaceutical Precursor Chemicals,” ChemLinked, June 25, 2014. [Retrieved online.](#)

57 Zhou.

58 Pardo, Kilmer, and Huang, *Contemporary Asian Drug Policy*, 60.

sors.⁵⁹ Media reports also note that Chinese vendors “are often camouflaged by a complex network of corporate entities registered in far-flung cities along China’s interior, where they use sophisticated shipping methods to bypass screening measures and where law enforcement scrutiny is often laxer than in bigger cities such as Beijing or Shanghai.”⁶⁰

The decentralized administration of pharmaceutical and chemical regulations means that the “local” drug regulatory departments are given considerable power in the licensing and supervision of drug manufacturers and distributors. Article 113 of the DAL requires the local drug regulatory departments to forward any information about “illegal behaviors related to drugs which allegedly constitutes a criminal offense” to public security authorities,⁶¹ which presents a serious vulnerability in oversight as the RAND Corporation notes that “many local authorities are economically and politically affiliated with producers—and therefore reluctant to crack down” on illicit activities.⁶²

Another challenge involves a lack of capacity in staffing. Provincial regulatory departments are responsible for inspecting drug manufacturers, and per the Regulations to Implement the DAL, inspectors must meet certain qualifications and are to be chosen at random for inspections.⁶³ However, as the U.S.-China Economic and Security Review Commission (“U.S.-China Commission”) points out, due to a severe shortage of inspectors, many illicit precursor chemical operations are able to evade detection; they can further improve their odds by choosing to operate in remote areas since “Chinese law enforcement personnel are mainly concentrated in urban centers.”⁶⁴

There is very low political and social tolerance of drug use and trafficking in China, which to a great extent is connected to the country’s history with opium; this has translated into draconian measures to monitor, combat, and punish those involved. However, the brunt of the government’s response is directed to the consumption and trafficking that directly affect China; external impacts related to internal dynamics (such as the production of narcotics and precursors) are not always treated with the same level of gravity.

A brief released in 2004 by the Permanent Mission of the PRC to the UN in Vienna shows that China’s narrative on drug trafficking portrays itself as more of a victim of outside influences, stating that “since the late 1970s, the illicit international narcotics tide has constantly invaded China,” turning China “from a victim of the transit drug trade into a victim of both drug transit and consumption.”⁶⁵ This statement gives the impression that China views the country’s own internal consumption as a result of external influences (i.e. drug transit) rather than internal demand.

The disparity in treatment of internal versus external drug crimes can best be seen with the issue of controlling precursor chemicals and drugs. Although China has made statements asserting that

59 National Narcotics Control Commission, “Drug Situation in China (2019),” 6.

60 Emily Feng, “‘We Are Shipping to the U.S.’: Inside China’s Online Synthetic Drug Networks,” NPR, November 17, 2020. [Retrieved online.](#)

61 Drug Administration Law of the People’s Republic of China.

62 Bryce Pardo and Beau Kilmer, “China’s Ban on Fentanyl Drugs Won’t Likely Stem America’s Opioid Crisis,” *The RAND Blog* (blog), May 22, 2019. [Retrieved online.](#)

63 See Article 7 of “Regulations for the Implementation of the Drug Administration Law of the People’s Republic of China,” Pub. L. No. Decree No.360 (2002). [Retrieved online.](#)

64 O’Connor, “Meth Precursor Chemicals from China,” 9.

65 “Narcotics Control in China.”

the government “takes seriously its responsibility to the international community” in regards to controlling precursors, their commitment is questionable in light of the fact that the regulation and oversight of the chemical and pharmaceutical sectors remains weak.⁶⁶

The NDU paper notes that “the Chinese government’s response to the export of massive quantities of illegal drugs and precursor chemicals is largely driven by external pressure and characterized by a lack of credible commitment to reduce the flow of illegal drugs and precursor chemicals.”⁶⁷ For example, the U.S. scheduled N-Phenethyl-4-piperidinone (NPP) and anilino-Nphenethylpiperidine (ANPP), both popular precursors for fentanyl and some fentanyl analogs, in 2007 and 2008; however, China did not do so until in 2017 after significant diplomatic pressure from the U.S., which meant that, previously, manufacturers in China “faced no reporting or export restrictions.”⁶⁸

The production and trafficking of fentanyl and its precursors have been sources of contention in U.S.-China relations over the last several years, as China has been the primary supplier, directly and indirectly, of fentanyl entering the U.S. The U.S. has exerted both diplomatic and economic pressure, such as via trade negotiations during the Trump administration, to compel China to crack down on fentanyl.

Over the period 2017 to 2018, China placed six fentanyl analogues and two precursor chemicals on its list of controlled substances. In a significant step, in May 2019, the Chinese government placed all fentanyl-like substances (current or future) on its list of controlled narcotics which, it is hoped, will improve safeguards against the production and import/export of the drug. Additionally, in 2021, China “class scheduled synthetic cannabinoids, 18 other new psychoactive substances, such as fluoro-ketamine... [and] Six chemicals, including Methyl alpha-phenylacetate (MAPA), will be listed as precursor chemicals.”⁶⁹

Statements from the Chinese Embassy in the U.S. give the impression that China sees fentanyl as primarily a U.S. issue or responsibility, and that China’s class-wide scheduling of fentanyl substances was a gesture of goodwill to the U.S., as the Chinese government took action despite there being “no large-scale abuse or prominent hazards of [fentanyl substances] in China.”⁷⁰ China suggests that the U.S. fentanyl problem is related to the fact that the U.S. is “the biggest producer and user of fentanyl drugs in the world... but it has not officially scheduled fentanyl substances permanently yet.”⁷¹

While it is correct that U.S. has not permanently scheduled all fentanyl analogues, it has done so via a temporary order that has been continuously renewed since 2018.⁷² In addition, while the U.S. is a major producer of fentanyl, China remains the primary source country of illicit fentanyl and fentanyl substances that are trafficked into the U.S.⁷³ Despite its efforts to class schedule fentanyl, due

66 “Narcotics Control in China.”

67 Gilroy, “Great Power Competition and Counternarcotics,” 3.

68 Pardo, Kilmer, and Huang, *Contemporary Asian Drug Policy*, 62.

69 “Remarks by the Spokesperson.”

70 “Remarks by the Spokesperson.”

71 “Remarks by the Spokesperson.”

72 Alyssa Hundrup, Triana McNeil, and Kimberly M. Gianopoulos, *Synthetic Opioids: Considerations for the Class-Wide Scheduling of Fentanyl-Related Substances* (Washington, D.C.: U.S. Government Accountability Office, 2021). [Retrieved online.](#)

73 Lauren Greenwood and Kevin Fashola, “Illicit Fentanyl from China: An Evolving Global Operation,” Issue Brief (Washington, D.C.: U.S.-China Economic and Security Review Commission, August 24, 2021), 1. [Retrieved online.](#)

to weak regulation and enforcement, “unilateral efforts by China to confront distribution of illicitly manufactured fentanyl will continue to fail until the regime overhauls its regulatory infrastructure. Until that time, shrewd chemists will almost certainly continue to exploit China’s clumsy anti-drug bureaucracy to export fentanyl and fentanyl analogues abroad through illicit channels.”⁷⁴

Chinese Enforcement Response to Drug Trafficking

While the Chinese government did respond to international pressure to better control fentanyl and its analogues, the size of the chemical and pharmaceutical industries coupled with gaps in regulation will make enforcement difficult. As much of the trade is conducted online, it is harder to identify and disrupt the real-world actors behind these digital sales. Additionally, as Felbab-Brown explains, the question is now “whether and how effectively China will enforce this new regulation both with regard to finished fentanyl and the large quantities of fentanyl precursors transshipped to Mexico.”⁷⁵

In regards to punishing those involved in drug trafficking and consumption, China can be extremely tough. Punishments for trafficking can range from a few months in prison up to life imprisonment and death.⁷⁶ *The Economist* notes that “many traffickers are among the thousands of people executed annually.”⁷⁷ For drug users, China had long had a policy of “re-education through labor” (RTL), which existed until the ADL was amended in 2008. However, RTL was simply substituted with “compulsory isolated rehabilitation”, which, as Yang et al. point out, is “still delivered by judicial staff, in the same settings as former RTL camps, with an average stay of 2 years” and involves forced labor.⁷⁸

While much of China’s response to drug abuse, production, and trafficking could be considered draconian, the punishment for mislabeling shipments of precursor chemicals, the most common diversion tactic, is significantly lighter and typically involves civil penalties and small fines.⁷⁹ It is interesting to note the disparity in punishment between those crimes that directly affect the state internally and those that have external impact (i.e. on other countries).

While China clearly prosecutes individuals for drug trafficking, it is unclear if the government has ever prosecuted any company or other entity for the same crime. This would be applicable in regards to chemical or pharmaceutical companies for knowingly producing and/or supplying narcotics or precursors. Articles 30 and 31 of China’s Criminal Law do extend criminal liability entities (referred to as “units”), specifically that “any company, enterprise, institution, State organ, or organization” that commits a crime “shall bear criminal responsibility,” with the unit to be fined and “the persons who are directly in charge and the other persons who are directly responsible for the crime shall be given criminal punishment.” Additionally, Article 43 of the DAL state that the manufacturer’s legal representative as well as its “principal responsible person” are “fully responsible for the drug man-

74 Razi Lane, “Focused Accountability: A Bilateral Response to the International Proliferation of Fentanyl Analogues,” *Notre Dame Journal of International & Comparative Law* 11, no. 1 (2021): 169.

75 Vanda Felbab-Brown, *Fentanyl and Geopolitics: Controlling Opioid Supply from China, The Opioid Crisis in America: Domestic and International Dimensions* (Washington, D.C.: Brookings Institution, 2020), 3. [Retrieved online.](#)

76 Bill Chappell, “China Jails 9 In Fentanyl Trafficking Case That Began With A Tip From The U.S.,” NPR, November 7, 2019. [Retrieved online.](#)

77 “China’s Strong-Arm Approach to Drug Addiction Does Not Work,” *The Economist*, March 23, 2019. [Retrieved online.](#)

78 Mei Yang et al., “Drug Policy in China: Progress and Challenges,” *The Lancet* 383, no. 9916 (February 2014): 509. [Retrieved online.](#)

79 Zhang and Chin, “A People’s War,” 2,4,6-7; U.S. Department of State, *INCSR Vol. I, 2021*, 50.

ufacturing activities.”⁸⁰

Furthermore, Article 350 of the Criminal Law criminalizes the illegal transportation of precursor chemicals (“any other raw material or elixir used in the manufacture of narcotic drugs”), and treats anyone who provides another person with such substances “while clearly knowing that the person manufactures narcotic drugs” as a joint offender.⁸¹ This would suggest that any chemical or pharmaceutical company that knowingly supplies precursor chemicals could be prosecuted under the Criminal Law as well as the DAL or other relevant laws, which would serve as a very important deterrent, as the Criminal Law has much stronger penalties compared to the DAL, which is more administrative.

Keeping in line with the country’s surveillance-state policies, the country has maintained an aggressive system of identifying, registering, and “rehabilitating” drug users. The Brookings Institution reports that Chinese police will “comb through neighborhoods” throughout the country, conducting door-to-door interviews to “find out who the drug users are” in order to populate this registry.⁸² As noted above, the treatment of/penalties for drug use include compulsory testing of suspected drug users, registration of drug users, and compulsory treatment for drug addicts, including “in-community” treatment (for up to three years) or “isolation for drug rehabilitation” (for up to two years) and may involve forced labor.⁸³

Proactive measures to combat drug abuse and trafficking include a series of campaigns in 2019 under the slogan “Combating Drug Manufacture and Trafficking, and Controlling Drug Precursors and Drug Use,” which included targeting of synthetic drug manufacturing, online drug-related activities, and the flow of drugs into the country.⁸⁴ In 2020, the NNCC reported that, over the past five years, successes in China’s “war on drugs” included “638,000 drug crimes cracked, 32,000 drug trafficking gangs eliminated, 780,000 suspects arrested, and more than 400 tons of drugs of various kinds seized” as well as the identification of more than 4.2 million drug users, of which nearly 1.6 million were sent to compulsory rehabilitation.⁸⁵

International Cooperation

While China’s regulatory cooperation has been strained, overall it has had improved law enforcement collaboration, such as the 2019 conviction of nine fentanyl traffickers in China from an investigation that began with a tip from the U.S. Department of Homeland Security.⁸⁶ However, because of the somewhat aggressive economic, political, and military policies that China has used to maintain/extend its spheres of influence, some countries may have concerns when collaborating with China. Zhang and Chin note that despite China’s “eagerness to seek cooperation from neighboring countries to help reduce the influx of illicit drugs, China’s growing economic and political power in the

80 Drug Administration Law of the People’s Republic of China.

81 Criminal Law of the People’s Republic of China, 1979.

82 Zhang and Chin, “A People’s War,” 4.

83 Anti-Drug Law of the People’s Republic of China.

84 National Narcotics Control Commission, “Drug Situation in China (2019),” 1.

85 “Xi Jinping Urges ‘consistent, Resolute’ Effort to Win War on Drugs,” CGTN, June 23, 2020. [Retrieved online.](#)

86 Chappell, “China Jails 9 In Fentanyl Trafficking Case.”

region also make these neighbors nervous.”⁸⁷

It is interesting to note that, while the country has been challenged in controlling the production and trafficking of certain narcotics (e.g. ATS, synthetics, etc.) and precursors, it has essentially been able to successfully maintain its grip on eradicating opium/poppy cultivation.⁸⁸ Some of this can be attributed to the fact that poppy cultivation (or the cultivation of any illicit crop such as coca or cannabis) has a much larger and more fixed footprint than the production of a narcotic or precursor in a lab, and it is therefore easier to detect. However, a question remains about the role of political will, as the cultivation and production of opium/heroin had a direct impact on Chinese citizens and therefore the country itself, whereas the production of synthetic drugs and precursors primarily impacts other countries.

China’s failures in regulation and supervision hurt itself just as much as the rest of the world, as the same chemicals and pharmaceuticals that are manufactured in this void end up being used to produce drugs, such as methamphetamine and ketamine, that end up being trafficked back into China. China’s Achilles heel will remain its pharmaceutical and chemical industries until the country greatly improves regulation and oversight. As pointed out in the NDU paper, it remains to be seen how, and if, China will balance its hegemonic ambitions—for example its “Made in China 2025” policy which includes making “revenue growth within its biopharmaceutical sector a top development priority”—with the need to increase the regulation and oversight of its pharmaceutical and chemical sectors in order to effectively combat drug trafficking.⁸⁹

87 Zhang and Chin, “A People’s War,” 12.

88 Zhang and Chin, 2.

89 Gilroy, “Great Power Competition and Counternarcotics,” 16.

Human Trafficking

Like every country, China suffers from human trafficking. What makes China's situation unique is a combination of social and cultural drivers, weak legislation, and most importantly, the government's active use of forced labor. Human trafficking deeply affects China, with both Chinese citizens and foreign nationals victimized in the country, and Chinese and foreign nationals victimized in other countries.

The internationally recognized definition of human trafficking is the “recruitment, transport, transfer, harboring or receipt of a person by such means as a threat or use of force or other forms of coercion, abduction, fraud, or deception for the purpose of exploitation.”⁹⁰ Trafficking itself consists of three elements: the *act* of trafficking, which involves recruitment, transport, transfer, harboring or receipt of a person; the *means* of trafficking, which refers to the threat and/or use of force, coercion, fraud or deception, among other methods; and, the *purpose* of the trafficking, which is always exploitation.⁹¹

The International Labor Office (ILO), in their report *Profits and Poverty: The Economics of Forced Labor*, divides human trafficking into three main categories: sexual exploitation, such as forced prostitution; labor exploitation, which can include forced begging and domestic work in addition to work within sectors such as the agriculture, construction, and manufacturing; and, state-imposed forced labor, which can involve forced labor at prisons and detention centers.⁹² While organ trafficking is a subset of human trafficking, this chapter will not focus on this particular form of human trafficking.⁹³

Human trafficking is interconnected with human smuggling, but the two are distinct activities. Human trafficking is always an involuntary act, whereas human smuggling, which Polaris defines as “the business of transporting people illegally across an international border,” is a largely voluntary act that the individual being transported chooses to do.⁹⁴ Another important distinction is that the act of human smuggling always involves crossing from one jurisdiction to another, while human trafficking does not require “movement” per se, with an individual capable of being victimized outside their country of citizenship, domestically, or even in their own neighborhood.

The Scale of Human Trafficking and Victimization Rates

The ILO estimates that the total global profits generated from human trafficking—which includes forced sexual exploitation, domestic work, and non-domestic labor—amount to US\$150.2 billion annually.⁹⁵ The general “value” of a trafficked person is the fact that traffickers—whether “traditional” criminals, formal enterprises, or any other actor—can get any type of labor for little to no cost. At a regional level, annual profits from human trafficking are highest in the Asia-Pacific (US\$51.8 bil-

90 “Human Trafficking,” United Nations Office on Drugs and Crime, accessed February 16, 2022. [Retrieved online.](#)

91 “The Crime: Defining Human Trafficking,” United Nations Office on Drugs and Crime, accessed February 16, 2022. [Retrieved online.](#)

92 International Labor Organization, *Profits and Poverty: The Economics of Forced Labour* (Geneva: International Labor Organization, 2014), 7. [Retrieved online.](#)

93 The topic of organ trafficking was not covered due to page limits.

94 “Trafficking vs. Smuggling: Understanding the Difference,” Polaris, May 25, 2021. [Retrieved online.](#)

95 International Labor Organization, *Profits and Poverty*, 13.

lion), whereas the annual profit per victim in that region was second lowest (US\$5,000) among all regions, meaning that there must be a considerable number of victims in the region in order to generate such high profits, though it is also the region with the largest population.⁹⁶ Profits generated by forced sexual exploitation account for two-thirds of the total global value, estimated at US\$99 billion per year, with forced labor exploitation estimated at US\$51.2 billion annually.⁹⁷

Although no solid estimates for the value of human trafficking within China were identified, there have been estimates made in terms of the number of victims within China. The Global Slavery Index (GSI) estimated that, as of 2016, there were more than 3.8 million victims of modern slavery in China.⁹⁸ Pairing the ILO's average annual profit of US\$5,000 per victim in the Asia-Pacific region with the GSI's estimated 3.8 million trafficking victims in China gives a rough estimate for the value of human trafficking in China at US\$19 billion.

China has high levels of domestic human trafficking with the presence of both forced labor and forced sexual exploitation. Sexual exploitation most commonly involves forced prostitution, forced marriage, and online sex exploitation. Forced labor by state and non-state actors most frequently is used in the manufacturing, construction, fishing, and agricultural sectors.

Chinese as well as foreign nationals are victimized, however it is very likely that there are more Chinese than foreign victims due to widespread state-sponsored forced labor. The 2021 *Trafficking in Persons Report (TIP Report)* published by the U.S. Department of State includes 24 country summaries whereby the country has reported their citizens as being victimized in China; most are women and children.⁹⁹ For victims (many of them women) of other countries that ended up within Chinese borders, they were forced into sex work or domestic servitude, while foreign men were often exploited in China's fishing industry.

Forced Labor

A unique influence on domestic human trafficking is China's national household registration system, known as *hukou*. The system was implemented in the late 1950s as a way to register the population; its current functions are "the control of internal migration, the management of social protection, and the preservation of social stability."¹⁰⁰ However, by linking the provision of social services to an individual's official residence, the *hukou* system can increase the risk of victimization for internal migrants working/living outside their official residence.

The GSI reports that the main driver of migration from China's rural areas is poverty, and that the inability to find work locally causes these individuals to "become part of China's 'floating population'

96 International Labor Organization, 14.

97 International Labor Organization, 13.

98 According to Walk Free, which publishes the Global Slavery Index, modern slavery "covers a set of specific legal concepts including forced labour, debt bondage, forced marriage, slavery and slavery-like practices, and human trafficking... Essentially, it refers to situations of exploitation that a person cannot refuse or leave because of threats, violence, coercion, deception, and/or abuse of power." "What Is Modern Slavery?," Walk Free, accessed June 6, 2022. [Retrieved online.](#); "Global Slavery Index 2018: China," Global Slavery Index, accessed February 22, 2022. [Retrieved online.](#)

99 U.S. Department of State, *Trafficking in Persons Report 2021* (Washington, D.C.: U.S. Department of State, 2021). [Retrieved online.](#)

100 Antoine Boquen, "China's Hukou System Explained," *New Horizons*, June 28, 2021. [Retrieved online.](#)

of migrant workers moving from rural to urban areas in search of work.”¹⁰¹ As these internal migrants are not living at their official residence, the Congressional-Executive Commission on China (CECC) explains that they therefore “have limited access to housing and government benefits due to the lack of official status in their new places of residence and thus are more likely to work in informal employment sectors... [which] increases the vulnerability of migrant workers to exploitative working practices.”¹⁰²

Forced labor in China is primarily connected to the “production of [labor-intensive, cheap goods for export],” explains GSI, “including in the manufacturing and construction sectors, as well as in more informal industries, such as brick kilns.”¹⁰³ This is supported by statements from those individuals who had been sentenced to forced labor as part of detention. Political activists as well as members of religious groups are subjected by the Chinese government “to forced labor as part of detention for the purpose of ideological indoctrination; survivors report having been forced to work in brick kilns, food processing centers, and factories manufacturing clothing and housewares.”¹⁰⁴

State-imposed forced labor, referred to as “reeducation through labor” (RTL) or “reform through labor” in China, is a commonplace legal punishment for “criminals, offenders who have committed minor offenses, drug addicts, sex workers, religious offenders, [and] critics of the government.”¹⁰⁵ Although the National People’s Congress did technically put an end to the RTL system in 2013, which included closing most RTL facilities, the U.S. Department of State explains that the government “reportedly converted some RTL facilities into state-sponsored drug rehabilitation facilities or administrative detention centers where, according to civil society and media reports, forced labor continues.”¹⁰⁶

In addition to state-imposed forced labor against Chinese citizens, North Korea has sent tens of thousands of its citizens to work in China in forced labor conditions in order to provide income for the Kim regime. The laborers serve as an important source of foreign currency for Pyongyang, which the regime has used to fund its nuclear and ballistic missile programs.

A 2017 report by the BSI Group estimated the number of North Korean workers in China at between 20,000 and 30,000, with most employed in the manufacturing sector.¹⁰⁷ BSI relates that North Korean laborers “are often viewed as more reliable than Chinese factory workers by Chinese manufacturers,” due to multiple “benefits” that are yielded from forced labor, including “restrictions on North Korean workers’ freedom of movement and the long hours they are required to work... the lack of sick leave or paid time off afforded to them... [as well as] cheaper wages, as workers are often paid much less than Chinese workers,” and the inability to “[freely] leave their employment.”¹⁰⁸

101 “Global Slavery Index 2018: China.”

102 Congressional-Executive Commission on China, *Congressional-Executive Commission on China Annual Report 2020* (Washington, D.C.: Congressional-Executive Commission on China, 2020), 179. [Retrieved online.](#)

103 “Global Slavery Index 2018: China.”

104 U.S. Department of State, *TIP Report 2021*, 179.

105 Titantian Zheng, “Human Trafficking in China,” *Journal of Historical Archaeology & Anthropological Sciences* Volume 3, no. Issue 2 (March 2018): 173. [Retrieved online.](#)

106 U.S. Department of State, *TIP Report 2021*, 178.

107 BSI, *North Korean Forced Labor in International Supply Chains* (Herndon, VA: BSI Supply Chain Services and Solutions, 2017), 6. [Retrieved online.](#)

108 BSI, 6.

By accepting North Korean laborers who are sent by the Kim regime, China was violating UN Security Council Resolution 2735 which prohibits Member States from providing work authorizations for North Korean nationals in their jurisdictions.¹⁰⁹ Although China officially stopped issuing or renewing work visas for North Koreans in 2017, due to “significant supply chain corruption in China and the number of unregistered or informal businesses utilizing North Korean labor,” the presence of North Korean forced labor in the country still persists.¹¹⁰

Oliver Cushing of Rights DD points out that North Korea “has exported people abroad” as forced labor for many years, and while these laborers do end up in many different countries, “it is in the Chinese border city Dandong that they are most heavily concentrated.”¹¹¹ A 2020 investigation by *The Guardian* found that “Chinese factories in Dandong are using forced labour from North Korea to produce PPE for export to countries including the UK and US,” and the laborers, who are mostly women, “work for up to 18 hours a day, with little or no time off.... are under constant surveillance and are unable to freely leave the factories... [and] have about 70% of their wages seized by the North Korean state.”¹¹²

SPOTLIGHT ON...

FORCED LABOR IN CHINESE INTERNMENT CAMPS

The Xinjiang Uyghur Autonomous Region (“Xinjiang”) is an autonomous region located in northwest China, which was annexed by the Qing dynasty in the mid-eighteenth century. The region’s population is largely Turkic-speaking Muslims, most notably ethnic Uyghurs but also Kazakhs, Tajiks, and Kyrgyz.

Between its annexation and the 1949 Chinese Revolution, separatists founded two independent republics—the Turk Islamic Republic of East Turkistan and the East Turkistan Republic—in the region. After the 1949 revolution, the government worked to reaffirm its sovereignty and control over the region, for example directing ethnic Han citizens to “colonize” the region to improve demographics as well as economic output.

However, according to Castets, the colonization’s “socio-economic repercussions, together with [Beijing’s] domineering attitude towards the regional political system, have generated a malaise that has lent new vigour in recent years to Uyghur nationalism and separatism.”¹

1 Rémi Castets, “The Uyghurs in Xinjiang – The Malaise Grows,” *China Perspectives* 2003, no. 5 (October 2003). [Retrieved online.](#)

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109 United Nations, “Security Council Resolution 2375,” S/RES/2375 § (2017), 5.

110 BSI, *North Korean Forced Labor in International Supply Chains*, 7.

111 Oliver Cushing, “North Korean Forced Labour in China. What to Look for in Your Supply Chain.,” RightsDD, December 8, 2020. [Retrieved online.](#)

112 Pete Pattison, Annie Kelly, and Ifang Bremer, “UK Sourced PPE from Factories Secretly Using North Korean Slave Labour,” *The Guardian*, November 20, 2020. [Retrieved online.](#)

China's repressive policies toward Xinjiang began to accelerate in the 1990s, with the period 1996-1997 becoming a "turning point" due to the introduction of "an exhaustive list of strict directives aimed at tightening control over Xinjiang and eradicating potentially subversive activities," that was accomplished, in part, through "strong-arm police operations" and "constant human rights violations."² This response triggered a rise in resistance groups and protest movements, often framed by the government as insurrectional, from which a small number of more radical groups, some of which being Islamist, emerged and engaged in guerrilla tactics and terrorist attacks.

The New York Times describes previous attacks by Uyghur militants as "relatively small, scattered and unsophisticated," and that the violence "has never threatened Communist control of the region."³ This is supported by a report from Vox, which points out that despite incidents of violence committed by Uyghur extremist groups, "most experts say Beijing's repression and subjugation of millions of Uighurs is vastly disproportionate to the comparatively minor terror threat in the region."⁴

The Chinese government has rounded up more than one million of Xinjiang's ethnic minorities and forcibly placed them in internment camps and prisons, which they have depicted as vocational and educational training centers that, among other purposes, fight Islamic extremism.⁵ Dedicated internment camps first appeared in Xinjiang around 2014, and they have been expanded ever since. Using satellite imagery, media reports, official documents, and eyewitness interviews, a September 2020 report published by the Australian Strategic Policy Institute identified more than 380 suspected detention facilities in Xinjiang, which includes the internment camps as well as detention centers and prisons.⁶

An important component of Beijing's efforts to control the region are its labor programs, found both inside and separate from internment camps, where the region's Muslim minorities are coerced, sometimes using harsh methods including uprooting villagers and restricting their movement, to attend labor training programs and then are assigned by the government as "volunteers" to different jobs, such as working in factories.⁷

2 Castets.

3 Austin Ramzy and Chris Buckley, "Absolutely No Mercy": Leaked Files Expose How China Organized Mass Detentions of Muslims," *The New York Times*, November 16, 2019. [Retrieved online.](#)

4 Jen Kirby, "Concentration Camps and Forced Labor: China's Repression of the Uighurs, Explained," Vox, July 28, 2020. [Retrieved online.](#)

5 Patrick deHahn, "More than 1 Million Muslims Are Detained in China—but How Did We Get That Number?," Quartz, July 4, 2019, 1. [Retrieved online.](#)

6 Nathan Ruser, *Documenting Xinjiang's Detention System* (Barton, Australia: Australian Strategic Policy Institute, 2020), 3. [Retrieved online.](#)

7 Chris Buckley and Austin Ramzy, "Inside China's Push to Turn Muslim Minorities Into an Army of Workers," *The New York Times*, December 30, 2019. [Retrieved online.](#)

FORCED LABOR IN CHINESE INTERNMENT CAMPS

The U.S. Department of State reports that authorities in Xinjiang “use threats of physical violence, forcible drug intake, physical and sexual abuse, and torture to force detainees to work in adjacent or off-site factories or worksites” that produce a wide variety of goods including garments, consumer electronics, pharmaceuticals, and face masks, all of which “are finding their way into businesses and homes around the world.”⁸

Castets explains that the events of September 11, 2001, afforded Beijing the opportunity to tie “the marginal existence” of Islamist groups with the “wholesale repression of the Uyghur opposition [as part of] the international dynamic of the struggle against Islamist terrorist networks.”⁹ Beijing rooted its response in Xinjiang, including the internment and forced labor programs, in its Counter-Terrorism Law, marrying together terrorism with the relatively vague “separatism” and “extremism.”

In addition to the Counter-Terrorism Law, the Standing Committee of the Xinjiang Uyghur Autonomous Region Congress amended its legislation—specifically Article 33 regulating against extremism—to “allow local governments to ‘educate and transform’ people influenced by extremism at ‘vocational training centres’... [which,] apart from teaching vocational skills... are required to provide education on spoken and written Chinese, and aspects of the law and other regulations.”¹⁰

8 “Forced Labor in China’s Xinjiang Region,” U.S. Department of State, July 1, 2021. [Retrieved online.](#)

9 Castets, “The Uyghurs in Xinjiang.”

10 Nectar Gan and Mimi Lau, “China Changes Law to Recognise ‘re-Education Camps’ in Xinjiang,” South China Morning Post, October 10, 2018. [Retrieved online.](#)

Sex Trafficking

Sex trafficking in China involves different kinds of commercial sexual exploitation, most notably forced prostitution and cybersex. According to the U.S. Department of State, sex trafficking in China is typically conducted by “well-organized criminal syndicates and local gangs... [who] typically recruit [Chinese women and girls] from rural areas and take them to urban centers, using a combination of fraudulent job offers and coercion by imposing large travel fees, confiscating passports, confining victims, or physically and financially threatening victims to compel their engagement in commercial sex.”¹¹³ In addition to the victimization of Chinese nationals, women and children from Africa, Latin America, and neighboring countries are forced, coerced, and/or deceived into sexual exploitation in China.¹¹⁴

North Koreans are particularly at risk of victimization in China due to the country’s close proximity, their economic vulnerability, the fact that they often enter China illegally, and the likelihood they

113 U.S. Department of State, *TIP Report 2021*, 178.

114 U.S. Department of State, 180.

will receive severe punishment if they are deported back to North Korea. According to the Committee for Human Rights in North Korea, the famine that “struck North Korea in the mid-1990s... touched off an exodus to China that has continued since then, albeit at a slower pace,” with migrants primarily coming from North Korea’s northeastern provinces and crossing over into adjacent provinces in China.¹¹⁵

The men, women, and children that flee from North Korea to China often enter the country illegally; some are trafficked into the country, while others are smuggled into the country and then subsequently trafficked. Human traffickers may play both roles, acting as smugglers in order to move women out of North Korea, only to sell them on to other traffickers once inside China. Traffickers are typically North Korean or Chinese, and it is not uncommon for victims to be sold more than once.

A report from *The New York Times* found that thousands of women flee North Korea each year with the help of human smugglers who promise them jobs, “but once [there], many of the women are sold to unmarried men in rural towns or to pimps for exploitation in brothels and cybersex dens.”¹¹⁶ This is supported by Kook, who writes that many North Korean women choose to go to China, “often promised better jobs or good lives as wives in China, but their situations rapidly deteriorate when they fail to find jobs or suffer from abuse by their new husbands, and some women are even kidnapped and forced to work in the highly exploitive sex industry.”¹¹⁷

Bride Trafficking

China’s now-rescinded “one-child policy” as well as sex-selective abortion tied to a cultural preference for male children has had significant knock-on effects: a sex ratio at birth of 0.94 females to every male, the world’s lowest;¹¹⁸ an estimated 34 million more men than women;¹¹⁹ and a phenomenon known as “surplus males”, when there are many more eligible men than women seeking marriage.¹²⁰ This gender imbalance has led to an increase in human trafficking, in particular what is known as “bride trafficking.”

Lhomme et al. date the emergence of bride trafficking from Southeast Asia to China to the 1980s, but report that its prevalence has gradually increased since 2000, in part due to the country’s economic growth, until it has “become one of the primary forms of cross-border human trafficking in the region.”¹²¹ Also contributing to the prevalence of bride trafficking in China are local drivers in

115 Committee for Human Rights in North Korea, *Lives for Sale: Personal Accounts of Women Fleeing North Korea to China* (Washington, D.C.: Committee for Human Rights in North Korea, 2009), 9. [Retrieved online.](#)

116 Choe Sang-Hun, “After Fleeing North Korea, Women Get Trapped as Cybersex Slaves in China,” *The New York Times*, September 13, 2019. [Retrieved online.](#)

117 Kyunghee Kook, “‘I Want to Be Trafficked so I Can Migrate!’: Cross-Border Movement of North Koreans into China through Brokerage and Smuggling Networks,” *The ANNALS of the American Academy of Political and Social Science* 676, no. 1 (March 2018): 115. [Retrieved online.](#)

118 World Economic Forum, *The Global Gender Gap Report 2018* (Geneva: World Economic Forum, 2018), 21, 63. [Retrieved online.](#)

119 Simon Denyer and Annie Gowen, “‘There’s Too Many Men’: What Happens When Women Are Outnumbered on a Massive Scale,” *Washington Post*, April 18, 2018. [Retrieved online.](#)

120 Quanbao Jiang, “Gender Imbalance and the Marriage Squeeze in China,” *Asia Dialogue* (blog), November 18, 2019. [Retrieved online.](#)

121 Laetitia Lhomme, Sue Zhong, and Billie Du, “Demi Bride Trafficking: A Unique Trend of Human Trafficking from South-East Asia to China,” *Journal of International Women’s Studies* 22, no. 3 (2021): 28.

neighboring countries such as Burma, where “extreme poverty, land grabs and military conflicts have made livelihoods unsustainable for many women.”¹²²

It is important to note that arranged marriages are not the same as forced marriages, however some may toe the “fine line between consent and coercion.”¹²³ Bride trafficking can involve forced marriages as well as voluntary arranged marriages where the bride and her family are deceived as to the groom’s circumstances or where the bride, upon arrival in China, is forced into sexual or labor exploitation.

Unsurprisingly, the demand for brides, as well as instances of bride trafficking, are most common in provinces that have the greatest gender imbalance. The gender gap is particularly pronounced in rural areas, which is connected to an overall cultural preference for male children as well as the localized need to have a supply of labor for family farms.¹²⁴

While China did amend its one-child policy in 2013 to allow families to have two children, which should have a positive impact on reducing some of the demand drivers, the government will still have to deal with the fact that human trafficking is an endemic problem with strong cultural ties. Additionally, as it took many decades to skew the population towards males, the country will not be able to resolve the gender imbalance quickly.

Chinese Policy Response to Human Trafficking

China’s treatment of human trafficking in its legislation and regulations reflects the country’s overall narrow view on the different forms of human trafficking. China does not have a law specifically targeting human trafficking, rather the crime is addressed primarily by China’s Criminal Law with additional coverage provided by the Labor Contract Law and Labor Law.

Human trafficking is directly covered under two articles in China’s Criminal Law: Articles 240 criminalizes the abduction and trafficking of women or children, while Article 241 criminalizes the purchase of abducted women and children, with the crimes covered by Article 240 treated as a more severe form of trafficking and therefore carrying harsher penalties.

The current language of Article 240 is unclear, as the Chinese government does not maintain an easily accessible, up-to-date catalog of official English translations of its laws. More than one government website shows Article 240 as described above, that is, targeting the abduction and trafficking of women and children with special provisions for serious offenses.¹²⁵

However, other sources, such as the UK Home Office’s 2021 report *China: Modern Slavery* and the Law & Regulations Database of The Republic of China (Taiwan) shows Article 240 as including both male and female victims as well as considering scenarios where victims are under the age of twenty,

122 Laura K. Hackney, “Re-Evaluating Palermo: The Case of Burmese Women as Chinese Brides,” *Anti-Trafficking Review*, no. 4 (2015): 98–119. [Retrieved online.](#)

123 “The Question of Arranged and Forced Marriages” (MilanMUN), accessed February 23, 2022. [Retrieved online.](#)

124 Jane Ni, “Selling Bodies and Souls: Human Sex Trafficking in China” (Honors Thesis, Albany, New York, University at Albany, State University of New York, 2015), 10. [Retrieved online.](#)

125 “Criminal Law of the People’s Republic of China,” The Supreme Court of the People’s Republic of China, December 1, 2015. [Retrieved online.](#); “Criminal Law of the People’s Republic of China,” Permanent Mission of the People’s Republic of China to the United Nations and Other International Organizations in Vienna, accessed March 16, 2022. [Retrieved online.](#)

victims are married, and when the trafficking is committed “for purpose of gain or for purpose of causing an abducted person to submit to an obscene act or to sexual intercourse.”¹²⁶

The Criminal Law directly addresses sex trafficking, specifically prostitution, and differentiates between an individual that “arranges for or forces” another person into prostitution (Article 358) and when an individual “lures... shelters... or procures” another person(s) into prostitution (Article 359). In 2011, Article 358 was amended to address anyone who “recruits or transports persons for an organizer of prostitution or otherwise assists in organizing prostitution.”¹²⁷ The two Articles are weighted differently in terms of severity, with the former carrying harsher punishments.

Both articles contain a provision whereby anyone who forces or lures “a girl under the age of 14 to engage in prostitution” is treated with harsher penalties. This means that anyone who forces or lures a girl aged 14 to 17, who are still considered minors under Chinese law, into prostitution is treated as though they were trafficking an adult. Additionally, the provisions ignore the fact that a boy could be forced or lured into prostitution, which is a major loophole in the treatment of sex trafficking and the protection of victims.

In 2015, the Standing Committee of the NPC amended the Criminal Law, whereby they reclassified the crime of “sex with underage prostitutes” (i.e. those under the age of 14) as rape, which significantly strengthened the level of punishment to include the death penalty.¹²⁸ While this is an important step forward in protecting children and recognizing them as underage victims of sexual exploitation, it only applies to individuals who rape minors, and does not appear to impact the penalties against those who force or lure children into prostitution.

Positively, China does criminalize any involvement—arranging for, forcing, or luring another person to engage in prostitution, sheltering prostitution, or procuring others to engage in prostitution—by employees of a business (referred to as “units”) in “the trade of hotels, in the catering or entertainment services, or in the taxi services” who takes advantage of their position (Article 361).¹²⁹ This is a valuable provision as it seeks to hold accountable those individuals who, in a “professional” capacity, actively or passively facilitate sex trafficking, and it could be strengthened by opening it up to all trades.

The crime of forced labor is covered in the Criminal Law under Article 244, which originally only addressed forced labor that was obtained via the restriction of personal freedom, and criminal punishment only appeared to be applicable in “serious circumstances.” However, in 2011 Beijing amended the law to criminalize “[forcing] any other person to work by violence, threat or restriction of personal freedom,” which would be punished with up to three years in prison or criminal detention and a fine, with serious circumstances resulting in three to 10 years imprisonment and a fine.¹³⁰

126 UK Home Office, *China: Modern Slavery*, Country Policy and Information Note (London: UK Home Office, 2021), 14. [Retrieved online.](#); “Criminal Code of the Republic of China,” Laws & Regulations Database of The Republic of China (Taiwan), June 16, 2021. [Retrieved online.](#)

127 “Criminal Law of the People’s Republic of China,” December 1, 2015.

128 “New Law Repeals Crime of Sex with Underage Prostitutes,” The National People’s Congress of the People’s Republic of China, August 31, 2015. [Retrieved online.](#)

129 “Criminal Law of the People’s Republic of China,” December 1, 2015.

130 “Criminal Law of the People’s Republic of China.”

The Labor Contract Law of 2007 includes several articles that touch on forced labor, such as Article 26, which states that a labor contract is invalidated if, among other items, “it is concluded or modified against a party’s true intention by means of deception or coercion, or when the party is in a precarious situation.” In addition, Article 38 states that an employee may terminate a labor contract if, among other circumstances, the employer forces them to work “by resorting to violence, intimidation, or illegal restriction of personal freedom” or if the employer “[fails] to pay labor remuneration on time and in full.”¹³¹

The law primarily calls for administrative sanctions and financial compensation, such as when an employer fails to pay an employee on time and in full (Article 85), however it does allow the State to apply criminal penalties for instances where an employer uses violence, intimidation, or the restriction of personal freedom to force an employee to work (Article 88).

The Labor Law of the People’s Republic of China, which was most recently amended in 2018, was drafted to protect, among other things, “the legitimate rights and interests of labourers [as well as] regulate labour relationship.” Article 96 compliments Article 26 of the Labor Contract Law by prohibiting employers from using “violence, intimidation or illegal restriction of personal freedom” to compel a laborer to work, and lays out penalties.¹³²

China’s Criminal Law reflects a limited appreciation of what human trafficking can entail, overlooking some of the nuances of the actions involved in trafficking as well as the different types of exploitation. The Palermo Protocol defines human trafficking as “the recruitment, transportation, transfer, harbouring or receipt of persons, by means of the threat or use of force or other forms of coercion, of abduction, of fraud, of deception, of the abuse of power or of a position of vulnerability or of the giving or receiving of payments or benefits to achieve the consent of a person having control over another person, for the purpose of exploitation... [that] shall include, at a minimum, the exploitation of the prostitution of others or other forms of sexual exploitation.”¹³³

The CECC points out that China’s definition of human trafficking under its Criminal Law is not consistent with the Palermo Protocol, notably that “Chinese law focuses on the act of selling a woman or child, rather than the purpose of exploitation. Furthermore, the definition of trafficking in the PRC Criminal Law does not clearly cover all forms of trafficking listed in the Palermo Protocol, including certain types of non-physical coercion; offenses against male victims; and forced labor, though forced labor is illegal under a separate provision of the law.”¹³⁴

For example, China’s law focuses largely on prostitution; however, sex trafficking encompasses more than just prostitution and prostitution does not always involve sex trafficking. Exploitative commercial sex acts can involve prostitution, but can also include acts such as “sexually explicit performances... participation in the production of pornography, performance in a strip club, or exotic dancing or display.”¹³⁵ By fixating on prostitution in its discourse on human trafficking, the Chinese government

131 “Labor Contract Law of the People’s Republic of China” (2007). [Retrieved online.](#)

132 “Labor Law of the People’s Republic of China” (1994). [Retrieved online.](#)

133 United Nations, “Protocol to Prevent, Suppress and Punish Trafficking in Persons, Especially Women and Children, Supplementing the United Nations Convention against Transnational Organized Crime (Palermo Protocol)” (2000). [Retrieved online.](#)

134 Congressional-Executive Commission on China, *CECC Annual Report 2020*, 176.

135 “Commercial Sex Definition,” Law Insider, accessed February 22, 2022. [Retrieved online.](#)

falls into a trap like many other countries: they are much more likely to overlook other forms of trafficking, both sexual and labor, which limits their ability to craft effective legislation/regulations, successfully identify victims (as well as traffickers), and engage in meaningful enforcement actions.¹³⁶

Besides the government's use of forced labor, one reason why the crime may not be given as much attention by the Chinese government is that some of the scenarios, or indicators, of forced labor involve accepted practices. For example, GSI reports that it is common practice in the construction sector to pay workers in arrears, as well as "other exploitative practices such as withheld wages and non-payment, excessive and illegal overtime, and widespread lack of employment contracts."¹³⁷

While China has corrected some loopholes, there is still some weakness with penalties, which can translate to ineffective deterrence. For example, a recent NPR article points out that "purchasing trafficked people was not covered by criminal law until 1997, and a serious loophole allowed the crime to avoid prosecution until 2015, after which a purchaser now faces a maximum three-year prison sentence—a lighter punishment than that for purchasing an endangered wild animal."¹³⁸

China has released three action plans to combat human trafficking, publishing the first more than 15 years ago. China first established its five-year National Plan of Action on Combating Trafficking in Women and Children in 2008, with the country identifying child abduction, forced marriage and trafficking into the sex industry as its priorities. The ensuing action plan, China's Action Plan Against Human Trafficking (2013–2020), was broadened to include "labour trafficking, forced begging, child performance, and organised theft to the list of human trafficking crimes," however Hackney points out that "despite these inclusions, the Chinese government continues to mainly focus on child abductions and bride trafficking, due to international concerns."¹³⁹

According to the Chinese government, the China National Plan of Action on Combating Trafficking in Persons (2021–2030) calls for, among other areas of action, "improving community-based network for preventing human trafficking... a severe crackdown on human trafficking using the internet... [and] investigation methods to be modernized and upgraded, calling for improving the information release system and the national DNA database for missing children."¹⁴⁰

Chinese Enforcement Response to Human Trafficking

China's record on investigations, prosecutions and convictions for human trafficking offenses is unclear as the government has not released any comprehensive data. Despite this, the overall impression of China's enforcement response is that it is predominately focused on sex trafficking, particularly forced prostitution, and that effective actions are inhibited by corruption, bureaucracy, and a desire to minimize any negative press.

136 Ella Cockbain and Kate Bowers, "Human Trafficking for Sex, Labour and Domestic Servitude: How Do Key Trafficking Types Compare and What Are Their Predictors?," *Crime, Law and Social Change* 72, no. 1 (August 1, 2019): 9–10. [Retrieved online.](#)

137 "Global Slavery Index 2018: China."

138 Aowen Cao and Emily Feng, "The Mystery of the Chained Woman in China," NPR, February 17, 2022. [Retrieved online.](#)

139 Hackney, "Re-Evaluating Palermo."

140 "China Issues Action Plan to Fight Human Trafficking," The State Council of the People's Republic of China, April 29, 2021. [Retrieved online.](#)

In an interview with the Council of Foreign Relations, Margaret Lewis described the state of human trafficking in China as “deeply troubling,” and that there are “concerns regarding the seriousness with which the government is investigating and prosecuting sex and labor traffickers.”¹⁴¹ This opinion on the effectiveness of China’s enforcement is shared by Hackney, who explains that the Ministry of Public Security, when implementing the Action Plans, typically uses “strike hard” tactics when targeting traffickers. She reports that these campaigns “are short-lived and expensive, both in terms of financial expenditures and human capital,” and have “dismal success rates,” yet allow the Chinese government to avoid making meaningful “reforms to economic or immigration policy.”¹⁴²

The superficial nature of some of China’s actions also underscore its preoccupation with prostitution and the misconceptions that the act is the be-all and end-all form of human trafficking and that all prostitution qualifies as sex trafficking. Ling explains that China has used its law enforcement crackdowns on prostitution as evidence of its efforts to combat human trafficking, despite the fact that human trafficking is “a broad category that includes different victims and for various purposes of exploitation beyond the prostitution of others.”¹⁴³

The strong social stigma around prostitution in China has caused many human trafficking victims to be arrested for prostitution, even when law enforcement is aware that they were involved involuntarily. The GSI reports that, while “the National Action Plan to Combat Human Trafficking states that the penalties for victims who are deceived or coerced into engaging in criminal activity are to be reduced or exempted... victims of commercial sexual exploitation are reportedly punished for engaging in prostitution, an activity that is illegal in China.”¹⁴⁴

Another deterrent to victims seeking help is fear of deportation, which is particularly true for North Koreans who have fled the country to China. North Korean human trafficking victims may believe their present situation of victimization is better than the punishment they will receive upon being deported from China and repatriated to North Korea. China typically treats North Koreans who flee their country’s regime and enter China as criminals and/or illegal economic migrants rather than refugees.

China has shown a reluctance to pursue criminal cases using anti-trafficking statutes; rather, the State Department reports, they prosecute human trafficking crimes “under laws pertaining to domestic violence, labor contract violations, and child abuse, all of which prescribed lesser penalties... [for example,] the government continued to handle most cases with indicators of forced labor as administrative issues through the Ministry of Justice.”¹⁴⁵

International Cooperation

China does engage with other jurisdictions, including law enforcement cooperation, to investigate and combat human trafficking. The most notable example is the Coordinated Mekong Ministerial

141 Margaret K. Lewis, *Why Beijing Fails to Fight Human Trafficking*, interview by Eleanor Albert, Council on Foreign Relations, July 10, 2017. [Retrieved online.](#)

142 Hackney, “Re-Evaluating Palermo.”

143 Bonny Ling, “Prostitution and Female Trafficking in China,” *China Perspectives* 2018, no. 1–2 (June 1, 2018): 65. [Retrieved online.](#)

144 “Global Slavery Index 2018: China.”

145 U.S. Department of State, *TIP Report 2021*, 175.

Initiative against Trafficking in the Greater Mekong Sub-region (COMMIT). This initiative stems from a memorandum of understanding signed by China, Cambodia, Laos, Myanmar, Thailand and Vietnam in 2004 which sought to “[combine] efforts on prevention of trafficking, prevention of victims, and their repatriation and reintegration, and prosecution of the criminals responsible.”¹⁴⁶

According to partner countries, however, shortcomings in the country’s international collaboration include China’s almost sole focus on the victimization of Chinese nationals abroad as well as China having “cumbersome law enforcement bureaucracy” and being “unresponsive to requests for bilateral cooperation on cross-border trafficking cases.”¹⁴⁷

Another major impediment to combatting human trafficking in the region is China’s political and economic influence. *The New York Times* writes that the reports of bride trafficking from Pakistan “are a disturbing aspect of China’s growing presence in [the country], a longtime ally drawn closer lately by expanding economic ties—including China’s Belt and Road infrastructure project.”¹⁴⁸

For example, a 2019 Pakistani government investigation into bride trafficking identified 629 Pakistani girls and women who “since 2018 had been allegedly trafficked to China and forced to marry Chinese men... many [of whom] were isolated and physically and sexually abused... [or] were forced into prostitution.”¹⁴⁹ However, as the *Associated Press* reports, despite building strong intelligence and cases against traffickers, both Chinese and Pakistani, the “investigators’ aggressive drive against the networks has largely ground to a halt... because of pressure from government officials fearful of hurting Pakistan’s lucrative ties to Beijing.”¹⁵⁰

Social and cultural phenomena in China combined with economic policy have played an important role in creating the demand for trafficking victims. While some of this demand is met locally, it has also spilled over into neighboring countries. In addition, China’s political policies have authorized state-sponsored forced labor as a widely-used tool to use against dissidents, criminals, and any other persons who draw Beijing’s ire.

China’s response to human trafficking, in terms of policy and enforcement, can be characterized as failing to effectively and efficiently acknowledge and/or address both the different types of human trafficking as well as the range of potential victims. The human trafficking framework is strongly exclusionary to men, focusing almost exclusively on women and children, and largely fixates on sex trafficking, particularly forced prostitution. This has major repercussions in terms of adequately identifying and responding to both traffickers and victims.

146 “Coordinated Mekong Ministerial Initiative against Trafficking (COMMIT Process),” International Organization for Migration, accessed February 16, 2022. [Retrieved online.](#)

147 U.S. Department of State, *TIP Report 2021*, 176.

148 Salman Masood and Amy Qin, “She Thought She’d Married a Rich Chinese Farmer. She Hadn’t.,” *The New York Times*, May 27, 2019. [Retrieved online.](#)

149 Miriam Berger, “An Investigation Found Pakistani Christian Women Being Trafficked to China as Brides. Then Officials Shut It Down.,” *The Washington Post*, December 5, 2019. [Retrieved online.](#)

150 “AP Exclusive: 629 Pakistani Girls Sold as Brides to China,” Associated Press, December 7, 2019. [Retrieved online.](#)

Counterfeiting and Intellectual Property Theft

Despite being the most valuable transnational crime in the world, counterfeiting and intellectual property (IP) theft has long flown under the radar, overshadowed by the violence generated by crimes such as drug and human trafficking. However, counterfeiting and IP theft present significant economic and security threats to both the public and private sectors. As a crime it also represents a grave risk to global public health and safety. While China plays an oversized role in the production of synthetic drugs and precursor chemicals, as highlighted earlier in this report, this activity is dwarfed by the country's contribution to the production of counterfeits and the perpetration of IP theft.

Counterfeiting refers to the manufacturing and/or distribution of goods, typically of lesser value and quality, that violate a patent, design rights, or trademark of the genuine product. This can range from knock-offs of famous brands to fake everyday consumer goods as well as specialized items. Any product is fair game for counterfeiting as long as there is a profit to be made. Closely related to counterfeiting is IP crime, which involves the theft of “ideas, inventions, and creative expressions... which can include everything from trade secrets and proprietary products and parts to movies, music, and software.”¹⁵¹

A 2016 report by Frontier Economics estimated the global trade in counterfeit and pirated products—which includes international trade, domestic trade, and digital trade—generated US\$923 billion to US\$1.13 trillion in 2013; of this, US\$461 billion was related to the international trade of counterfeits, equal to 2.5 percent of global GDP.¹⁵² A 2019 study by the Organization for Economic Co-operation and Development (OECD) and the European Union Intellectual Property Office (EUIPO) has shown that these crimes continue to grow, putting the value of international counterfeit trade alone at US\$509 billion in 2016, equivalent to 3.3 percent of global GDP.¹⁵³

In the international trade in counterfeit and pirated goods, China holds the preeminent position. The U.S. Chamber of Commerce estimated that 86 percent of globally-traded counterfeits originated in mainland China and Hong Kong (70 percent and 16 percent, respectively).¹⁵⁴ Assuming their share of the market has remained the same, this would be worth almost US\$438 billion when applied to the most recent international trade estimate from the OECD and EUIPO.

Counterfeiting

When most people think about counterfeit and pirated goods, the first things that come to mind are luxury goods or popular brands, such as fake Louis Vuitton purses or Apple products.¹⁵⁵ However, the range of goods which are counterfeited is much more universal as well as insidious, including items

151 “Intellectual Property Theft/Piracy,” Federal Bureau of Investigation, accessed January 15, 2020. [Retrieved online.](#)

152 Frontier Economics, *The Economic Impacts of Counterfeiting and Piracy* (Paris: International Chamber of Commerce; International Trademark Association, 2016), 8. [Retrieved online.](#)

153 Organization for Economic Co-operation and Development and European Union Intellectual Property Office, *Trends in Trade in Counterfeit and Pirated Goods* (Paris: OECD Publishing; EUIPO, 2019), 11. [Retrieved online.](#)

154 U.S. Chamber of Commerce, *Measuring the Magnitude of Global Counterfeiting* (Washington, D.C.: U.S. Chamber of Commerce, 2016), 3. [Retrieved online.](#)

155 “Thousands of Fake Apple AirPods Worth \$1.3 Million Seized by Cincinnati CBP,” U.S. Customs and Border Protection, July 15, 2021. [Retrieved online.](#); “\$30M in Fake Designer Bags, Clothes Seized at SoCal Ports Ahead of Holidays,” FOX 5 San Diego, December 2, 2021. [Retrieved online.](#)

like toothpaste and baby food as well as microchips and pharmaceuticals. The variety of counterfeit goods produced and exported from China is vast, including perfumery and cosmetics, footwear, leather articles, clothing, jewelry, electronics and electrical equipment, sunglasses, and watches.¹⁵⁶ Yet some of the more notable counterfeits of Chinese origin include items that have a direct impact on health and safety.

In the midst of the COVID-19 pandemic, these two issues—health and safety—have been at the forefront of global concern. No item exemplifies this more than the face mask, particularly N95 masks and their Chinese equivalent, KN95. The U.S. has been flooded by counterfeit or ill-constructed masks, with China as the overwhelming source country. *The New York Times* notes that e-commerce platforms like Amazon are inundated with “fake or poorly made KN95s, a Chinese-made mask that is often marketed as an N95 equivalent;”¹⁵⁷ the U.S. Centers for Disease Control estimates that 60 percent of KN95s sold within the United States are counterfeit.¹⁵⁸

Other counterfeit goods from China include medicines, which can cause adverse side effects, directly result in deaths, and contribute to public health crises as the reduced or missing active ingredients in anti-infective medicines can lead to drug resistance.¹⁵⁹ Counterfeit Chinese goods also negatively impact the public sector, with fraudulent items, such as crucial military vehicle, aircraft, and computer parts, finding their way into government supply chains, including that of the U.S.¹⁶⁰

While China is by far the largest source country for counterfeit and pirated goods consumed internationally, the domestic Chinese market is quite small, with the OECD reporting that those counterfeit and pirated goods imported into the country are “fundamentally different” than those exported.¹⁶¹ However, this does not mean that Chinese companies are left unscathed; the OECD noted that “the majority of internationally traded goods that infringe Chinese brands (72%)” are actually produced in China, suggesting that Chinese counterfeiters cause significant harm both at home and abroad.¹⁶²

IP Theft

Closely connected to counterfeiting is IP theft, which, as noted above, is the theft of designs, inventions, or trade secrets from an individual or entity. Just like counterfeiting, China leads the world in IP infringement: The National Bureau of Asian Research estimates that globally, China is responsible for 50 to 80 percent of international IP theft.¹⁶³ As noted by the OECD, “trade secret theft is a seri-

156 Organisation for Economic Co-operation and Development, *Governance Frameworks to Counter Illicit Trade* (Paris: OECD, 2018), 172. [Retrieved online.](#)

157 Andrew Jacobs, “Counterfeit Covid Masks Are Still Sold Everywhere, Despite Misleading Claims,” *The New York Times*, November 30, 2021. [Retrieved online.](#)

158 CDC, “Types of Masks and Respirators,” Centers for Disease Control and Prevention, September 23, 2021. [Retrieved online.](#)

159 Erwin A. Blackstone, Joseph P. Fuhr, and Steve Pociask, “The Health and Economic Effects of Counterfeit Drugs,” *American Health & Drug Benefits* 7, no. 4 (June 2014): 217.

160 Brandon Sullivan and Jeremy Wilson, “Counterfeit Parts in the U.S. Department of Defense Supply Chain,” Michigan State University, 2016. [Retrieved online.](#)

161 Organisation for Economic Co-operation and Development, *Governance Frameworks to Counter Illicit Trade*, 172.

162 Organisation for Economic Co-operation and Development, 172.

163 Eric Rosenbaum, “1 in 5 Corporations Say China Has Stolen Their IP within the Last Year: CNBC CFO Survey,” CNBC, March 1, 2019. [Retrieved online.](#)

ous and growing problem” in China.¹⁶⁴ This theft can be attributed to both private and public sector actors; however, due to the Chinese government’s large involvement in the private sector, most commonly through state-owned enterprises (SOEs), it could be argued that much of the IP theft is state-sanctioned.

In regards to how the IP is obtained, China takes both indirect and direct approaches. As the *Chicago Tribune* explains, Beijing doesn’t just rely on spies to engage in commercial espionage, rather it also “encourages Chinese [citizens] who study and work abroad to copy or steal technology and rewards them when they do.”¹⁶⁵ For example, two Chinese nationals who were working at Apple have been indicted in the U.S. for theft of trade secrets for allegedly stealing IP—including photos, schematics, manuals, etc.—related to the company’s self-driving car initiative; both individuals were in the process of applying for positions at Chinese companies engaged in autonomous vehicle development.¹⁶⁶ Closer to the government, in 2019, Chinese state-owned Fujian Jinhua Integrated Circuit Co. Ltd., along with Taiwan-based United Microelectronics Corp., was charged in U.S. federal court for stealing IP trade secrets linked to the American company Micron Technology, which produces computer memory and data storage components.¹⁶⁷

SPOTLIGHT ON...

CHINESE IP THEFT OF MILITARY TECHNOLOGY

by Brett Bolog

The Chinese government, through its military and intelligence services, government-sponsored hacking groups, and SOEs, engages in large-scale IP theft from foreign militaries, with a central focus on U.S. military technology.¹ Through multiple espionage and cyberattack operations, China has obtained U.S. IP and trade secrets in the maritime, aviation, aerospace, cybersecurity, satellite, and nuclear industries, as well as military technical data and plans.²

The main targets for Chinese IP theft within the U.S. include defense contractors, technology and cybersecurity companies, academia, and the military. Additionally, China targets nations around the world that interfere with their geopolitical interests or those that have advanced industries from which China can benefit. Examples include military plans, secret documents, intelligence surveillance and communications systems infiltrated by the Chinese in the Phil-

1 National Counterintelligence and Security Center, *Foreign Economic Espionage in Cyberspace, 2018* (Washington, D.C.: National Counterintelligence and Security Center, 2018), 5. [Retrieved online.](#)

2 National Counterintelligence and Security Center, 7.

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164 Organisation for Economic Co-operation and Development, *Governance Frameworks to Counter Illicit Trade*, 185.

165 Paul Wiseman and Michael Liedtke, “Here Are 5 Cases Where the U.S. Says Chinese Companies and Workers Stole American Trade Secrets,” *Chicago Tribune*, February 21, 2019. [Retrieved online.](#)

166 Mike Peterson, “FBI to Charge Second Chinese Citizen for Stealing Apple Car Trade Secrets,” *IDrop News* (blog), December 21, 2020. [Retrieved online.](#)

167 Kathrin Hille, “Trade War Forces Chinese Chipmaker Fujian Jinhua to Halt Output,” *Financial Times*, January 28, 2019. [Retrieved online.](#)

ippines and Vietnam,³ along with supply chain and advanced technology information in Canada, Germany, and Australia.⁴

Within the U.S., the Chinese government and/or its affiliates have stolen IP on American undersea-warfare capabilities, such as quieter submarines, radio communications, and advanced sensors,⁵ and technical data and design plans on the C-17 transport aircraft,⁶ F-18A and F-35 fighter jets, the Patriot Missile System, the Navy's Littoral Combat Ship, the Navy's Aegis ballistic-missile defense system, and the V-22 Osprey and Blackhawk helicopters.⁷

China has a variety of methodologies with which to steal IP and foreign military technologies. Similar to the way in which China steals economic, commercial, and cyber intellectual property and information, China enlists a broad range of actors. The Chinese military and intelligence services use non-traditional collectors, joint ventures, research partnerships, academic collaborations, sales and trading investments, mergers and acquisitions, front companies, and talent recruitment programs to acquire technical information and trade secrets from U.S. academic, military, and intelligence facilities.⁸

For example, Chinese SOEs like China General Nuclear Power Company (CGNPC) have allegedly stolen military technology: the U.S. indicted CGNPC in 2016 for illegally attaining sensitive nuclear technology over a 20-year period, which may have bolstered Chinese nuclear-powered submarines, icebreakers, and other advanced weaponry.⁹ In addition, Beijing is known to sponsor hacking groups, known as advanced persistent threat (APT) groups, to steal IP; the indirect manner provides the government with plausible deniability.¹⁰ There are numerous APT groups with suspected affiliation with China including APT31, APT40, and APT41, which typically deploy malware via spear phishing campaigns, web compromises, and/or application vulnerabilities.¹¹

3 Anni Piiparinen, "The Chinese Cyber Threat in the South China Sea," *The Diplomat*, September 18, 2015. [Retrieved online.](#)

4 U.S. Department of Defense, *Assessing and Strengthening the Manufacturing and Defense Industrial Base and Supply Chain Resiliency of the United States: Report to President Donald J. Trump by the Interagency Task Force in Fulfillment of Executive Order 13806* (Washington, D.C.: U.S. Department of Defense, 2018), 36. [Retrieved online.](#)

5 Sinéad Baker, "The US Says China Is Stealing Technology to Modernize Its Military, and That Could Erode American Dominance," *Business Insider*, May 3, 2019. [Retrieved online.](#)

6 "Chinese National Pleads Guilty to Conspiring to Hack into U.S. Defense Contractors' Systems to Steal Sensitive Military Information," U.S. Department of Justice, March 23, 2016. [Retrieved online.](#)

7 Alexander Abad-Santos, "China Is Winning the Cyber War Because They Hacked U.S. Plans for Real War," *The Atlantic*, May 28, 2013. [Retrieved online.](#)

8 National Counterintelligence and Security Center, *Foreign Economic Espionage in Cyberspace*, 2018, 6.

9 "China Hacked Sensitive U.S. Navy Undersea Warfare Plans: Washington Post," Reuters, June 8, 2018. [Retrieved online.](#); "U.S. Nuclear Engineer, China General Nuclear Power Company and Energy Technology International Indicted in Nuclear Power Conspiracy against the United States," U.S. Department of Justice, April 14, 2016. [Retrieved online.](#)

10 "Two Chinese Hackers Associated With The Ministry Of State Security Charged With Global Computer Intrusion Campaigns Targeting Intellectual Property And Confidential Business Information," U.S. Department of Justice, December 20, 2018. [Retrieved online.](#)

11 "Advanced Persistent Threat Groups," Mandiant, accessed April 4, 2022. [Retrieved online.](#)

When China acquires IP from foreign militaries and defense contractors, they are illicitly and unfairly bolstering their military and closing the technological gap between themselves and their counterparts. Rampant IP theft allows the Chinese government to advance their geopolitical interests, which places the safety and security of the all nation states at risk.

In China, the issue of IP theft is tied to the state's forced technology transfer, which "refers to an informal government practice which requires the transfer of technology from foreign investors as a condition of market access or investment."¹⁶⁸ It is important to note that technology transfer is not, in and of itself, a negative or damaging practice, and can actually be quite beneficial for developing countries; nor is the practice rare. Although foreign companies do voluntarily accept this precondition, a 2018 study by the European Union Chamber of Commerce in China found that "1 in 5 foreign companies says it feels compelled to transfer technology to the Chinese as the price of market access."¹⁶⁹

As the largest economy in the world, it is not surprising that the U.S. is a primary target of Chinese IP theft. CNBC reports that "one in five North American-based corporations on the CNBC Global CFO Council says Chinese companies have stolen their intellectual property within the last year."¹⁷⁰ A 2017 investigation of China's technology transfer regime by the U.S. Trade Representative (USTR) determined that the country's practices were unreasonable as well as restrictive on U.S. commerce due to "(1) forced technology transfer requirements, (2) cyber-enabled theft of U.S. IP and trade secrets, (3) discriminatory licensing practices, and (4) state-funded strategic acquisition of U.S. assets."¹⁷¹ The U.S. Department of Justice launched the China Initiative in 2018, a campaign to address Chinese trade theft cases,¹⁷² which, in 2020 alone, numbered around 1,000.¹⁷³

Actors

Counterfeiting and IP theft are high-profit, low-risk activities that attract a variety of actors. While the sale of counterfeit goods by criminal and terrorist actors has received a relatively large amount of attention, it is the companies that produce counterfeits that arguably are the worst actors. Indeed, some of these companies also actively work with purchasers to improve the quality of the counterfeit

168 Jyh-An Lee, "Forced Technology Transfer in the Case of China," *Boston University Journal of Science & Technology Law* 26, no. 2 (2020): 328. [Retrieved online.](#)

169 Wiseman and Liedtke, "Here Are 5 Cases."

170 Rosenbaum, "1 in 5 Corporations Say China Has Stolen Their IP within the Last Year: CNBC CFO Survey."

171 Andrew B. Schwarzenberg, "Section 301 of the Trade Act of 1974" (Washington, D.C.: Congressional Research Service, June 15, 2021), 2. [Retrieved online.](#); U.S. Trade Representative, *Findings of the Investigation into China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation Under Section 301 of the Trade Act of 1974* (Washington, D.C.: Executive Office of the President, U.S. Trade Representative, 2018). [Retrieved online.](#)

172 "Attorney General Jeff Sessions Announces New Initiative to Combat Chinese Economic Espionage," U.S. Department of Justice, November 1, 2018. [Retrieved online.](#)

173 Catalin Cimpanu, "FBI Is Investigating More than 1,000 Cases of Chinese Theft of US Technology," ZDNet, February 8, 2020. [Retrieved online.](#)

and/or facilitate the sales. For example, in November 2021 the owner of a Texas vape shop pleaded guilty to trafficking in counterfeit vaping-related goods, revealing that he “regularly communicated with Chinese manufacturers about the production and sale of counterfeit vaping products... [including consulting] with Chinese manufacturers on methods to imitate the branding and logos of well-known American vape companies and imported and sold imitation vaping devices, labels and packaging.”¹⁷⁴

Chinese e-commerce platforms like Alibaba (including Taobao), Pinduoduo, JD, Suning, and Meituan-Dianping have come under fire in the past from Chinese authorities (and other international authorities as well as companies) for hosting the sale of counterfeit goods. A report by China’s State Administration of Industry and Commerce found “only 37.25 percent of the goods the authorities examined on Taobao to be genuine.”¹⁷⁵ The USTR has “blacklisted” Taobao, Pinduoduo and other similar platforms, placing them on its Notorious Markets Review, a list of digital marketplaces that fail to sufficiently prevent copyright piracy and the sale of counterfeit goods.¹⁷⁶

Many of the marketplaces have stepped up their efforts to fight counterfeits, such as quickly identifying and shutting down those suspected of IP infringement, working with brand owners, and refunding consumers that unknowingly buy counterfeit goods. Despite attempts to better police their platforms, these companies still face a serious game of “whack-a-mole,” with counterfeit sellers using a variety of ways to evade detection, such as “[redirecting] clients to separate sales websites [and modifying] the brand name” as well as listing the counterfeit good at a price similar to the real item, only revealing the actual, much lower price to interested buyers in a private chat.¹⁷⁷

SPOTLIGHT ON...

THE DAIGOU SYSTEM

While much attention has been placed on the manufacture of counterfeit goods in China and their distribution onto the international market, brand owners also face serious challenges with parallel imports, also known as gray market goods. Parallel imports involve “branded goods that are imported into a market and sold there without the trademark owner’s consent in that market.”¹ While legal in many countries, including China, parallel import products can in some instances “create market distortions, attack the official supply chain, double the risk of product liability and dilute trademarks.”²

1 “Parallel Imports / Gray Market,” International Trademark Association, accessed December 8, 2021. [Retrieved online.](#)

2 Paolo Beconcini, “Time to Act Against Chinese Parallel Import of Foreign Cosmetic Products,” Global IP & Technology Law Blog, September 15, 2020. [Retrieved online.](#)

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174 “Texas Vape Shop Owner Pleads Guilty to Unlawful Importation of Counterfeit Vaping Products,” U.S. Department of Justice, November 24, 2021. [Retrieved online.](#)

175 Eunice Yoon and Haze Fan, “China Agency Slams Alibaba for Fakes,” CNBC, January 28, 2015. [Retrieved online.](#)

176 Franklin Chu, “Why It’s so Hard to Root out Fake Goods in China Ecommerce,” Digital Commerce 360, May 30, 2019. [Retrieved online.](#); U.S. Trade Representative, “2020 Review of Notorious Markets for Counterfeiting and Piracy” (Washington, D.C.: U.S. Trade Representative, 2020). [Retrieved online.](#)

177 “Behind the Counterfeit Goods Industry in Modern China,” Daxue Consulting, July 4, 2021. [Retrieved online.](#)

THE DIAGOU SYSTEM

China's extensive *daigou* system, by which Chinese expatriates purchase goods overseas—particularly those that can't be found in China or are cheaper abroad—on behalf of consumers in China, is a massive US\$40 billion a year “industry” that “can make life very difficult for foreign brand owners’ authorized distributors in [China], which are forced to compete against cheaper genuine imports available to any reseller that can source them through those *daigou* channels.”³ As noted in a recent court case brought by Fendi (via its parent company LVMH) some “parallel traders in China often take things a step further... [by making] extensive use of other intellectual property belonging to the brand owner to enhance their sales pitch, and to try to create the false impression that they are authorized by the brand owner.”⁴

³ “China's Vast Network of Gray-Market Shoppers Grounded by the Pandemic,” *Bloomberg.com*, 2021. [Retrieved online.](#)

⁴ Dan Plane and Mai Lin, “Fendi Case Shed Light on Challenging Fight Against Parallel Imports in China,” *The Fashion Law* (blog), September 17, 2021. [Retrieved online.](#)

Chinese Policy Response to Counterfeiting and IP Theft

The majority of China's recognition of and laws on IP were developed over the last 40 years. Daniel Fleming points to the 1979 Agreement on Trade Relations Between the United States and the People's Republic of China as “one of the earliest indications of China's attempt to adopt Western concepts in intellectual property.”¹⁷⁸ China's legal foundation for addressing intellectual property was established in the 1980s and is enforced by the China National Intellectual Property Administration (CNIPA).

China's IP legislation is founded around the idea of “first to file,” that is, the law protects whomever is the first to file a patent rather than whomever actually first came up with the invention. This position is seen in China's trademark law, which only provides protection “for marks that are already ‘famous,’ thus making it difficult, if not impossible, to protect new or relatively unknown trademarks.”¹⁷⁹

China undertook comprehensive reforms of its IP regime between 2018 and 2020, including amendments to the Trademark Law (with a focus to “curb bad-faith applications, strengthen protection, and foster a favourable business environment”), the Anti-Unfair Competition Law, the Patent Law, and the Copyright Law.¹⁸⁰ While China has taken these much-needed steps, more still needs to be done, and it is yet to be seen whether the country will enforce its updated IP legislation both sufficiently and evenly.

¹⁷⁸ Daniel C. Fleming, “Counterfeiting in China,” *East Asia Law Review* 10, no. 2 (2014). [Retrieved online.](#)

¹⁷⁹ Fleming.

¹⁸⁰ World Trade Organization, *Trade Policy Review, Report by the Secretariat: China*, vol. WT/TPR/S/415 (Geneva: World Trade Organization, 2021), 109. [Retrieved online.](#)

Chinese Enforcement Response to Counterfeiting and IP Theft

In regards to enforcement action that has occurred, over the last five years, reports and media coverage do show an increase compared to previous years, however crackdowns have been largely focused on the sale of counterfeits, particularly e-commerce websites that have not instituted sufficient safeguards to prevent the sale of counterfeits on their platform, rather than the manufacture of counterfeit goods.

China's new E-Commerce Law, which entered into force in 2019, now holds e-commerce platform owners/operators equally liable as the merchants that knowingly sell counterfeit goods on the platforms. In addition, individual sellers, such as those who operate via e-commerce platforms as well as social media, are now required to "register their businesses, obtain a business license, and file and pay taxes. This includes many *daigou* sellers, who smuggle products into China and resell them at a mark-up."¹⁸¹

Modernization and innovation have been driving tenets behinds China's economic and social development, with the government investing significant resources—financial, political, and more—into achieving the country's goal of becoming a global powerhouse. It could be argued that the counterfeit industry in China is a "symptom of economic growth," that with the massive reform and opening of China's economy beginning in the late 1970s, the country's manufacturing capabilities grew to the point that "Chinese factories now have the skills needed to copy almost everything."¹⁸²

And given the scale of IP crime in China, in particular the production of counterfeit goods, it would be reasonable to conclude that counterfeiting represents a relatively important share of China's economy. A 2007 Euromonitor International piece reported that "official estimates suggest that counterfeit products account for 15%-20% of products made in China, representing 8% of China's US\$2.6 trillion GDP."¹⁸³ While the estimate is 15 years old, counterfeiting has, at the very least, remained a stable—if not growing—"industry" in China; assuming counterfeiting still represents 8 percent of China's GDP, this would be equal to nearly US\$1.2 trillion in 2020.¹⁸⁴

Considering the significant economic implications, the willingness of Chinese officials to sufficiently crackdown on counterfeiting, including putting a not-so meager number of people out of work, comes into question. A 2012 report provided the following anecdote: "When a local government in Shenyang, China announced a crackdown on counterfeit goods, nintey [sic] percent of store owners responded by shutting down, creating a veritable ghost town... The Shenyang authorities held an emergency meeting in response to the store closures and announced that they were not conducting a crackdown and asked stores to reopen."¹⁸⁵

Likewise, China understandably has a considerable desire to protect the competitiveness of its ever-expanding economy, including innovation and growth from sectors such as digital communication and computer technology. There is little doubt as to the extent to which the country will show

181 Chu, "Why It's so Hard to Root out Fake Goods in China Ecommerce."

182 "Behind the Counterfeit Goods Industry in Modern China."

183 "Fake Brands Recognising a Real Trend," Euromonitor International, July 27, 2007. [Retrieved online.](#)

184 "GDP (Current US\$) - China," The World Bank, accessed December 9, 2021. [Retrieved online.](#)

185 Daniel Goodman, "This Is Why China Can't And Won't Try To Eliminate Fake Goods," yahoo! finance, August 9, 2012. [Retrieved online.](#)

preferential treatment to domestic companies over foreign companies in IP-related issues. As Foreign Policy points out, “countries do not enact strong IP rights systems until their ability to innovate at home displaces reliance on outside knowledge.”¹⁸⁶

While Beijing is technically committed to cracking down on IP theft, the *Wall Street Journal* reports that recent Chinese court rulings have suggested that this commitment may not actually be genuine. “In four major cases since 2020,” the article noted, “Chinese courts granted so-called anti-suit injunctions blocking foreign companies from taking legal action anywhere in the world to protect their trade secrets.”¹⁸⁷ Foreign companies can find themselves powerless, as China seemingly refuses to enforce IP law but also, via anti-suit injunctions, can prevent companies from pursuing legal action in other jurisdictions.

International Cooperation

The manufacture and export of counterfeit goods as well as protection of IP rights have been central issues between U.S.-China relations. An integral part of the U.S.-China trade disputes that erupted during the Trump administration is connected to the claim that “Beijing systematically steals American and other foreign intellectual property in a bid to become the world’s technology superstar.”¹⁸⁸ The China-United States Phase 1 Economic and Trade Agreement contained provisions intended to strengthen enforcement action in China, including effective actions both against e-commerce platforms that host counterfeit items and to “stop the manufacture and distribution of counterfeits with significant health or safety risks,” such as pharmaceuticals, along with strengthening the law enforcement and judicial response and increasing the civil and criminal penalties for IP crimes.¹⁸⁹

It is interesting to note that, while both countries commit to/implement the provisions of the Agreement, for the majority of IP and technology transfer provisions, China will need to amend its existing legislation while the United States’ existing measures meet the desired standards. For example, China committed to, among other things: expand the scope of liability for trade secret misappropriation to all natural and legal persons; in civil judicial proceedings, shift the burden of proof to the accused party; and eliminate the requirement for the trade secret holder to prove actual losses in order to initiate a criminal investigation.

Trademark infringement, particularly geographical indicators (GIs), have served as a source of political and economic tension between the European Union (EU) and China as well.¹⁹⁰ In September 2020, the EU and China signed a bilateral agreement to protect each other’s GIs in their respective territory, that is, the EU will protect 100 Chinese GIs in its territory, while China will protect 100 European GIs in theirs.

186 Yukon Huang and Jeremy Smith, “China’s Record on Intellectual Property Rights Is Getting Better and Better,” *Foreign Policy*, October 16, 2019. [Retrieved online.](#)

187 Josh Zumbrun, “China Wields New Legal Weapons to Fight Claims of Intellectual Property Theft,” *Wall Street Journal*, September 26, 2021. [Retrieved online.](#)

188 Wiseman and Liedtke, “Here Are 5 Cases.”

189 World Trade Organization, *Trade Policy Review: China*, WT/TPR/S/415:116–17.

190 Geographical indicators (GIs), as defined in the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), are “indications which identify a good as originating in the territory of a Member, or a region or locality in that territory, where a given quality, reputation or other characteristic of the good is essentially attributable to its geographical origin.” See World Trade Organization, “Agreement on Trade-Related Aspects of Intellectual Property Rights” (1994), 328. [Available online.](#)

The impacts and victims of counterfeiting or IP theft are often not as readily apparent as those of other more “traditional” crimes such as narcotics or human trafficking; however, this does not mean the repercussions are inconsequential. These crimes have serious monetary, health, and safety consequences and contribute to the financing of organized crime and terrorism. As the global hegemon in counterfeiting and IP theft, China has a leading role in combating these crimes. Yet, with the manufacture and sale of counterfeits as well as IP theft representing important contributions to the Chinese economy, coupled with weak IP laws and enforcement, the country will remain a favorable host for these crimes until they actively decide to combat it.

ILLICIT TOBACCO TRADE

by Karen Alex Lopez

The global tobacco trade is one of the most profitable industries, reflected in a worldwide value of approximately US\$760 billion in 2020.¹ However, this trade has a corresponding black market, which consists of tobacco products that are “illegally manufactured, distributed, or sold.”² Three primary factors contribute to the presence of the illicit tobacco trade: a strong, worldwide demand for the goods (evidenced by the global market value); the fact that the products are taxed at different rates in different countries thereby creating an opportunity for jurisdictional arbitrage; and weak domestic controls on manufacturing and trade.

The illicit tobacco trade has three categories determined by differences in manufacture and trade: illicit whites, contraband cigarettes, and counterfeit cigarettes. While cigarettes are the most common illicitly traded tobacco product, all products are found on the black market, including loose tobacco, smokeless tobacco, and e-cigarettes.³

Illicit or cheap whites, as described by the European Commission (EC), are cigarettes “manufactured legitimately in one market, either taxed for local consumption or untaxed for export, and sold knowingly to traders who transport them to another country where the products are sold illegally without domestic duty paid.”⁴ Here it is the manufacturers who are orchestrating the illicit activity.

Contraband or grey market cigarettes are also legitimately manufactured but are diverted from the intended destination jurisdiction somewhere along the supply chain. The cigarettes are diverted by smuggling them from a low- or no-tax (i.e. duty-free) jurisdiction to a high-tax jurisdiction in order to maximize profits. As the Financial Action Task Force (FATF) explains, while smugglers typically target high-tax jurisdictions, they “will operate wherever there is scope to undercut a legitimate market and generate a suitable profit against their initial outlay.”⁵ The tobacco or cigarette manufacturers are typically not involved in the diversion of the goods. Contraband cigarettes may be smuggled internationally or domestically, such as from one state to another.

Counterfeit cigarettes are manufactured without authorization, that is, they are produced and distributed “bearing a trademark without the approval of the trademark owner.”⁶ They

1 “Global: Tobacco Market Value 2012-2025,” Statista, June 16, 2021. [Retrieved online.](#)

2 U.S. Department of State et al., *The Global Illicit Trade in Tobacco: A Threat to National Security* (Washington, DC: U.S. Department of State, 2015), 3. [Retrieved online.](#)

3 U.S. Department of State et al., 4.

4 Robert Ireland, “Quantifying the Illicit Trade in Tobacco: A Matter of Public Interest and Self-Interest,” *WCO News* (blog), accessed April 8, 2022. [Retrieved online.](#)

5 Financial Action Task Force, *Illicit Tobacco Trade* (Paris: Financial Action Task Force, 2012), 10. [Retrieved online.](#)

6 “Counterfeit Cigarettes,” *Tobacco Atlas*, December 19, 2018. [Retrieved online.](#)

may be intended for domestic consumption or smuggled from one country to another. As they are manufactured outside the regulated industry, there is a likelihood that they are produced below minimum quality standards.⁷

The illicit tobacco trade attracts a variety of actors, including individual “bootleggers,” OCGs, and legitimate manufacturing companies. Lone operators principally engage in tobacco smuggling by trading “in relatively smaller quantities than would be associated with OCGs” with methodologies that “are often less sophisticated, determined by whether it is opportunistic or market driven.”⁸ OCGs, which are leading participants within the illicit tobacco trade, often conduct large-scale operations in order to take advantage of the high-value market where demand for the product is constant.⁹

Tobacco companies engage in the illicit trade for two primary reasons. First, they can increase their profit margins by evading taxes through smuggling their products into the destination jurisdiction. Second, smuggling may also be an alternative way for companies to gain entry to new markets.¹⁰ It is both inexpensive and easy to produce and transport illicit white cigarettes across borders, evading regulators, customs, and law enforcement.

China is the largest grower of tobacco in the world, producing 2.1 million tons of tobacco yearly, which represents one-third of global tobacco production.¹¹ The China National Tobacco Corporation (CNTC), an SOE founded in 1982, is the world’s largest producer of cigarettes by revenue,¹² and controls about 45 percent of the global cigarette market.¹³ It principally supplies China’s domestic market, however the company has begun to expand into the overseas market as well.¹⁴

China has a “unified” tobacco system, with the CNTC—the country’s tobacco manufacturer—coupled with the State Tobacco Monopoly Administration (STMA)—the tobacco industry regulator—into a single organization with shared management, personnel, and finance. There are inherent contradictions in marrying two entities with essentially opposite missions, as the profit-driven actions of the CNTC (and therefore the government) are welded together

7 Ulrik Boesen, “Cigarette Taxes and Cigarette Smuggling by State,” *Tax Foundation* (blog), November 24, 2020. [Retrieved online.](#)

8 Financial Action Task Force, *Illicit Tobacco Trade*, 9.

9 Arndt Sinn, “The Link Between Illicit Tobacco Trade and Organised Crime” (University of Osnabrück, March 23, 2018), 2–3. [Retrieved online.](#)

10 John Barned-Smith and Gabrielle Banks, “Inside the Lucrative Smuggling Operation That Sees Millions of Chinese Cigarettes Pass through Texas,” *Houston Chronicle*, June 29, 2021. [Retrieved online.](#)

11 “Tobacco Growing Industry in China - Market Research Report,” *IBIS World*, March 29, 2022. [Retrieved online.](#)

12 OCCRP, “What Is China Tobacco?,” *Organized Crime and Corruption Reporting Project*, June 22, 2021. [Retrieved online.](#)

13 Alessia Cerantola and Andrei Ciurcanu, “China’s State Tobacco Company Is Massive at Home. Now It’s Ready to Take Over the World,” *Organized Crime and Corruption Reporting Project*, June 22, 2021. [Retrieved online.](#)

14 Cerantola and Ciurcanu.

with an agency responsible for setting and enforcing standards.¹⁵ This certainly influences broader policy in the domestic market as well as the government's commitment to the World Health Organization's Framework Convention on Tobacco Control (FCTC).

The CNTC has allegedly supplied global markets with illicit whites in order to enter new markets and attract new consumers.¹⁶ Illicit whites from the CNTC have turned up across the globe, including in conflict zones like Libya, Syria, and Iraq, as well as areas known for illicit trade.¹⁷ For example, they have been detected by law enforcement in the Panama Canal, where they are pushed into Latin America and, in some cases, further north to the United States.¹⁸

In 2016, Italy's Guardia di Finanza seized 17 tons of illicit cigarettes that were linked to a network of Italian and Moldovan smugglers who were working with a "high-ranking executive at China Tobacco International Europe Company (CTIEC)," CNTC's Romanian subsidiary.¹⁹ The case served as "the first public evidence that China Tobacco officials have engaged in cigarette smuggling, and links their operation to criminal groups active in Europe."²⁰ The cigarettes, produced by CTIEC in Romania, were, on paper, to be transiting Italy on the way to Libya, and therefore not subject to excise tax, however, the cigarettes were removed in Italy and the shipping container was filled with 17 tons of junk, all in order to bring the Chinese cigarettes illegally into Europe without paying taxes.²¹

There has not been considerable research into the dynamics of counterfeit tobacco production and trade in China, however given the immense size of China's counterfeit industry, it is unsurprising that tobacco products would number among those goods. Counterfeit cigarettes—knockoffs of popular brands like Marlboro and Newports—have flooded markets around the globe. According to a 2009 report, 99 percent of counterfeits in the U.S. come from China.²² A 2010 memo from the EC reported China as the primary source of counterfeit cigarettes in the EU.²³

Within China, a study by Shen et al. indicates that counterfeiters have filled the niche created

15 Cerantola and Ciurcanu.

16 "Collaborations with China National Tobacco Corporation Belie PMI & BAT's Smoke-Free Agendas," Southeast Asia Tobacco Control Alliance, July 29, 2021. [Retrieved online.](#)

17 Cerantola and Ciurcanu, "China's State Tobacco Company Is Massive at Home. Now It's Ready to Take Over the World."

18 Barned-Smith and Banks, "Inside the Lucrative Smuggling Operation."

19 Andrei Ciurcanu and Alessia Cerantola, "A Fake Shipping Container Leads to Chinese Cigarettes — and Italy's Camorra Crime Group," Organized Crime and Corruption Reporting Project, June 22, 2021. [Retrieved online.](#)

20 Ciurcanu and Cerantola.

21 Ciurcanu and Cerantola.

22 Te-Ping Chen, "China's Marlboro Country," Slate, June 29, 2009. [Retrieved online.](#)

23 "Contraband and counterfeit cigarettes: frequently asked questions," European Commission, July 15, 2010. [Retrieved online.](#)

by “the reluctance of licensed cigarette sellers to trade in cheap legal cigarettes due to the small profit margin and the subsequent reduction or even cessation of production of cheap cigarettes by local authorized factories, despite the demand for cheap cigarettes.”²⁴

Besides expanded distribution, the CNTC has also begun producing tobacco products in other countries. Africa’s biggest tobacco producer is the Tian Ze Tobacco Company (TZTC) in Zimbabwe, which was established in 2005. The CNTC subsidiary “engages in a host of projects from reforestation to funding orphanages and schools;” however, these projects are “flagrant violations of the FCTC” since “all Parties to the treaty must institute a comprehensive ban on tobacco advertising, promotion and sponsorship.”²⁵

In addition, the TZTC has created an environment within Zimbabwe that has placed rural farmers into contractual agreements with buying companies like the TZTC, but these agreements do not create an ideal situation for local farmers.²⁶ Local farmers have reported that they are stuck within a cycle of debt, with the TZTC creating agreements that have farmers shoulder debts that are unlikely to be paid off given their revenue.²⁷ The CNTC’s continued expansion into other markets, like in the case of Zimbabwe, creates increased dependency on tobacco as a crop and on China as an export destination.²⁸ It also creates a toxic cycle of debt that places rural farmers in a position where they cannot profit from their business, keeping them in poverty.

The lack of transparency about CNTC’s operations, which is unsurprising given Beijing’s opaque nature, makes it difficult to ascertain the actual extent of the company’s domestic and global footprints in terms of production and distribution.²⁹ With the CNTC’s status as an SOE, and its relation to STMA being so closely related, questions have been raised about Beijing’s knowledge of and/or complicity in the illicit trade, primarily the trade of illicit whites. The CNTC’s operations linked to debt-trap operations and smuggling networks signals that the SOE may have broader knowledge of these illicit flows.

24 Anqi Shen, Georgios A. Antonopoulos, and Klaus Von Lampe, “The Dragon Breathes Smoke: Cigarette Counterfeiting in the People’s Republic of China,” *British Journal of Criminology* 50, no. 2 (November 2010): 253.

25 Cerantola and Ciurcanu, “China’s State Tobacco Company Is Massive at Home. Now It’s Ready to Take Over the World”; “Banning Advertising, Sponsorship and Promotion,” World Health Organization, accessed April 11, 2022. [Retrieved online.](#)

26 Jennifer Fang et al., “All Weather Friends: How China Transformed Zimbabwe’s Tobacco Sector,” *International Journal of Environmental Research and Public Health* 17, no. 3 (February 2020): 5. [Retrieved online.](#)

27 Dumisani Muleya, Owen Garare, and Nhau Mangirazi, “Contract Tobacco Farmers in Zimbabwe Say They Are ‘Drowning in Debt,’” Organized Crime and Corruption Reporting Project, September 8, 2021. [Retrieved online.](#)

28 Fang et al., “All Weather Friends,” 8.

29 OCCRP, “What Is China Tobacco?”

Wildlife Trafficking

Just as China dominates the world as the source country for counterfeits, it also commands the title of the largest destination country for the illegal wildlife trade. And just like the other transnational crimes discussed in this report, the pervasiveness of wildlife trafficking in China comes down to government regulation, enforcement and political will, or lack thereof.

Although there is not a universally accepted definition of “wildlife trafficking” (also known as “the illegal wildlife trade” or “wildlife crime”), the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES) defines the term as the “taking, trading (supplying, selling or trafficking), importing, exporting, processing, possessing, obtaining and consumption of wild fauna and flora, including timber and other forest products, in contravention of national or international law.”¹⁹¹ It can involve the trade of live animals (such as great apes, reptiles, or birds), animal parts (such as ivory or rhino horn) or animal products (such as tiger bone wine). There are both legal and illegal trades in wildlife. The legal trade is regulated by CITES, which is an international agreement to ensure that the trade in wildlife does not threaten species survival.¹⁹² There is no international agreement against wildlife trafficking, which has hampered global efforts to collectively and effectively fight wildlife crime, however the Global Initiative to End Wildlife Crime has called for a new protocol on wildlife trafficking to be added to the UN Convention Against Transnational Organized Crime.¹⁹³

Like all transnational crime, there is no firm value of wildlife trafficking, however estimates put the global illegal trade at up to US\$23 billion a year.¹⁹⁴ This would put the size of the illegal wildlife trade at roughly one-fifth the value of the global legal trade of wildlife, which one estimate put at US\$119 billion in 2020.¹⁹⁵ A 2017 Chinese Academy of Engineering report estimated the domestic value of the country’s legal wildlife trade at US\$74 billion, which means that China is responsible for more than 62 percent of the global market.¹⁹⁶ This makes China the biggest player in both the legal and illegal wildlife trades.

International Wildlife Trafficking

Not only is Chinese demand responsible for the largest share of the global illegal wildlife trade, its citizens have also played a large part in sourcing and consuming wildlife abroad, including being at the front of wildlife trafficking networks in Africa. *The Diplomat* notes that “...with the growing soft

191 “Wildlife Crime,” CITES, accessed February 1, 2022. [Retrieved online.](#)

192 “What Is CITES?,” CITES, accessed February 1, 2022. [Retrieved online.](#)

193 Per the Global Initiative to End Wildlife Crime, the protocol “would represent a major step forward in the fight against these serious crimes by embedding them into the international criminal law framework... [and] signify an unequivocal recognition by States Parties of the devastating scale, nature and consequences of such crimes, of the need to scale up collaborative efforts to prevent and criminalize them, and provide States with the means to do so. See “UNTOC Wildlife Protocol,” Global Initiative to End Wildlife Crime, accessed February 1, 2022. [Available online.](#)

194 Channing May, *Transnational Crime and the Developing World* (Washington, D.C.: Global Financial Integrity, 2017), 53. [Retrieved online.](#)

195 Jia Hao Tow, William S. Symes, and Luis Roman Carrasco, “Economic Value of Illegal Wildlife Trade Entering the USA,” *PLOS ONE* 16, no. 10 (October 12, 2021): e0258523. [Retrieved online.](#)

196 Michael Standaert, “Illegal Wildlife Trade Goes Online as China Shuts down Markets,” *Al Jazeera*, March 24, 2020. [Retrieved online.](#)

power of China in Africa, more and more Chinese nationals have started to move there and live in countries where heavy Chinese industry operates. As the ivory craze took hold, some of these Chinese discovered they could operate lucrative side operations without arousing too much suspicion from the local governments.”¹⁹⁷

For example, 69-year old Chinese national Yang Feng Glan, the so-called “Ivory Queen,” ran legitimate businesses in Tanzania but was also responsible for running one of the largest ivory trafficking rings in Africa. In 2019, she was convicted of smuggling nearly two tons of ivory worth US\$5.6 million from Africa to China over a 14-year period, with prosecutors alleging that she “did intentionally organize, manage and finance a criminal racket by collecting, transporting or exporting and selling government trophies.”¹⁹⁸

Tanzania’s elephants were hit hard by poaching from 2009 to 2014, with the population plunging by 60 percent, which was during the period that Yang was operating. *The Times* reports that the Tanzanian government “had been heavily criticised for failing to stop the illegal flow of ivory and rhino horn and was accused of turning a blind eye to cartels linked to the country’s large and influential Chinese community.”¹⁹⁹

In an example of “high-level” trafficking, Chinese officials allegedly purchased “large amounts of illegal ivory” during a state visit by President Xi to Tanzania in 2013, using diplomatic bags to smuggle the ivory out via Xi’s plane.²⁰⁰ The Environmental Investigation Agency (EIA) reports that this method was also allegedly used by North Korean embassy officials as one avenue of trafficking rhino horns to China from Africa—specifically Zambia and Zimbabwe—as they would smuggle the horns out of the country “in diplomatic bags [which] eventually transited to Guanzhong in China and sold on to the Chinese market.”²⁰¹

While China’s footprint in Latin America is relatively smaller compared to that in Africa, the country has still had a large impact on wildlife trafficking in the region. Marine species like sea cucumbers as well as parts like totoaba swim bladders and shark fins have been poached in highly unsustainable numbers, with the majority of the goods destined for Chinese markets to be used in traditional Chinese medicine (TCM) or as a delicacy.²⁰²

More recently, Latin America’s big cats have come into the crosshairs. A study by Morcatty et al. in *Conservation Biology* found a strong correlation between the jaguar trade and “the recent influx of Chinese people encouraged especially by new investments” in the region, and that “the influx of illegal jaguar products is likely a side effect of the economic partnership between southern American countries and China and the high corruption rates in the supply-side chain.”²⁰³ A similar relationship

197 Kevin T. Bielicki, “China’s Ivory Ban: A Work in Progress,” *The Diplomat*, March 15, 2019. [Retrieved online.](#)

198 “Tanzanian Court Sentences Chinese ‘Ivory Queen’ to 15 Years for Smuggling,” VOA, February 19, 2019. [Retrieved online.](#)

199 Jane Flanagan, “Yang Feng Glan: Chinese ‘Ivory Queen’ Jailed after Selling Two Tonnes of Elephant Tusks,” *The Times (London)*, February 19, 2019, sec. world. [Retrieved online.](#)

200 Fumbuka Ng’wanakilala, “Tanzania Probes Alleged Ivory Smuggling during Chinese State Visit,” Reuters, November 6, 2014. [Retrieved online.](#)

201 Evie Kirschke-Schwartz, “Wild Laws: China and Its Role in Illicit Wildlife Trade,” Wilson Center, June 2, 2016. [Retrieved online.](#)

202 Michael Lohmuller, “How China Fuels Wildlife Trafficking in Latin America,” *InSight Crime*, June 10, 2015. [Retrieved online.](#)

203 Thais Q. Morcatty et al., “Illegal Trade in Wild Cats and Its Link to Chinese-Led Development in Central and South America,” *Conservation Biology* 34, no. 6 (2020): 1533. [Retrieved online.](#)

was reported two years earlier by *Mongabay*, which reported that residents described how “an influx of Chinese companies to build roads and bridges in Bolivia is contributing to increased trafficking of jaguar parts.”²⁰⁴

Along China’s southeastern border lies Laos, identified by CITES as a place where “everyone can buy everything and cross the border.”²⁰⁵ In order to obtain tiger bone products, the *Washington Post* explains that “some Chinese customers flock to border towns sprinkled throughout the Golden Triangle area, where the countries of Myanmar, Laos and Thailand converge, and where weaker rule of law and government corruption abet black market wildlife trade.”²⁰⁶ A notable example of blatant wildlife trafficking is the Golden Triangle Special Economic Zone (GTSEZ), a free trade zone in northwest Laos which is run by Chinese businessman Zhao Wei, chairman of the Kings Romans Group, since 2007 when he received a 99-year lease from the Laotian government. The GTSEZ “exists under the de facto sovereignty of Zhao,” operates as “an extension of China,” and serves as an enclave of activities ranging from gambling to prostitution, drug trafficking, and “a bustling trade in endangered species’ parts” catering to Chinese tourists.²⁰⁷

Domestic Wildlife Trafficking

Illicit wildlife in China are most frequently destined for zoos or safari parks, whereas wildlife products are incorporated into traditional medicine, consumed as delicacies, used as status symbols, or accumulated as an asset. Per the Deputy Director of the Research Institute of Resources and Environment Policies at the Development Research Center (DRC) of the State Council, the main reasons for China’s illegal wildlife trade are “a lack of viable substitutes for raw materials used in traditional Chinese medicines (e.g., bear bile, bear bile powder, pangolin, and other products); a preference in traditional food culture for delicacies made from wildlife; and of the private consumption by some rich and corrupt government officials of tiger’s meat, bear’s paw, pangolin and other wild animal products—bear’s paw and pangolin being the most popular.”²⁰⁸

The use of wildlife parts in TCM is a stimulus for both the illegal and legal wildlife trades that is unique to China. The Chinese Academy of Engineering estimated that the farming of wildlife in China for the TCM industry is worth US\$7 billion annually, however, as *The Guardian* points out, “that figure does not take into account the illegal trade... That number is likely to be many times higher, judging by seizures of animal parts such as pangolin scales, rhino horn and tiger bone.”

TCM is a legitimate system of medicine, a major industry in China, and an integral part of Chinese culture for millennia. Understandably, Beijing has “forcibly backed the industry” for a long time in

204 Roberto Navia, “Fang Trafficking to China Is Putting Bolivia’s Jaguars in Jeopardy,” *Mongabay*, January 26, 2018. [Retrieved online.](#)

205 Terrence McCoy, “The Man Risking His Life to Expose the Destruction of the Tiger,” *Washington Post*, May 9, 2019. [Retrieved online.](#)

206 McCoy.

207 Sebastian Strangio, “Chinese Casino Magnate’s Empire Set to Expand in Laos,” *The Diplomat*, April 8, 2021. [Retrieved online.](#); Flavia Olivieri, “Laos, the Ups and Downs of the Illegal Wildlife Trade in a Chinese-Controlled Special Economic Zone,” *LifeGate*, January 8, 2020. [Retrieved online.](#); Jeremy Hance, “High-End Laos Resort Serves up Illegal Wildlife for Chinese Tourists,” *The Guardian*, March 19, 2015. [Retrieved online.](#)

208 Jiwen Chang, “China’s Legal Response to Trafficking in Wild Animals: The Relationship between International Treaties and Chinese Law,” in *Studies in Global Animal Law*, ed. A. Peters (Berlin: Springer, 2020), 71–72. [Retrieved online.](#)

order to protect it and promote its development.²⁰⁹ The major controversy with TCM and the legal/illegal wildlife trade stems from the use of 70 wild species in different medical treatments.²¹⁰ This can be linked to the fact that some of these wild species are poached/trafficked in order to meet demand.²¹¹ For example, ADM Capital Foundation reported in 2019 that the “[TCM] industry [accounted] for more than three-quarters of the trade in endangered wildlife products in Hong Kong over the past 5 years.”²¹² Equally as important is the fact that there are alternative ingredients—plants and minerals—that can be used in the place of animal parts, however there are still consumers who perceive the animal parts as being more potent, and an industry that is willing to supply them.²¹³

Besides TCM, the consumption of wildlife as food is another driver of the illegal wildlife trade. In China, wildlife is often sold in “wet markets,” marketplaces that sell perishable goods like fresh meat, fish, and produce in a “non-supermarket setting.”²¹⁴ It is important to note that wet markets are commonplace throughout the world, and are not at all inherently illicit or dangerous.

Those markets that do sell wildlife, however, present a greater risk from a health and safety standpoint. As *National Geographic* explains, “buying, selling, and slaughtering wild animals for food is one way an animal-borne disease may infect people... Other forms of wildlife trade can be risky too, including the exotic pet industry and tapping animals or their parts for traditional medicine or ornamental uses, such as rugs or carvings. Animals used for those purposes may harbor viruses that can sicken preparers and customers.”²¹⁵ Disease outbreaks connected to wild animals are not difficult to anticipate; Ebola and HIV are two examples of diseases that originated from close human contact with wildlife.

At the center of the COVID-19 outbreak was the Huanan Seafood Market in Wuhan, which *National Geographic* reports had “a wild animal section where live and slaughtered species were for sale: snakes, beavers, porcupines, and baby crocodiles, among other animals.”²¹⁶ A broader study of Wuhan’s wet markets between May 2017 and November 2019 found more than 47,000 different animals from 38 terrestrial wild animal species were sold by vendors; the most commonly sold species was the Amur hedgehog, while the wild boar was the most expensive. As the authors point out, although 13 of the 17 stores did have the required permits, “none of the 17 shops posted an origin certificate or quarantine certificate, so all wildlife trade was fundamentally illegal.”²¹⁷

209 Owen Dyer, “Beijing Proposes Law to Ban Criticism of Traditional Chinese Medicine,” *BMJ* 369 (June 9, 2020): m2285. [Retrieved online.](#)

210 The Pharmacopoeia of the People’s Republic of China lists 70 wild species, whereas the Medical Fauna of China lists 2,275 animal species. See Tom P. Moorhouse et al., “Beyond the Pharmacopoeia: To What Extent Is Trade for ‘TCM’ Limited to Official TCM Taxa?,” *Global Ecology and Conservation* 32 (2021): e01906.

211 “EIA: China’s Tiger Farms Are a Threat to the Species,” *China Dialogue* (blog), June 15, 2017. [Retrieved online.](#)

212 Farah Master, “As China Pushes Traditional Medicine Globally, Illegal Wildlife Trade Flourishes,” Reuters, March 28, 2019. [Retrieved online.](#)

213 Michael Standaert, “‘This Makes Chinese Medicine Look Bad’: TCM Supporters Condemn Illegal Wildlife Trade,” *The Guardian*, May 26, 2020. [Retrieved online.](#)

214 B. Rose Huber, “A Better Understanding of ‘wet Markets’ Is Key to Safeguarding Human Health and Biodiversity,” Princeton University, June 11, 2021. [Retrieved online.](#)

215 Dina Fine Maron, “‘Wet Markets’ Likely Launched the Coronavirus. Here’s What You Need to Know,” *National Geographic*, April 15, 2020. [Retrieved online.](#)

216 It is important to note, however, that it would be more accurate to describe the Huanan market as a hybrid, that being “a wet market, a live-animal market, and a wildlife market all in one.” Huber, “A Better Understanding of ‘wet Markets’ Is Key”; Fine Maron, “‘Wet Markets’ Launched the Coronavirus.”

217 Xiao Xiao et al., “Animal Sales from Wuhan Wet Markets Immediately Prior to the COVID-19 Pandemic,” *Scientific Reports* 11, no.

The illegal wildlife trade in China is supplied in three main ways: wildlife, their parts, and products are either “sourced” abroad and trafficked into the country; they are legally farmed/produced domestically; and, to a lesser extent, they are poached domestically. Illegal wildlife products are trafficked into China via air, sea, and land, smuggled by individuals or inside legitimate trade shipments. The products move via circuitous routes, with some being amassed in key locations prior to being trafficked to China. For example, both pangolin scales and ivory are harvested throughout Africa before being transported to Nigeria, where they are consolidated into larger shipments; the country has turned into a major global transit hub for wildlife trafficking.²¹⁸

Wildlife Farming

The commercial breeding and sales of wildlife is not unique to China. As mentioned above, the global legal wildlife trade is estimated to be worth more than US\$100 billion annually, and an international convention (CITES) was established to regulate the legal trade. What is singular about China is the size of the industry, the involvement of the government, the species that are farmed, and the function of the farming, notably farming for consumption and TCM. Although the dynamics of the wildlife industry—particularly its size—have been murky, the government’s reporting of its response to COVID-19 has shed some light, with *The Guardian* writing that Beijing shuttered “nearly 20,000 wildlife farms raising species including peacocks, civet cats, porcupines, ostriches, wild geese and boar” connected to meat production.²¹⁹

The farming of tigers has been one of the most hotly contested components of China’s wildlife trade. The Chinese government helped to establish the tiger farming industry in the 1980s, possibly through the misplaced belief that captive-bred tigers could meet the demand for tiger products, relieving the pressure on wild tiger populations. As *China Dialogue* explains, in 1986, eight tigers that had been born in American zoos were sent to China, obtained by the Chinese Ministry of Forestry, with the ostensible purpose of establishing “a new captive breeding programme, to benefit the conservation of the species,” yet the tigers ended up at a fur farm that became the Hengdaohezi Breeding Centre, which was “founded as a government-funded operation to breed tigers for profit and supply bones for medicinal use.”²²⁰

According to transnational crime expert Vanda Felbab-Brown, however, the opposite happened: demand intensified, leading to increased poaching of wild tigers.²²¹ In response, Beijing banned the trade in tiger parts (along with rhino horn) in 1993, although the trade in tiger skins was still allowed. An investigation by the EIA, however, found that a particular government notification—Notification 2005 No. 139—seems to permit the use of captive-bred tiger bone in medicinal products, stating that the notification would “enable the use of captive-bred tiger bone in medicine and the gradual reduction of use of leopard bones.”²²²

1 (June 7, 2021): 11898. [Retrieved online.](#)

218 United Nations Office on Drugs and Crime, *World Wildlife Crime Report: Trafficking in Protected Species* (New York: United Nations Office on Drugs and Crime, 2016), 14–15. [Retrieved online.](#)

219 Michael Standaert, “Coronavirus Closures Reveal Vast Scale of China’s Secretive Wildlife Farm Industry,” *The Guardian*, February 25, 2020. [Retrieved online.](#)

220 “EIA. China’s Tiger Farms Are a Threat to the Species.”

221 McCoy, “The Man Risking His Life.”

222 “Briefing on the Manufacture of Tiger Bone Wine in China” (Environmental Investigation Agency, 2013), 2. [Retrieved online.](#)

Wildlife expert Judith Mills reports that tiger farms in China, which in 2007 were estimated to house more than 5,000 tigers, “are basically feedlots where tigers are bred like cattle to make luxury products, including tiger bone wine and tiger skin rugs.”²²³ Tiger farm owners have continued to breed the animals in captivity in the hope that Beijing would lift the ban, “lobbying the government to reopen trade in tigers complaining that the upkeep of so many tigers is a financial burden.”²²⁴ This has been detailed by TRAFFIC as well, which reported that “investors in massive, captive tiger breeding centers in China have been pressuring the Chinese government to lift its successful 14-year-old ban on trade in tiger parts so they can legally sell products like tiger bone wine and tiger meat. These facilities have acknowledged stockpiling tiger carcasses in the hopes that the trade ban will be lifted.”²²⁵

Chinese Policy Response to Wildlife Trafficking

Over the last 30 years, China’s protection of wildlife as well as regulation of the wildlife trade has become stricter as a whole, however weaknesses still remain in China’s response. While the farming of wildlife for consumption has been banned, wildlife farming still exists, which continues to contribute to wildlife trafficking. In addition, the decentralized implementation of legislation leaves vulnerabilities in the management of wildlife and their habitats and creates potential loopholes.

Wildlife trafficking is addressed in both the Wildlife Protection Law (WPL) and China’s Criminal Law. The National Forestry and Grassland Administration (NFGA) is the primary government agency responsible for *wild* populations of wildlife, however the Ministry of Agriculture is responsible for *farmed* populations, which could lead to challenges in terms of information sharing and policy coherence. *China Dialogue* reports that “effective oversight and coordination are still problematic” between the two agencies.²²⁶

Article 1 of the WPL establishes the intent of the law, which is “protecting wild animals, saving species of wildlife which are rare or near extinction, maintaining biodiversity and ecological balance, and promoting the establishment of ecological civilization,” which would suggest that the country’s priority is wildlife protection.²²⁷ However, this intention seems somewhat at odds with Article 3, which establishes that wildlife resources are owned by the state, which is also responsible for safeguarding “the lawful rights and interests of organisations and individuals engaged in the protection of wildlife and related activities, including scientific research and captive breeding.”²²⁸ The fact that the WPL enshrines the right for individuals and entities to engage in captive wildlife breeding sets the stage for a conflict of interests.

Similar to the CITES’ Appendices, China has a two-tier system for classifying protected wildlife (Article 10), with the most endangered/threatened species in the first tier. One of the gaps that remains in China’s legislation on wildlife trafficking is that its two-tier list is not harmonized with the CITES Appendices; one of the most notable divergences involves black bears, which are afforded the high-

223 Kirschke-Schwartz, “Wild Laws”; McCoy, “The Man Risking His Life.”

224 “The World Votes to End China’s Tiger Trade,” Wildlife Trust of India, accessed January 26, 2022. [Retrieved online.](#)

225 “CITES: Breeding Tigers for Trade Soundly Rejected,” TRAFFIC, June 13, 2007. [Retrieved online.](#)

226 Gao Baiyu, “China’s List of Protected Animals to Be Updated after 32 Years,” *China Dialogue* (blog), October 1, 2020. [Retrieved online.](#)

227 People’s Republic of China, “Wildlife Protection Law” (2016). [Retrieved online.](#)

228 People’s Republic of China.

est protection (Appendix I) under CITES but are on the second-tier of China's list, giving them less protection than other endangered species like elephants. The List of Wildlife under Special State Protection has only been updated three times since 1988, with the musk deer being moved from Class II to Class I in 2003, and the same for the pangolin in 2020.²²⁹ In 2021, the government greatly expanded the list, "with the number of protected species increasing from ≈500 to ≈1500, covering over 20% more threatened species."²³⁰

Permits to buy, sell, or utilize protected wild animal species and products are issued by the NFGA. These activities are authorized under Article 27 of the WPL, which allows the domestic trade of "wildlife under special state protection or the products thereof [when] necessary for scientific research, captive breeding, public exhibition or performances, heritage conservation or other special purposes."²³¹ However, the EIA explains that the "heritage conservation" exemption in Article 27 "appears to be being used to sanction commercial trade in protected wildlife, including leopards, for the production of traditional medicines and tonics."²³²

One of the biggest points of contention regarding Chinese wildlife regulation involves commercial captive wildlife breeding. While some might argue that the captive breeding of certain species will take the pressure off their wild counterparts, or prevent the need to poach these species at all, several challenges still remain. First, some consumers prefer wild versus farm-raised animals (or their products) as they perceive them to be of a better quality. They therefore may be willing to pay more for "wild caught" parts/products, which raises the incentive to engage in poaching. Second, related to this, is the fact that it is likely less work and expense to poach than to operate a breeding farm, providing another incentive.

Third, by allowing a legal trade of captive-bred animals/parts/products, the government "legitimizes" consumers' demand, potentially stimulating it. Finally, whenever there is a demand for a particular product or species and it is illegal to poach and/or traffic wild animals but there exists a legal alternative, an opportunity is created for illegally-obtained items to be laundered through the legal trade. For example, GFI's 2018 report *Illicit Financial Flows and the Illegal Trade in Great Apes* outlines how, because CITES allows a legal trade in captive-bred chimpanzees in certain circumstances, traffickers will poach wild chimpanzees in West and Central Africa and export them with falsified documentation (i.e. CITES permit) declaring they are captive-bred.²³³

While Beijing may feel that its legislation/regulations on the captive breeding of wildlife, such as tiger farming, only have domestic implications, the impacts actually extend much further. EIA points out that since China is "the primary consumer market for tiger products, China's official policies relating to tiger trade and the impact they have on demand are of critical importance for all wild tigers."²³⁴

229 Baiyu, "China's List of Protected Animals to Be Updated after 32 Years."

230 Guangping Huang et al., "Wildlife Conservation and Management in China: Achievements, Challenges and Perspectives," *National Science Review* 8, no. 7 (July 1, 2021): 1. [Retrieved online.](#)

231 People's Republic of China, Wildlife Protection Law.

232 Environmental Investigation Agency, *A Bitter Pill to Swallow: China's Flagrant Trade in Leopard Bone Products* (London: Environmental Investigation Agency, 2020), 9. [Retrieved online.](#)

233 Christine Clough and Channing May, *Illicit Financial Flows and the Illegal Trade in Great Apes* (Washington, D.C.: Global Financial Integrity, 2018), 10–12. [Retrieved online.](#)

234 "China's Wildlife Protection Law," Environmental Investigation Agency, accessed January 20, 2022. [Retrieved online.](#)

Another gap exists in the disparity of protection between actual wild animals and captive-bred wildlife. As noted above, certain species are given greater protection under the WPL when they are placed on its protection list. According to Article 28, when there exists both “established knowledge and techniques for captive breeding” of a particular species on the protection list, and a stable wild population of that species, then the captive-bred animals “are no longer listed as wildlife under special state protection and are subject to different protection measures from wild populations.”²³⁵ As Deputy Director Chang points out, in the context of black bears, this means that “illegally purchasing or trafficking artificially bred black bears will not constitute the illegal acquisition or trafficking of precious and endangered wildlife.... [which] may diverge from the intent of CITES [in that] CITES provides that reared tigers, bears, and other animals continue to be included in the national specially protected wildlife list.”²³⁶

China’s National Biodiversity Conservation Strategy and Action Plan (2011-2030) (“Action Plan”) states that its long-term goal is to effectively protect biodiversity *in China* by 2030, which includes a “complete policy and legal system on biodiversity conservation and a sound mechanism of sustainable use of biological resources has been established.”²³⁷ However, in order to achieve this, China will need to modify the WPL to prohibit the trade in wild animals and their parts and products, regardless of whether they are endangered/threatened in China or in another jurisdiction; as it stands now, China’s legal wildlife trade has an *unsustainable* impact on biological resources around the world.

China is not singular in focusing its environmental conservation and management plans internally, on its own land, waters, and sky as well as their wild inhabitants. However, it seems to selectively ignore its impact—in particular its legislation/regulations and citizens—on the global environment. According to the Convention on Biological Diversity, to which China is party, while States have “the sovereign right to exploit their own resources pursuant to their own environmental policies,” they also have “the responsibility to ensure that activities within their jurisdiction or control do not cause damage to the environment of other States or of areas beyond the limits of national jurisdiction.”²³⁸

As part of the 2020 UN Summit on Biodiversity, the China released a position paper titled “Building a Shared Future for All Life on Earth: China in Action,” which highlights the country’s “experience, progress, position and propositions on biodiversity conservation.”²³⁹ In the paper, China writes that its government “has been advocating and working to advance ecological civilization, which draws upon the ancient Chinese notion of “unity of nature and man” and “follow nature’s course”, and that this philosophy is “underpinned by eight principles that China upholds,” two of which are “man and nature should coexist in harmony” and “the strictest regulations and laws must be applied in protecting the environment.”²⁴⁰

235 People’s Republic of China, Wildlife Protection Law.

236 Chang, “China’s Legal Response to Trafficking in Wild Animals,” 76.

237 People’s Republic of China, “China National Biodiversity Conservation Strategy and Action Plan (2011-2030)” (Beijing: People’s Republic of China, 2010), 10–11.

238 United Nations, “The Convention on Biological Diversity” (1992). [Retrieved online.](#)

239 “China Releases Position Paper of the People’s Republic of China for the United Nations Summit on Biodiversity Building a Shared Future for All Life on Earth: China in Action,” Embassy of the People’s Republic of China in the Republic of Estonia, September 25, 2020. [Retrieved online.](#)

240 Ministry of Foreign Affairs and Ministry of Ecology and the Environment, “Building a Shared Future for All Life on Earth: China in Action” (Government of the People’s Republic of China, September 21, 2020). [Retrieved online.](#)

China frequently touts the importance of advancing ecological civilization in its messaging on the environment and biodiversity. “The concept of ecological civilisation (*shentai wenming*),” Berthold Kuh explains, “considers nature to be part of life, rather than something that can be exploited without restraint. It serves as a reference framework for the Chinese political leadership to develop visions of modern ecological socialism.”²⁴¹ This concept, particularly that nature should be exploited with restraint, seems at odds with some of China’s regulations, particularly those concerning wildlife farming.

China’s position paper, as well as its Action Plan, notes its continuing improvement in “ex-situ conservation,” pointing to the fact it has “built over 240 zoos (animal exhibition sites), in which 775 species of animals are being cared for, and 250 wild animal rescue and breeding centers.”²⁴² However, zoos, safari parks, animal rescue and breeding centers in China are largely more commercial operations rather than institutions primarily focused of conservation. In addition, some have been accused of acquiring animals in their collections via illegal means; others are allegedly connected to the trade in wildlife parts, such as tiger bones and pangolin scales.²⁴³ For all of the tiger breeding farms in China, no tiger has ever been successfully reintroduced into the wild in the country.²⁴⁴

Chinese Implementation and Enforcement Response to Wildlife Trafficking

Besides the legislative shortcomings with commercial wildlife farming, there are also deficiencies in the supervision of these operations. The EIA points out that, not only is the permitting system for the commercial use of protected wildlife opaque, but the government “has continued to issue permits to buy, sell or utilise protected wild animal species or the products thereof to companies previously implicated in commercial trade in tiger bone wine, tiger skins, leopard bone and elephant skin.”²⁴⁵

Another implementation challenge lies with the distribution of responsibilities among administrative divisions, which, in China, starts at the national level and then proceeds to the provincial, county, and township levels. The implementation of the WPL is executed at the provincial level, meaning that the relevant agency of each provincial-level government is responsible for establishing the regulations/measures for implementing the WPL, which can cause regulatory variances between jurisdictions.

Additionally, as the county-level governments are responsible for surveying the wildlife and their habitats (Article 11), it would be important that all of the data collected by each county is shared and pooled so that more-informed decisions on species protection could be made. However, it appears there is no mechanism for this, as Huang et al. explain:

Although several wildlife monitoring networks are in operation, monitoring gaps and overlaps are common in practice, and indicators, methods and guidelines for regulating

241 Berthold Kuhn, “Ecological Civilisation in China” (Berlin: Dialogue of Civilizations Research Institute, 2019), 1. [Retrieved online.](#)

242 Ministry of Foreign Affairs and Ministry of Ecology and the Environment, “Building a Shared Future.”

243 Michael Standaert, “Wuhan Facilities Shed Light on China’s Oversight on Wildlife Use,” Al Jazeera, August 27, 2021. [Retrieved online.](#)

244 Standaert.

245 “Behind Closed Doors: Lack of Transparency in Ongoing Permitted Use of Threatened Wild Animal Species in China” (Environmental Investigation Agency, October 2020), 1. [Retrieved online.](#)

these networks are inconsistent because of the lack of top-level design. Most importantly, monitoring data cannot be shared fully, integrated and analyzed to guide management decisions and policy.²⁴⁶

The status of China's List of Wildlife under Special State Protection is related to the efficacy of surveying wildlife, as a regularly updated list, *China Dialogue* notes, "would encourage ongoing surveys to track wildlife numbers – currently, there is a lack of data on the populations of the vast majority of China's wild animals, which in turn means the list lacks scientific grounding."²⁴⁷

Over time, China has amended its legislation to address loopholes, such as criminalizing the purchase of protected wildlife and wildlife products, as well as bringing it to meet international standards. The 2016 amendments to the WPL prohibited the production, sale, and purchase of wild animals (and their products) both under and not under state protection for food.²⁴⁸ China has also slowly made moves to address the ivory trade beginning circa 2012, culminating with the Notice by the General Office of State Council on the Orderly Cessation of Commercial Processing and Sale of Ivory and Ivory Products which ceased the domestic processing and sale of ivory and ivory products by the end of 2017. The ban has been relatively successful due to strong political support from the very top from President Xi.

While stepped up international coordination, law enforcement actions as well as legislative/regulatory changes do show improved protection of wildlife and the combat of wildlife trafficking, Beijing's actions still present a conflicted message regarding the country's commitment and the future of wildlife conservation.

SPOTLIGHT ON...

BEIJING'S RESPONSE TO COVID-19

The COVID-19 pandemic has been one of the most important catalysts for change. As Koh et al. explain, the pandemic, "at great human and economic costs, has mainstreamed the discourse of wildlife conservation for human well-being, clarified legislations on what species can be farmed, and provided a policy framework for systematic and enforceable wildlife management and conservation."¹ While the impetus behind policy changes was largely motivated out of public health concerns rather than wildlife conservation, it still does serve as a step forward in China's protection of wildlife.

In February 2020, the Standing Committee of the NPC passed the Decision to Comprehen-

¹ Lian Pin Koh, Yuhan Li, and Janice Ser Huay Lee, "The Value of China's Ban on Wildlife Trade and Consumption," *Nature Sustainability* 4, no. 1 (2021): 2–4. [Retrieved online.](#)

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246 Huang et al., "Wildlife Conservation and Management in China," 3.

247 Baiyu, "China's List of Protected Animals to Be Updated after 32 Years."

248 Chang, "China's Legal Response to Trafficking in Wild Animals," 74.

sively Prohibit the Illegal Trade of Wild Animals, Eliminate the Bad Habits of Wild Animal Consumption, and Protect the Health and Safety of the People (“Decision”) that “all terrestrial wild animals that naturally grow and reproduce in the wild are also prohibited from being hunted, traded or transported for the purpose of their consumption.”² Later, in September 2020, the NFGA issued guidance to farmers on the 64 wild animals that could no longer be bred/farmed for consumption purposes, which included civets, porcupines, and badgers as well as a variety of rodents, deer, fowl, amphibians, and reptiles; however, 19 of these species can still be farmed for medicinal display and scientific purposes.³

In October 2020, China introduced a proposed amendment to the WPL. The EIA points out that, while there are “some positive changes, such as consolidating [the February 2020 Decision], along with improvements to enforcement mechanisms and increased penalties,” the changes “did not go far enough, in that commercial breeding and trade – even in protected species such as tigers – is still permitted for non-food purposes such as traditional medicine or decorative items.”⁴

Following the Decision, the Standing Committee of the NPC launched “law enforcement inspections” in all provinces in order to evaluate the implementation of the Decision as well as better understand the efficacy of current legislation/regulation, enforcement, and supervision. The NPC does recognize that there are loopholes in both the supervision and enforcement of wildlife law/regulations. For example, it noted that besides insufficient law enforcement capacity, both in terms of staffing as well as technical expertise, there “are problems such as scattered and overlapping functions, poor work connection, and insufficient information sharing” between responsible agencies.⁵

Additionally, the Standing Committee noted that the WPL “needs to be revised and improved urgently.”⁶ As it stands, the WPL only prohibits the consumption of “precious, endangered” wildlife that has “important ecological, scientific and social value.”⁷ The Decision expanded the scope to include all terrestrial wildlife, however it still needs to be incorporated into the WPL.

² “Decision of the Standing Committee of the National People’s Congress on Comprehensively Prohibiting Illegal Wildlife Trade, Eliminating the Bad Habits of Indiscriminately Eating Wild Animals, and Effectively Protecting People’s Lives, Health and Safety,” National People’s Congress of the People’s Republic of China, February 24, 2020. [Retrieved online.](#)

³ “Circular of the State Forestry and Grassland Administration on Regulating the Scope of Classification and Management of Fasting Wild Animals,” Government of the People’s Republic of China, September 30, 2020. [Retrieved online.](#)

⁴ “China’s Wildlife Protection Law,” Environmental Investigation Agency, accessed January 20, 2022. [Retrieved online.](#)

⁵ “The Law Enforcement Inspection Team of the Standing Committee of the National People’s Congress Has Inspected the ‘Decision of the Standing Committee of the National People’s Congress on Comprehensively Prohibiting Illegal Wildlife Trade, Eliminating the Bad Habits of Eating Wild Animals, and Effectively Protecting People’s Lives, Health and Safety’ and the ‘People’s Republic of China Wildlife’ Report on the Implementation of the Protection Act,” National People’s Congress of the People’s Republic of China, August 10, 2020. [Retrieved online.](#)

⁶ “Law Enforcement Inspection Team.”

⁷ “Decision of the Standing Committee of the National People’s Congress on Comprehensively Prohibiting Illegal Wildlife Trade, Eliminating the Bad Habits of Indiscriminately Eating Wild Animals, and Effectively Protecting People’s Lives, Health and Safety.”

It will be important to see how China's near single-minded focus on economic development and growth will influence its wildlife policy in the future, particularly in a post-COVID world. For example, until early 2020, *The Guardian* reported that "wildlife farming was still being promoted by government agencies as an easy way for rural Chinese people to get rich." While Beijing banned wildlife farming for consumption in February 2020, the Global Initiative against Transnational Organized Crime has noted there have been several actions by the Chinese government post-COVID that promote the use of wild animals in TCM, in particular the use of bear bile in a recommended COVID-19 treatment as well as guidance from the NFGA "laying out options for dealing with wild animals which had been bred legally for trade as food, [which] includes suggestions that breeders should shift towards supplying traditional medicine if the species has 'medicinal value'."²⁴⁹

Beijing has been "persistent" in its efforts to promote TCM globally, which has been described as a "soft power push" that would also have important economic impacts, with the State Council estimating in 2019 that the industry would be worth US\$420 billion by the end of 2020.²⁵⁰ Research by the EIA found that "TCM is gaining ground in Africa, with an increasing number of African governments entering into official agreements with the Government of China to support TCM development," which, unfettered, could pose "a serious threat to biodiversity in Africa, all in the name of short-term profit" if endangered wildlife is used in TCM products.²⁵¹

Additionally, while consumption-related wildlife farming is still banned, the farming of wildlife for TCM is permitted, which still presents biosecurity risks. The farmed wildlife industry in China has serious implications in regards to virus transmission, with Peter Daszak, president of EcoHealth Alliance, stating that "the opportunities for these viruses to spill over across a very active wildlife–livestock–human interface is clear and obvious."²⁵² While the NPC acknowledges that "there is a lack of standardized management and evaluation" of these farms, with unsound regulations and supervision, until these issues are addressed wildlife farming will remain a major vulnerability for the country.

The Chinese government has the ability to police its domestic market, demonstrated by its success in protecting the giant panda as well as in curtailing the trade of ivory. This, like the other crimes covered in this report, shows that China's response to wildlife trafficking is largely dictated by will and not capacity. China must amend its wildlife legislation and regulations in order to close loopholes related to wildlife farming as well as the use of wildlife in TCM so that its action move towards its purported support of the "unity of nature and man."

249 Aron White, "China's Wildlife Trade Policy: What Has Changed since COVID-19?," Global Initiative against Transnational Organized Crime, May 27, 2020. [Retrieved online.](#)

250 Pratik Jakhar, "Covid-19: China Pushes Traditional Remedies amid Outbreak," BBC News, June 29, 2020. [Retrieved online.](#)

251 Environmental Investigation Agency, *Lethal Remedy: How the Promotion of Some Traditional Chinese Medicine in Africa Poses a Major Threat to Endangered Wildlife* (London: Environmental Investigation Agency, 2021), 4.

252 Smriti Mallapaty, "Animal Source of the Coronavirus Continues to Elude Scientists," *Nature*, May 18, 2020. [Retrieved online.](#)

Illicit Financial Flows

The methods used to launder illicit proceeds of Chinese origin, as well as the methods used by illicit Chinese actors, are both strongly linked to each other as well as Chinese culture and society. For example, there is a strong symbiotic relationship between trade-based money laundering (TBML), informal currency exchange, and illicit capital flight, as TBML schemes can serve as method for Chinese citizens to convert yuan to a foreign currency and illicitly move it out of the country. Some of these methods involve the abuse of legitimate sectors and industries, such as trade, real estate, and gaming, while others have licit origins and purposes, such as underground banking, a centuries-old type of informal value transfer system developed to facilitate international trade without the need to move vast sums of money.

The following are excerpts directly from the book *Money Laundering and Illicit Financial Flows: Following the Money and Value Trails* by John A. Cassara, published in 2020.²⁵³ Slight modifications have been made to reflect any changes that have occurred since the book was published, such as the passing of the U.S. Anti-Money Laundering Act in December 2020, as well as to provide updated statistics and sources, when possible. The views and opinions expressed in this section are those of Mr. Cassara and do not necessarily reflect the views or positions of GFI.

Trade-Based Financial Crime

Perhaps the most pervasive form of Chinese money laundering comes from “trade misinvoicing.” Most forms of trade misinvoicing revolve around invoice fraud and manipulation. Generally speaking, invoice fraud means the contents, description, and/or the value of goods has been misrepresented. Sometimes this is done to facilitate simple customs fraud, i.e. minimizing the payment of taxes and duties.

Customs fraud is the most prevalent predicate offense in TBML. Yet it is often overlooked because worldwide customs authorities generally do not have an investigative mandate. Invoice fraud is also sometimes part of value transfer or sending of trade goods instead of fund payment transfers from one country or jurisdiction to another. Often this facilitates capital flight. Value transfer is also commonly used in “counter-valuation” or as a means of settling accounts between informal value transfer brokers and traders. This is often accomplished via underground financial networks (see below).

For money launderers, transferring value via trade goods is particularly attractive because it generally does not trigger financial transparency reporting requirements. Trade-based value transfer is not closely examined by law enforcement and customs services.

The most common forms of trade misinvoicing are:

- Over- and under-invoicing
- Multiple invoicing
- Falsely described goods
- Misrepresentation of the quantity being shipped
- Misrepresentation of shipment origin to evade customs duties

²⁵³ While the text comes directly from Chapter 11 “China: The Biggest Money Laundering Threat” in Cassara’s book, some parts have been removed to consolidate the information, the order of the paragraphs has been changed and citations have been updated.

China and the U.S. are the world's two largest general merchandise traders (imports and exports). In 2020, China ranked first in worldwide exports with an export value of nearly \$2.6 trillion.²⁵⁴ China Inc. completely depends on trade. It is logical that trade is also manipulated and used in ways to facilitate illicit financial flows. This manifests itself in many different ways including underground financial systems and capital flight (see below). Perhaps the most common technique to move money (value) out of China is when companies import goods at overvalued prices or export goods at undervalued prices. To move money (value) into China, companies or fronts import goods at undervalued prices or export goods at overvalued prices.

Criminal organizations often use trade-based money laundering and trade fraud techniques to launder the proceeds of crime. The U.S. Department of Treasury has stated that the black market peso exchange (BMPE) is one of the largest money laundering methodologies in the Western Hemisphere and is responsible for laundering billions of dollars of drug proceeds every year.²⁵⁵ It is commonly used by both Colombian and Mexican drug cartels that purchase and sell Chinese products in order to launder funds.

In the BMPE, drug proceeds, acquired by black market dealers, are used to purchase trade items such as electronics, garments, and toys. Twenty years ago, most of the goods were purchased from U.S. companies. Drug money was used to buy tractors, refrigerators, cigarettes and other business and consumer goods. These products, in turn, were sent by the black market dealers to Colombia. American manufacturers involved in the trade were accused of "willful blindness." They did not ask questions about the source of the money being used to purchase their products even though the broker and routing were often suspect.

Over the last decade, the BMPE has evolved. Drug money is increasingly used to purchase Chinese-manufactured merchandise either directly from Chinese vendors or via US importers. Taking advantage of preferential trade policies, imported Chinese goods are sometimes fraudulently presented as made in the U.S. thus saving the conspirators from paying import taxes.²⁵⁶ This customs fraud is also a predicate offense for money laundering. Once again willful blindness comes into play. The manufacturers and middlemen involved are not practicing due diligence. This technique has still expanded further. Importing cheaply manufactured Chinese goods at overvalued prices gives reason to send criminally derived money directly out of Mexico and other drug-producing countries. In some places in the developing world, this trade-based money laundering technique sometimes avoids currency controls.

U.S. law enforcement has seen a spike of BMPE investigations involving Mexican drug cartels and Chinese-manufactured goods. This is a byproduct of burgeoning China/Mexico trade. For example, "when China and Mexico established diplomatic relations in 1972, trade between the two countries barely tipped the scales at \$13 million. By 2016, trade had exploded to almost \$75 billion."²⁵⁷

254 Updated from 2017 statistical data. M. Szmigiera, "Leading Export Countries Worldwide in 2020 (in Billion U.S. Dollars)," Statista, May 7, 2021. [Retrieved online.](#)

255 U.S. Department of the Treasury, *2007 National Money Laundering Strategy* (Washington, D.C.: U.S. Department of the Treasury, 2007), 7. [Retrieved online.](#)

256 Jamila Trindle, "Drugs, Cash, Luxury Goods, and Maternity Wear," *Foreign Policy*, October 13, 2014. [Retrieved online.](#)

257 Kaya Forest and Sierra Rayne, "The Sino-Mexican Influence in America's Backyard," *American Thinker* (blog), July 5, 2018. [Retrieved online.](#)

Europe has also been hard-hit with other versions of Chinese trade-based money laundering and black market exchanges. Italy, Poland, Spain and many other countries have seen a flood of cheap Chinese imports and counterfeit goods. Warehouses in industrial parks are found outside major European cities. They offer a vast range of consumer goods such as tools, paper products, electronics, and kitchen supplies. Importers declare only a fraction of each shipment (the volume of trade is so high customs officials are only able to physically inspect a very small percentage of shipping containers). The under-valued goods are sold and the proceeds are often laundered back to China. Proceeds rarely stay in the host country. The government loses tax revenue. Billions of euros have been laundered. VAT fraud is sometimes also involved.

There has been a major multi-billion-euro TBML investigation in Italy where Chinese authorities were found to have actively obstructed justice.²⁵⁸ In Spain, China's largest bank is accused of facilitating some of the laundering schemes run by "Chinese criminal organizations."²⁵⁹ Prosecutors say the sums of illicit proceeds are so large that the "damage to the socio-economic order and the national economy is clear."²⁶⁰

In addition, black market exchanges are common in the developing world. In Africa, Latin America, and parts of Asia, Chinese cheaply manufactured consumer merchandise (much of it counterfeit and/or smuggled) dominates both the legitimate and black markets. Generally speaking, there is an unfortunate lack of investigations and political interest in cracking down on this type of trade.

Underground Banking

According to the 2007 FATF mutual evaluation of China, there are four primary means of laundering money: 1) via banks; 2) via bulk cash; 3) "by importing or exporting over/under priced goods, or falsifying/counterfeiting import/export contracts, shipment bills, customs declarations and other related documents (i.e. trade-based money laundering)"; and 4) "through the underground banking system."²⁶¹ Points 3 and 4 are intertwined because invoice manipulation and trade fraud are commonly used in underground finance.

It is difficult to determine the magnitude of Chinese underground banking, but there is no doubt it has been used to move vast sums beyond China's borders. For example, Chinese authorities seized approximately \$130 billion "from underground banks operating on the mainland, half through a single illegal operation. Authorities seized another US\$148 billion in the first nine months of 2016."²⁶² In China, declared confiscated amounts are usually just the tip of an iceberg. According to some anti-corruption specialists, "Chinese underground banks are estimated to have over 10,000 clients and are believed to launder over \$100 billion every year."²⁶³

258 Mark Hanrahan, "China Obstructed Huge Money Laundering Investigation By Italy: Report," *International Business Times*, June 5, 2015. [Retrieved online.](#)

259 Angus Berwick and David Lague, "How China's Biggest Bank Became Ensnared in a Money Laundering Probe," Reuters, July 31, 2017. [Retrieved online.](#)

260 Berwick and Lague.

261 Financial Action Task Force, *First Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: People's Republic of China* (Paris: Financial Action Task Force, 2007), 8. [Retrieved online.](#)

262 Zhongxia Chen, "Chinese Banks Are Accused of Widespread Money Laundering. What Does This Mean for China?," *LSE Management* (blog), January 12, 2017. [Retrieved online.](#)

263 Elizabeth Gail, "Mexican Narcos Are Using Chinese Crypto Money Laundering Syndicates," CoinCentral, January 11, 2019. [Retrieved online.](#)

Chinese underground financial methods or alternative remittance systems are primarily used to remit wages from the Chinese diaspora back to the homeland. Of course, authorities have no wish to interfere with hard working immigrants sending money “back to the home country” to help support extended family. On the other hand, unfortunately, these low-cost and efficient financial systems are also abused by criminals to move, transfer, and launder illicit proceeds. They are attractive because by their very nature they are opaque. Underground financial systems avoid government scrutiny, taxes, and countermeasures such as the filing of financial intelligence.

As noted in the article “‘Flying money’ may land in U.S.”:

It is believed that *fei-chien*—sometimes known as “flying money”—was invented during the T’ang Dynasty (618 to 907 AD). At the time, there was a growing commodity trade within China. Some historians believe it was the rice trade and others the tea trade that were the catalysts for the new financial system. Ironically, as opposed to modern-day practice, the transfer schemes were not invented as an underground method of evading the grasp of authorities but rather as a tool to facilitate taxation.²⁶⁴

Strong Chinese family bonds are incorporated into *guanxi*, which is an overarching social system of rules that govern relationships and social behavior. *Guanxi* is the guarantor of both secrecy and the integrity of the parties to the transaction. Those who violate its prescriptions find themselves a social outcast, essentially shunned in all circles. *Guanxi* is an integral component of *fei-chien* or so-called “flying money.” In other words, similar to hawala and other indigenous informal value transfer systems, an essential element of *fei-chien* is trust. It is very difficult for law enforcement to penetrate the underground financial networks.

One of the most popular methods of getting yuan out of China involves finding a foreign contact who would like to set up a private exchange for Chinese RMB. “Flying money” networks are sometimes used but so are informal personal networks and business associates. For instance, the overseas person puts their dollars into an account in Hong Kong belonging to the Chinese individual. The Chinese individual in China puts the Chinese RMB in an account in Beijing that is connected with the overseas investor who wants the money in China.²⁶⁵ What is often overlooked is that trade continues to be involved with the settling of accounts. This little understood concept was identified in the FATF mutual evaluation quoted above. Most “flying money” brokers are directly involved or associated with trading companies. In our discussion of trade-based money laundering techniques above, invoice fraud and manipulation are employed particularly in over- and under-invoicing.

Another form of Chinese underground banking system (sometimes dubbed CUBS) is a loose-knit network of money dealers, traders and cryptocurrency brokers who move currencies in and out of the economy while sidestepping the country’s banking system, currency controls, and capital flight restrictions. According to the *2019 National Drug Assessment*, there is an alarming trend of Asian money laundering organizations acting on behalf of Mexican TCOs:

This trend is a result of the imposition of a cap by the Government of China on foreign exchange transactions (\$50,000/year) and overseas withdrawals on Chinese bank issued

264 John A. Cassara, “‘Flying Money’ May Land in U.S.,” *Banking Exchange*, February 21, 2016. [Retrieved online.](#)

265 Celia Hatton, “Report Reveals Offshore Dealings of China’s Elite,” *BBC News*, January 23, 2014. [Retrieved online.](#)

credit and debit cards (\$15,000/year). The demand of Chinese nationals to transfer their wealth outside of China and into the United States has fueled the demand for U.S. dollars. Asian MLOs are eager to acquire U.S. dollars (drug proceeds) from the Mexican TCOs in exchange for the payment of pesos in Mexico or their equivalent debts in China via a Chinese Underground Banking System (CUBS) scheme. Asian MLOs resell the U.S. dollars to customers (Chinese nationals within the United States) for a profit, normally in exchange for Renminbi (RMB) payments in China. This demand for foreign exchange, i.e. the U.S. dollar in particular, has provided an outlet for Mexican TCO drug proceeds that is changing the landscape of money laundering within the United States.²⁶⁶

There are indications that CUBS is being used in conjunction with the BMPE. Increasingly, the purchases, logistics, foreign exchange specialists, and trade intermediaries are Chinese and Chinese organized crime groups. They arrange for a drug dollar purchase of Chinese merchandise (much of it counterfeit) to be sent to South America including Colombia, Mexico, the Tri-Border Area, and the Colon Free Trade Zone.

Certainly, related to CUBS is the exponential growth of Chinese cryptocurrencies. For example, there are some reports that Mexican cartels are opting to collaborate with the Chinese partners due to their vast cryptocurrency money laundering networks.²⁶⁷ According to the DEA:

Many Chinese-based firms manufacturing goods used in TBML schemes now prefer to accept Bitcoin. Bitcoin is widely popular in China because it can be used anonymously to transfer value overseas, circumventing China's capital controls... CUBS money brokers sell Bitcoin to drug traffickers for cash earned from drug sales in the United States, Australia, and Europe. This drug cash is then sold to Chinese nationals in exchange for Bitcoin the Chinese nationals use to transfer the value of their assets outside of China.²⁶⁸

Real Estate

Investment in real estate is one of the most widely used international money laundering methodologies. For criminals and criminal organizations, large property purchases, sometimes paid for using cash and often with no beneficial ownership information, can facilitate the placement, layering, and integration stages of money laundering in a single operation. According to C4ADS, real estate “represented 30 percent of all criminal assets confiscated between 2011 and 2013.”²⁶⁹

Over the last five to ten years, Chinese citizens have gone on an international real estate buying spree. Overseas investment from China includes residential, commercial and industrial property. Preferred targets for residential real estate investment include the United States, the United Kingdom, Europe, Australia, New Zealand, Malaysia, Canada, and Dubai. According to the National As-

266 Drug Enforcement Administration, *2019 National Drug Threat Assessment* (Washington, D.C.: Drug Enforcement Administration, 2019), 103. [Retrieved online.](#)

267 Gail, “Mexican Narcos Are Using Chinese Crypto Money Laundering Syndicates.”

268 Drug Enforcement Administration, *2017 National Drug Threat Assessment* (Washington, D.C.: Drug Enforcement Administration, 2017), 130. [Retrieved online.](#)

269 C4ADS, *Sandcastles: Tracing Sanctions Evasion Through Dubai's Luxury Real Estate Market* (Washington, D.C.: C4ADS, 2018), 7. [Retrieved online.](#)

FLYING MONEY BROKERS

Flying money brokers essentially operate as informal money exchange businesses, often providing the service in conjunction with/behind legitimate front businesses such as corner shops, grocery stores, restaurants, and trade companies. They are the “human element” of Chinese underground banking, and earn a commission for each transaction they conduct.

The main operational difference between these brokers and those individuals and entities that operate formal exchange businesses is that they *transfer* money, or rather *value*, without *moving* money—physically or via the formal financial system. As explained in *Money Laundering and Illicit Financial Flows*: “A broker on one side of the transaction accepts money from a client who wishes to send funds to someone else. The first broker then communicates with the second broker at the desired destination, who distributes the funds to the intended recipient.”¹

Flying money brokers serve/operate within ethnic Chinese communities, due to both cultural ties as well as physical presence—a Chinese immigrant in the U.S. wouldn’t go to a Pakistani hawaladar to send money back to China. These brokers are preferred because the commissions they charge are much lower than those of banks and “formal” money service businesses such as Western Union or MoneyGram. Likewise, as the service is operated informally, AML/CFT regulations are not followed, so currency reporting and customer due diligence requirements (among other controls) are not observed.

¹ John A. Cassara, *Money Laundering and Illicit Financial Flows* (Middletown, DE: John Cassara, 2020), 103.

sociation of Realtors, Chinese buyers in the United States “have been the top foreign buyers in both units and dollar volume of residential housing for six years straight.”²⁷⁰

While foreign capital invested in real estate is not illegal (and is in fact encourage by certain sectors), the primary issue of concern is the origin of the money invested. In the United States there is little if any customer due diligence by real estate agents. Due to the magnitude of the money involved, there is no doubt that some purchases of real estate reflect criminal proceeds that are mixed or co-mingled with invested monies.

We also know that Chinese criminal syndicates are directly involved with real estate purchases. For example, in 2018, law enforcement seized “roughly 100 Northern California houses purchased with money wired to the United States by a Chinese-based crime organization and used to grow massive amounts of marijuana illegally.”²⁷¹ Chinese organized crime in San Francisco and elsewhere helped

²⁷⁰ Diana Olick, “Chinese Buyers Expand Their Reach in the US Housing Market as the Middle Class Gets in on the Act,” CNBC, January 8, 2019. [Retrieved online.](#)

²⁷¹ Don Thompson, “US Seizes Pot-Growing Houses Tied to China-Based Criminals,” Associated Press, April 4, 2018. [Retrieved online.](#)

coordinate the real estate purchases, cultivation of marijuana, sales, and distribution. According to the Associated Press, authorities were able to track “at least 125 wire transfers totaling \$6.3 million from Fujian Province in China, all just below the \$50,000 limit imposed by the Chinese government,” which were used to purchase the properties.²⁷²

Responding to concerns about criminals’ use of real estate to launder illicit funds, Treasury’s FinCEN has used geographic targeting orders (GTOs) that temporarily require U.S. title insurance companies to identify the natural persons behind shell companies used in all-cash purchases of residential real estate. As of 2021, “GTOs cover certain counties within the following major U.S. metropolitan areas: Boston; Chicago; Dallas-Fort Worth; Honolulu; Las Vegas; Los Angeles; Miami; New York City; San Antonio; San Diego; San Francisco; and Seattle.”²⁷³ Unfortunately, purchases outside these jurisdictions, or purchases of commercial property, are not covered by the GTOs which creates a loophole that is evaded easily by those who want to launder money through the purchase of real estate.

SPOTLIGHT ON...

VANCOUVER MONEY LAUNDERING MODEL: REAL ESTATE & CASINOS

The last five to ten years have served as a serious wakeup call to the Canadian Government in regards to massive failures in the country’s AML regime — pointedly, the vulnerabilities exploited by the so-called “Vancouver Money Laundering Model.” The Commission of Inquiry into Money Laundering in British Columbia (Cullen Commission) released its final report in June 2022 that highlighted the key themes brought to light during its investigation and provided recommendations to strengthen Canada’s fight against money laundering.¹

The money laundering was orchestrated by Chinese criminal syndicates, specifically the Triads, and used (and abused) CUBS as well as the real estate and gaming sectors. Comply Advantage provides an excellent overview of how the Vancouver money laundering model works:

“The Vancouver Model process begins in China, where currency controls prevent citizens from taking more than \$50,000 out of the country. To avoid that rule, wealthy Chinese citizens enter into arrangements with domestic criminal syndicates with links to Vancouver. The citizens transfer money to criminal-controlled bank accounts in China before traveling to Vancouver where the criminals’ associates provide them with their funds in Canadian dollars (which may be profits from fentanyl sales, for example). That money is then laundered through casino gambling. The outcomes of wagers made in the casinos are irrelevant since the money is effectively laundered

¹ “Commission Reports,” Commission of Inquiry into Money Laundering in British Columbia, June 15, 2022. [Retrieved online.](#)

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²⁷² Thompson.

²⁷³ Updated from 2019 information. “FinCEN Renews Real Estate Geographic Targeting Orders for 12 Metropolitan Areas,” Financial Crimes Enforcement Network, October 29, 2021. [Retrieved online.](#)

at the point of conversion from cash to casino chips. From there, financial proceeds from the Vancouver Model are either invested back into the acquisition of fentanyl supplies by the criminal gangs or invested into BC real estate by the Chinese citizens themselves, who are able to avoid the scrutiny of Chinese regulators and Chinese taxes by doing so.”²

The Triads have had a strong base in Vancouver for decades. While the “Vancouver Model” may have only come to light relatively recently, the Triads have been using real estate to launder money for decades, according to a 1994 report:

“In one method, Triad companies send drug funds to offshore bank accounts, and use these deposits to secure mortgages for purchasing and developing B.C. land. Another method involves falsified contracts used to make drug cash appear to be legitimate real estate wealth. The buyers pay artificially high prices for property, recording transactions in B.C.’s land title system. But a much lower actual price is paid to a Triad-linked seller, in an offshore bank account transaction.”³

Billions of dollars have been laundered through the Vancouver real estate sector, facilitating criminal activity and capital flight, but also having serious economic impacts on Canadian citizens. A confidential police investigative study found that “than 1,200 luxury real estate purchases in B.C.’s Lower Mainland in 2016 found that more than 10 per cent were tied to buyers with criminal records. And 95 per cent of those transactions were believed by police intelligence to be linked to Chinese crime networks.”⁴

The Expert Panel on Money Laundering also identified the strong connection between real estate in British Columbia and criminal proceeds, assessing that, of the estimated US\$5.9 billion (CA\$7.4 billion) laundered in the province in 2018, approximately 72 percent of these funds were laundered through real estate.⁵ As the primary goal is to launder money, not actually reside in/use the real estate, criminals are willing to pay top dollar—and even more—to secure properties. This has had the unfortunate consequence of driving up property prices within the province by at least five percent, making the market unaffordable to many legitimate buyers.⁶

² “Vancouver Money Laundering Model,” Comply Advantage, accessed November 18, 2021. [Retrieved online.](#)

³ Sam Cooper, “How Chinese Gangs Are Laundering Drug Money through Vancouver Real Estate,” Global News, April 19, 2018. [Retrieved online.](#)

⁴ Sam Cooper, Stewart Bell, and Andrew Russell, “Secret Police Study Finds Crime Networks Could Have Laundered over \$1B through Vancouver Homes in 2016,” Global News, November 26, 2018. [Retrieved online.](#)

⁵ Maureen Maloney, Tsui Somerville, and Brigitte Unger, *Combatting Money Laundering in BC Real Estate* (Victoria, British Columbia: Expert Panel on Money Laundering in BC Real Estate, 2019), 48, 51–52. [Retrieved online.](#)

⁶ Richard Zussman, “Report Finds \$5B Laundered through B.C. Real Estate in 2018,” Global News, May 9, 2019. [Retrieved online.](#)

VANCOUVER: REAL ESTATE AND CASINOS

A case study from the Cullen Commission highlighted the scale of Chinese money laundering in Vancouver as well as the failures by the government and private sector: A Chinese citizen (referred to in the study as Person A) immigrated to Canada in 2006 along with his family, bringing assets of more than US\$990,000 despite declaring an annual salary of a little more than US\$32,000. Over approximately eight years, Person A, along with his wife, child, and mother, “went on to buy US\$25 million worth of Vancouver real estate after moving US\$90 million from Hong Kong-based depositors with connections to organized crime and the Chinese Communist Party.”⁷

While the majority of criminal proceeds were laundered through real estate, the gaming sector—in particular casinos and gambling junkets—also played a crucial role. With gambling junkets, junket operators work directly with casinos, reaching out to wealthy gamblers to attract them—and their money—to particular casinos by offering travel and accommodation, and, more importantly, bankroll the gamblers. This model of using junkets and CUBS to launder criminal proceeds had been used in Macau for a long time, so it is not surprising that it was implemented elsewhere. The money laundering was so flagrant that criminals openly carried hockey bags full of drug cash into B.C. casinos to provide wealthy Chinese gamblers.

⁷ Graeme Wood, “Man Making \$40k/Year Bought \$32m in Vancouver Real Estate via CCP-Linked Offshore Accounts,” *Business in Vancouver*, October 27, 2021. [Retrieved online.](#)

Gaming

Casinos have long been used to launder money—particularly in areas where there is poor governance, lack of AML safeguards in the gaming sector, and weak law enforcement. For example, countries in South Asia and Africa as well as the Philippines and other locations have a heavy Chinese gaming presence. The FATF has long recognized casinos and gaming as a major money laundering methodology.

While gaming is illegal in mainland China, illegal gambling in China is still very popular, including unofficial lotteries, betting games such as mahjong and various card games, and clandestine casinos. The Chinese territory of Macau is the only area where casino gaming is permitted. Millions of tourists flock to the territory each year. Macau’s economy is almost entirely dependent on gaming. Despite a recent downturn, the Chinese territory reported gambling revenue of 293.3 billion patacas (approximately US\$36.5 billion) for 2019;²⁷⁴ in comparison, Las Vegas casinos earned US\$6.6 billion the same year.²⁷⁵

²⁷⁴ Although data is available for 2020, due to the significant deviation in activity caused by COVID-19, data for 2019 was used. Lai Lin Thomala, “Gross Revenue from Gaming and Gambling in Macao from 2010 to 2020 (in Billion Macau Patacas),” *Statista*, June 3, 2021. [Retrieved online.](#)

²⁷⁵ Chris Sieroty, “Nevada Tops \$12B in Gaming Revenue in 2019,” *Gaming Today*, January 30, 2020. [Retrieved online.](#)

In addition to recreational gaming, Macau is also used to evade capital flight restrictions and to launder money. Via junket operators, visitors use renminbi (RMB) to buy casino chips and after playing, cash out in foreign currencies, including dollars. To evade currency controls, Chinese high rollers can do one of two things: they can deposit money with junket operators in the mainland and use that money in Macau, or they can borrow from junket agents. If they choose to deposit the money, the junket gaming promoters ferry money across borders or simply debit and credit accounts; the gamblers can then use that money in Macau. Once done gambling they can take their winnings in U.S. or Hong Kong dollars and direct it elsewhere. The money is effectively laundered.

The above techniques have also been used by Chinese elite to invest in foreign property or offshore tax havens. For example, there are a number of Canadian investigations into billions of dollars being laundered via integrated networks of underground banking, Chinese TCOs, gaming, and real estate investments; it's called the "Vancouver Model" of transnational crime [see above box article].²⁷⁶

While the Vancouver Model typically involved the Triads laundering narcotics proceeds in casinos owned by other entities, other TCOs have kept the laundering in-house. For example, two Chinese nationals owned and operated two casinos in Guatemala which they used to launder at least \$30 million from drug trafficking conducted by their TCO. The funds were link to "illegal drug sales in the United States, which were picked up by a series of couriers up and down the East Coast, and then laundered through Guatemala by the pair of men back to the Colombian cartels."²⁷⁷

Secrecy Jurisdictions and Anonymous Companies

Money launderers and those involved with illicit financial flows use many methods to "layer" and disguise their transactions so that law enforcement authorities have a difficult time "following the money." A common tactic is to use offshore shell companies without beneficial ownership information, i.e. anonymous companies.

SPOTLIGHT ON...

DIFFERENT TYPES OF SECRECY

The European Parliamentary Research Service notes that terms like "offshore jurisdiction," "secrecy jurisdiction," and "tax haven" have overlapping meanings, and are typically used to "describe jurisdictions that feature distinctive characteristics such as low or zero taxation, fictitious residences (with no bearing on reality) and tax secrecy. Each of them puts the focus on a different feature: the foreign location for offshore centres, and the anonymity or non-disclosure of financial dealings and ownership of assets, in the case of secrecy jurisdictions."¹

¹ Cécile Remeur, "Listing of Tax Havens by the EU" (Brussels: European Parliamentary Research Service, May 2018). [Retrieved online.](#)

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²⁷⁶ Cooper, "How Chinese Gangs Are Laundering Drug Money through Vancouver Real Estate."

²⁷⁷ Adam Rawnsley and Seamus Hughes, "Casino Royale: Feds Say Chinese Drug Barons Laundered U.S. Coke Cash in Guatemalan Casinos," *The Daily Beast*, January 23, 2020. [Retrieved online.](#)

DIFFERENT TYPES OF SECRECY

Offshore jurisdiction: Also known as an offshore financial center, these jurisdictions are known for having “relatively large numbers of financial institutions engaged primarily in business with non-residents; financial systems with external assets and liabilities out of proportion to domestic financial intermediation designed to finance domestic economies; and [provide benefits such as] low or zero taxation; moderate or light financial regulation; banking secrecy and anonymity.”²

Secrecy jurisdiction: A jurisdiction “that specialises in enabling individuals to hide their wealth and financial affairs from the rule of law, not just for the purpose of underpaying tax but for other financial crimes like money laundering and funding terrorist groups.”

Tax haven: A jurisdiction “with low or no corporate taxes that allow outsiders to easily set up businesses there... [and] typically limit public disclosure about companies and their owners.”³

Shell company: A company with no active and/or meaningful business activity or significant assets, and which is primarily used to conduct financial transactions.

Anonymous company: A corporate entity “that has disguised its ownership in order to operate without scrutiny from law enforcement or the public.”⁴

Legal entity: Also known as a “legal person,” a legal entity refers to an individual as well as “any company or organization that has legal rights and responsibilities, including tax filings... can enter into contracts either... and can sue or be sued in a court of law.”⁵

Natural person: An actual human being.

² Monetary and Exchange Affairs Department, “Offshore Financial Centers,” International Monetary Fund, June 23, 2000. [Retrieved online.](#)

³ Will Fitzgibbon and Ben Hallman, “What Is a Tax Haven? Offshore Finance, Explained,” International Consortium of Investigative Journalists, April 6, 2020. [Retrieved online.](#)

⁴ “Anonymous Companies,” Global Financial Integrity, accessed November 19, 2021. [Retrieved online.](#)

⁵ Lauren McMenemy, “What Is the Meaning of a Legal Entity?,” *Diligent Insights* (blog), May 13, 2019. [Retrieved online.](#)

Most offshore jurisdictions do not require companies to list the natural person(s) who profit from their existence or control their activities—the actual “beneficial owners” of the business.²⁷⁸ This has made anonymous companies the vehicle of choice for drug cartels, organized crime, corrupt foreign officials, and others who need to launder money. The inability of law enforcement to access beneficial ownership information frustrates police and prosecutors, and harms the American public in myriad ways.

²⁷⁸ This sentence originally referenced the U.S. as one of the offshore jurisdictions that did not have beneficial ownership requirements; it was modified due to the passing of the Corporate Transparency Act.

For example, the British Virgin Islands (BVI) is one of the world's largest offshore destinations for secrecy. It is also one of the favorite destinations for Chinese citizens that want to move businesses and cash offshore. Research by Capital Economics found that more than 40 percent of the BVI's offshore business came from mainland China and Hong Kong in 2015.²⁷⁹ In Chinese slang, having a "BVI" is "shorthand... for any offshore company, regardless of where in the world it is located."²⁸⁰

The massive information leaks that have popped up over the last decade, such as the Panama Papers and Pandora Papers, have shown how Chinese citizens and entities have also availed themselves of other offshore financial centers and anonymous structures in Singapore, Malaysia, Panama, other Caribbean islands, the Cook Islands, and other non-transparent havens. In the "China Leaks" investigation, the International Consortium of Investigative Journalists traced the ownership of approximately 22,000 secretive shell companies back to individuals in mainland China and Hong Kong, who included "some of China's most powerful men and women."²⁸¹

According to revelations in the Panama Papers, many clients unmasked in the document dump and subsequent journalistic investigations include ruling communist Chinese elites and their family members.²⁸² The documents provide a rare window as to how the Chinese privileged class sends wealth offshore. Other common techniques are to use trade-based value transfer and trade-mispricing techniques, dress up that wealth in offshore secrecy, and then sometimes return it to China disguised as foreign investment which enables special tax and other privileges.

In regards to the magnitude of the relationship between Mossack Fonseca and China, *The Economist* notes:

"China has been Mossack Fonseca's most important market. The firm's office in Hong Kong was its busiest. It also has offices in eight other Chinese cities. The International Consortium of Investigative Journalists, which has been poring over the Panama papers, says that at the end of 2015 Mossack Fonseca was earning fees from 16,300 offshore firms set up by its Chinese offices. That was 29% of all the active companies represented by the law firm."²⁸³

Just as Mossack Fonseca was popular in facilitating Chinese capital flight, so too have anonymous companies been a preferred tool for facilitating other IFFs. For example, Nate Sibley explains that "Chinese officials reportedly promised to bankroll the siphoning of \$4.5 billion from Malaysia's 1MDB development fund into anonymous companies, dissuade U.S. law enforcement from investigating, and then spy on the reporters exposing the scheme."²⁸⁴ Anonymous companies have also been linked to Chinese entities and individuals engaged in sanctions evasion in relation to dealings with North Korea and Iran.²⁸⁵

279 Xie Yu, "China, Hong Kong the Biggest Source of Funds to British Virgin Islands," South China Morning Post, June 25, 2017. [Retrieved online.](#)

280 Max de Haldevang, "The Secret Insider Terms Used in Chinese Money Laundering," yahoo! news, March 6, 2018. [Retrieved online.](#)

281 This paragraph has been modified from the original to reflect an updated source. Marina Walker Guevara et al., "Leaked Records Reveal Offshore Holdings of China's Elite," International Consortium of Investigative Journalists, January 21, 2014. [Retrieved online.](#)

282 Juliette Garside and David Pegg, "Panama Papers Reveal Offshore Secrets of China's Red Nobility," *The Guardian*, April 6, 2016. [Retrieved online.](#)

283 "The Panama Papers Embarrass China's Leaders," *The Economist*, April 7, 2016. [Retrieved online.](#)

284 Nate Sibley, "How to Fight China's Financial Abuses: Crack Down on Anonymous Companies," Hudson Institute, February 5, 2019. [Retrieved online.](#)

285 This paragraph has been modified to reflect an updated source. Sibley.

Illicit Financial Flows and the China Context

The Chinese government has made no secret of its ambition to surpass the West both militarily and economically by the regime's 100th anniversary in 2049 in the hope that the 21st century will be dominated by China in the same way that the 20th century was dominated by the United States. According to a popular saying in Chinese mythology, "there is only one sun in the sky."

Scholar Evan Ellis aptly frames the far-reaching impacts of China's ambitions:

There is nothing wrong, per se, about China's aspirations for prosperity and security, as expressed by President Xi's "dream" for the rejuvenation of the great Chinese Nation, or his goal for the PRC to be a powerful developed country by the 100th anniversary of Chinese Communist rule in 2049. What is worrisome is how the PRC achieves and maintains that wealth and power within the increasingly interdependent global environment and what those activities and the position of Beijing means for the liberal world order, political and economic conditions, and rights and liberties of the rest of the world.²⁸⁶

Michael Collins, the deputy assistant director of the CIA's East Asia Mission Center stated in 2018 that Beijing's tactics to achieve its ambitions fit the definition of a cold war: "I would argue by definition what they're waging against us is fundamentally a cold war... A country that exploits all avenues of power licit and illicit, public and private, economic and military, to undermine the standing of your rival relative to your own standing without resorting to conflict."²⁸⁷

Indeed, under President Xi the Communist party has moved in the last few years to become more forceful and controlling both internally and globally. For example, Xi's efforts to boost internal control include a continuation of the brutal crackdown on the Uyghur ethnic group as well as an accelerated civilian surveillance program which includes the use of drones, video monitoring, and a social credit system in which individuals garner credits which help them obtain loans and jobs. Additionally, in 2018 the Communist Party of China (CCP) freed President Xi Jinping from term limits. In 2019 it attempted to exert increasing influence in Hong Kong where it tried [to] institute an extradition law so scofflaws could be tried in mainland China.

China is also increasingly using its power and influence in the international arena. For example, Made in China 2025 and China's Belt and Road initiative have the joint goal of transforming the country into a hi-tech powerhouse that dominates complex industries like robotics, advanced information technology, aviation, and new energy vehicles while simultaneously engaging in infrastructure projects in well over 100 countries. The ability to transform and, indeed, dominate business sectors while concurrently garnering political influence through overseas investment could be the platform on which China's economic dominance is built.

Over the past few decades, to further their influence globally, China has pursued unfair trade practices, intellectual property theft, predatory investment, and other key national economic security im-

286 Evan Ellis, "Latin America and the Emerging Ideological Struggle of the 21st Century," *Global Americans*, June 17, 2018. [Retrieved online.](#)

287 Tom Porter, "China Is Waging a New 'Cold War' to Topple the U.S. as the World's Leading Superpower: CIA Official," *Newsweek*, July 22, 2018. [Retrieved online.](#)

peratives. However, China has pursued one area of economic influence that has received significantly less attention by the West — but is no less important. It's the threat it poses to the international financial system and the licit economy.

There are a number of endemic contributing factors to Chinese financial malfeasance and criminality including corruption, weak rule of law, lack of effective financial oversight and enforcement, weak regulatory controls, entrenched underground financial systems, and government policies that work to facilitate profit, growth, exploitation, and cheating at the expense of international standards and norms. While each of these issue areas may fall in the purview of traditional law enforcement or trade regulation, viewed together they undermine much of the world's efforts over the last twenty years to combat corruption, illicit finance, and money laundering.

Moreover, the illicit finance threats emanating from China pose serious risks to the integrity of the global financial system which is the bedrock of much of the West's economic and political power. This is a risk that is too big to ignore. With China's assumption of the presidency of the FATF in July 2019, its inability or unwillingness to address these risks [was] thrown into even sharper focus and causes one to wonder whether Clausewitz's famous dictum should be updated for the 21st Century as "transnational crime is the continuation of war by other means."

This section highlights many of the risks China poses to the legitimate world economy and explores ways China is the primary actor in international money laundering and is complicit in illicit financial flows. Available metrics show China has the dubious distinction as being the largest player in almost every major sector of transnational crime. Collectively, the criminal categories outlined [earlier] annually generate trillions of dollars of illicit funds that are laundered into the licit economy. In 2019 the State Department included China on its list of "primary countries of concern" for money laundering.²⁸⁸

Over the last twenty years criminal activity has seemingly become part of China's strategy to grow its economic and military power. China uses a combination of statecraft, military buildup, espionage, theft, cheating, trade, loans, debt traps, payoffs, investment and other forms of exchanges and engagement to structure a 21st century world order "with Chinese characteristics" in which global trading networks, political relationships, and international institutions support China's expanding wealth and power. "China Inc.," a term that refers to behemoth market-oriented, state-owned enterprises with global commercial reach, also plays a key role in Chinese influence and control.²⁸⁹

Chinese growth has relied upon the twin pillars of cheap labor and technology theft from the West. From software to steel, from pharmaceuticals to powerplants, the Chinese are dependent upon both industrial and state espionage. In America and much of the West, this has led directly and indirectly to stagnant wages, a shrinking middle class, loss of manufacturing jobs, dependency on Chinese supply chains and production of vital goods and equipment, and hollowed-out towns and decaying cities. It threatens our national security.

There is no doubt that some activity such as forms of weapons proliferation, identity theft, and intel-

288 See U.S. Department of State, *International Narcotics Control Strategy Report, Volume II: Money Laundering, 2019* (Washington, D.C.: U.S. Department of State, 2019), 77. [Available online.](#)

289 "China Inc." is a generic term, however see Ted C. Fishman, *China, Inc.: How the Rise of the Next Superpower Challenges America and the World* (New York: Scribner, 2006).

lectual property rights violations are directed by the Government of China. In fact, China's National Intelligence Law from 2017 requires organizations and citizens to "support, assist and cooperate with the state intelligence work."²⁹⁰ Other suspect activity occurs due to independent actors, lack of capacity by law enforcement and customs, corruption, lack of political will and/or willful blindness. But by identifying the enormous illicit proceeds generated and laundered, the unmistakable picture that develops is that there is a worrisome convergence between the Chinese government/CCP, China Inc. and Chinese-organized crime that directly impacts the United States and order in the world economy.

The following are some of the major internal factors that impact the flow of IFFs to and from China as well as China's response.

Capital Flight

According to a former Canadian Ambassador to Beijing, "China is the number one exporter of hot money to the world."²⁹¹ The exodus of capital has fueled worries about the Chinese economic outlook. Issues of concern include a China/U.S. trade war, the plummeting Chinese stock market, devaluation of the Chinese currency, fears of a real estate bubble, suspect loans and balance sheets by Chinese banks, the theft of state funds by Chinese officials, paltry returns on savings accounts, the coronavirus pandemic, and other social unrest. Furthermore, as the Chinese government clamps down on corruption, savvy Chinese are transferring wealth out of the country. Many Chinese elites also want "golden visas" and foreign citizenship that are offered for substantial sums of money.

Capital flight also exacerbates the perception of equality in the communist country. Frank Gunter explains some of the negative impacts of China's growth:

In one generation, China has transitioned from one of the most egalitarian states in the world to one of the most unequal. While Chinese government estimates of income and wealth inequality are state secrets, Forbes reports that there are 400 billionaires in China, second only to the 540 billionaires in the United States. Combined with the country's millionaires, it appears that less than 0.5 percent of the population controls wealth equal to 25 to 33 percent of China's GDP.²⁹²

As a result, the Chinese government has imposed capital controls on its citizens and has recently begun penalizing severe violators with jail time. Chinese citizens are restricted to sending the equivalent of approximately \$50,000 per person out of the country per year.

So how does capital flee China? There are a number of methods including:

- Tapping political and personal connections
- Using the transfer quotas of friends and family members to get money out of the country

290 William Evanina, "Keynote Remarks as Prepared for Delivery" (LegalSEC Summit 2019, Arlington, VA, June 4, 2019), 2. [Retrieved online.](#)

291 Frank O'Brien, "Property Sales Spike Sparks Money Laundering Fears," *Compliance Alert* (blog), accessed April 27, 2022. [Retrieved online.](#)

292 Frank R. Gunter, "Why China Lost About \$3.8 Trillion To Capital Flight In The Last Decade," *Forbes*, February 22, 2017. [Retrieved online.](#)

- Channeling funds through gaming and junkets, particularly via Macau
- Using the special relationship with Hong Kong that serves as a financial conduit to the rest of the world
- Trade-based value transfer
- Underground financial systems
- Obtaining special financial services offered to the elites

Capital flight poses a few important questions and issues regarding illicit financial flows and money laundering:

1. Massive amounts of capital leave China. Is illicit money co-mingled with legitimate money?
2. Does China consider capital flight over the reporting threshold money laundering? If so, is that designation reciprocal in the receiving country?
3. For the U.S. and most other countries, receiving foreign capital is not illegal. In fact, it is often encouraged. However, money laundering could occur if the foreign capital includes the proceeds of crime or it is used to further criminal activity in the destination country. (For example, see the section on real estate above.) Yet the source of Chinese money flooding into the United States and elsewhere is rarely questioned.
4. While the influx of capital can be helpful, it can also distort local markets, cause inflationary pressure, become the catalyst for social disruptions, create undue influence, etc.

Corruption

Corruption is the great facilitator for international money laundering. According to Transparency International's 2021 Corruption Perception Index, China is ranked 66 out of 180 countries.²⁹³

Over the last few years, the Chinese government has initiated a sweeping anti-corruption campaign that has led to thousands of arrests. Many of those arrested are the political enemies of Chinese President Xi Jinping and his cronies. Professor Joel Kotkin provides a good overview of how wealth has affected China's politics and society:

Rather than rule by proletarians and peasants, the leadership is increasingly dominated by so-called "red princelings," such as President Xi himself, who trace their roots to generals and top officials of the initial Maoist regime. Even the entrepreneurial class has been subsumed. Some 90% of China's millionaires, notes Australian political scientist David Goodman, are the offspring of high-ranking officials... In today's China, about 1,300 individuals hold roughly 20 percent of the country's wealth and the top 1 percent has roughly a third of it — while much of the country, particularly in the countryside, still lives at the brink of poverty.²⁹⁴

Unfortunately, corruption continues to negatively influence the business environment inside of China. According to the China Corruption Report, "Companies are likely to experience bribery, political interference or facilitation payments when acquiring public services and dealing with the judicial

293 Modified to reflect updated ranking. "Corruption Perceptions Index 2021," Transparency International, accessed April 27, 2022. [Retrieved online.](#)

294 Joel Kotkin, "A Clash of Values," *New Geography* (blog), November 14, 2019. [Retrieved online.](#)

system. The common practice of *guanxi* is a custom for building connections and relationships based on gifts, banqueting, or small favors.”²⁹⁵

The Economist explains that China has also exported its corruption to Africa:

According to China’s critics... the Chinese are bringing bad habits as well as trade, investment, jobs and skills. The mainland economy is riddled with corruption, even by African standards. International rankings of bribe-payers list Chinese managers near the top. When these managers go abroad they carry on bribing and undermine good governance in host countries. The World Bank has banned some mainland companies from bidding for tenders in Africa.²⁹⁶

Beijing routinely uses both a hard and soft a hand around the world that provides quid to extract pro-China quo. Chinese practice various forms of influence, but in most countries around the world corruption and payoffs are predicate offenses for money laundering. It is rarely investigated or prosecuted.

It is not always easy to put a number on the value of corruption, however AML expert Christine Duhaime writes that Chinese authorities estimate that approximately US\$1.5 trillion (CA\$2 trillion) of funds representing corruption have been laundered out of China since 1995.²⁹⁷ She notes that, while “China appears to have quit sharing data officially after 2011... [the Chinese government] said at that time that the outflows of proceeds of corruption [were] severe enough to threaten its economy and its political stability.”²⁹⁸

Duhaime adds that the Bank of China reports that “about 16,000 to 18,000 officials with ties to the public sector were involved in moving proceeds of corruption illegally from China to other countries,” with the top destinations for the corrupt funds being the United States, Australia, Canada, and the Netherlands.²⁹⁹

In addition to official corruption, there are forms of private and commercial corruption and payoffs which are rampant in Chinese society as well as “grey” income. Grey income is income earned or acquired off the books and not included on income tax reports.³⁰⁰ Much of this money also is laundered and enters into the world’s licit economy.

Chinese companies also facilitate corruption and crime though the manufacture of fake identification cards and other documents such as birth certificates, passports, test certifications, national identification cards, etc. They advertise their product online, and sales occur around the world including the United States. For example, in November 2019 U.S. Customs and Border Protection seized more than 5,000 fake IDs—both already-made and the blank cards used to make them—which

295 “China Corruption Report,” GAN Integrity, August 2020. [Retrieved online.](#)

296 “Trying to Pull Together,” *The Economist*, April 23, 2011. [Retrieved online.](#)

297 Sentence modified to reflect source. Christine Duhaime, “\$2,000,000,000,000 in Proceeds of Corruption Removed from China and Taken to US, Australia, Canada and Netherlands,” *Duhaime’s Anti-Money Laundering Law in Canada* (blog), January 2, 2017. [Retrieved online.](#)

298 Duhaime.

299 Sentence modified to reflect source. Duhaime.

300 Duhaime.

had been sent from China and destined for numerous destinations in the U.S.³⁰¹

Enforcement and AML Compliance

Generally speaking, China does not cooperate with other countries in pursuing financial crimes and anti-money laundering investigations. This is extremely important because it is imperative to have international cooperation in pursuing international illicit financial flows. The United States and China are parties to the Agreement on Mutual Legal Assistance in Criminal Matters. U.S. agencies consistently seek to expand cooperation with Chinese counterparts on AML/CFT matters and to strengthen both policy- and operational-level cooperation in this area.

Although there have been some recent improvements, particularly in the area of narcotics investigations, U.S. law enforcement agencies note China has not cooperated sufficiently on financial investigations.³⁰² In addition to the lack of law enforcement-based cooperation, the Chinese government's inability to enforce U.S. court orders or judgments obtained as a result of non-conviction-based forfeiture actions against China-based assets remains a significant barrier to enhanced U.S.-China cooperation in asset freezing and confiscation.³⁰³ It is not clear how diligently, and with what resources, China monitors illegal trading of all sorts by Chinese companies and investigates breaches. Concerns are also heightened by China's weak response to Western requests for interdiction of suspect trade practices.

China boasts the world's second largest economy and a vibrant financial sector. Almost all banks in China are state-owned and the world's top four banks in [terms of] assets are Chinese.³⁰⁴ Although in the Chinese banking sector, corruption, lack of honest oversight, high-risk loans, clever valuation techniques, and shadow banking are pervasive.

Shadow banking occurs when banks and non-bank financial institutions lend money outside of lending norms and safeguards. The loans are often packaged into complicated wealth management and other financial products. Banks market these risky loans as a way to increase profits and share debt. Chinese banks keep shadow banking assets off their balance sheets, thereby sidestepping regulatory constraints on lending.

Shadow banking in China is somewhat analogous to the 2007 and 2008 subprime lending crisis in the United States that triggered a global financial crisis, lost trillions of dollars in wealth, created bankruptcies and foreclosures, and destroyed millions of jobs. Since that time, shadow banking in China has mushroomed into a \$10 trillion obscure financial system.³⁰⁵ It connects thousands of financial institutions with companies, local governments and hundreds of millions of households.³⁰⁶ A 2016

301 Stephanie Pagonis, "CBP Finds More than 5,000 Fake IDs Sent from China," FOX Business (Fox Business, November 29, 2019). [Retrieved online.](#)

302 U.S. Department of State, *INCSR Vol. II*, 2019, 77.

303 See U.S. Department of State, *International Narcotics Control Strategy Report, Volume II: Money Laundering and Financial Crimes, 2016* (Washington, DC: Bureau of International Narcotics and Law Enforcement Affairs, U.S. Department of State, 2016), 95. [Available online.](#)

304 Peter Pham, "How Does China's Banking System Work?," Forbes, March 15, 2018. [Retrieved online.](#)

305 "A Guide to China's \$10 Trillion Shadow-Banking Maze," *Bloomberg*, June 7, 2018. [Retrieved online.](#)

306 "A Guide to China's \$10 Trillion Shadow-Banking Maze."

report from investment bank CLSA said that Chinese shadow banking comprised approximately 57 percent of total bank loans.³⁰⁷ In other words, Chinese economic activity and financial services are severely distorted. A panic or collapse could pose direct threats both to the [Government of China] and also to the licit global economy.

The head of the Central Commission of Discipline Inspection at the People's Bank of China, Xu Jia'ai, said China's financial system is dogged by a corrupt alliance of "cats and rats."³⁰⁸ Once again, corruption manifests itself, and the watchdogs and regulators turn a blind eye. Another area where the corrupt alliance manifests itself is in the weak culture of AML/CFT compliance.

For example, in Italy, the Bank of China (BOC)—the largest bank in the world based on assets—facilitated the laundering of billions of euros via a BOC branch in Italy. Over a four-year period, approximately 4.5 billion euros were illegally transmitted, in part by the Milan Branch of the BOC, from the greater Florence area to China.³⁰⁹ For years China and the BOC stonewalled the Italian investigation. In 2017, the BOC settled with the government of Italy on the criminal case and later paid a 20 million euro fine to Italian tax authorities.³¹⁰

It was initially reported that when Italian officials tried to appeal to Chinese authorities for help, "they got nowhere." Prosecutors discovered that "Money2Money," an Italian company owned by Chinese immigrants, had been transferring the proceeds of criminal activity. Italian authorities investigating the transactions had encountered the "great legal firewall [that] separates China from the West."³¹¹

China does not have an independent legal system that is recognizable in the West. The CCP is supreme in legal matters. The Party claims that China is a country ruled by law: the claim is fatally undermined by a 99 percent conviction rate. In 2014, only 1,039 of more than 1.2 million people were found not guilty in the country's Communist Party-controlled courts. The acquittal rate is approximately 0.08 percent.³¹² In other words, China is ruled by Party whim, not law.

In February 2016, Spanish police raided the Madrid subsidiary of Industrial and Commercial Bank of China, arresting five of the bank's local directors on suspicion of money laundering based on electronic intercepts of Chinese bank employees conspiring to launder money.³¹³ The investigation disclosed the bank's complicity in laundering approximately 1.2 billion euros out of Spain to China between 2009 and the end of 2012.³¹⁴ There has been a lack of cooperation in the investigation by Chinese authorities with the Spanish investigation.

307 "Shadow Banking Lies at the Core of China's Systemic Financial Risk," *China Banking News* (blog), December 29, 2017. [Retrieved online.](#)

308 Frank Tang, "China's Financial System Dogged by a Corrupt Alliance of Cats and Rats, Central Bank Discipline Chief Says," *South China Morning Post*, February 1, 2018. [Retrieved online.](#)

309 "Bank of China Paid Italy 20 Mln Euros to Settle Tax Dispute Linked to Money Laundering Case - Source," Reuters, June 16, 2017. [Retrieved online.](#)

310 "Bank of China Paid Italy 20 Mln Euros to Settle Tax Dispute Linked to Money Laundering Case - Source."

311 Stanley Lubman, "Dirty Dealing: China and International Money Laundering," *Wall Street Journal*, July 13, 2015. [Retrieved online.](#)

312 Neil Connor, "Chinese Courts Convict More than 99.9 per Cent of Defendants," *The Telegraph*, March 14, 2016. [Retrieved online.](#)

313 Berwick and Lague, "How China's Biggest Bank Became Ensnared."

314 Berwick and Lague.

A blog from the London School of Economics details how New York regulators fined the Agricultural Bank of China \$215 million:

...for a series of irregularities and apparently deliberate masking of suspicious transactions. Details of originators and counterparties on international payments were concealed through a coding system to hide suspicious sources. The coding was applied to transfers between suspicious Chinese and Russian trading companies and transfers enacted on behalf of an Afghan drug trafficker.³¹⁵

Some Chinese banks are also complicit in North Korea's efforts to evade financial sanctions. For example, in September 2016, the U.S. Department of Justice found that from 2009 to 2015, Chinese nationals had used 22 front companies to open accounts in Chinese banks.³¹⁶ The laundering facilitated dollar transactions through the U.S. financial system for sales to Pyongyang. Treasury also issued an advisory on North Korea's use of the international financial system, which emphasized the role of Chinese banks.³¹⁷

Agricultural Bank of China and China Construction Bank have been identified as helping North Korea launder its money. Both of these banks, China's second- and third-largest, each have more assets than JPMorgan Chase & Co., America's largest bank. Because of their size, some feel that they are "too large to sanction."³¹⁸

Chinese banks have also been instrumental in providing Iran relief from sanctions. China is Iran's largest trading partner and trade ties between China and Persia have existed for nearly 2,000 years. This close trade relationship has also been boosted of late through China's Belt and Road Initiative. The Export-Import Bank of China and Chinese banks are providing financing and lines of credit in support of Iran's economy. The tens of billions of dollars of loans provided by the Chinese are primarily targeted towards infrastructure projects in the water, energy and transport industries. In return, China is Iran's largest oil customer. China's insatiable appetite for petroleum accounts for a third of Iran's overall trade.³¹⁹

In 2012, the United States sanctioned China's Bank of Kunlun. The Treasury Department singled out the Bank of Kunlun because it provided financial services to designated Iranian banks and facilitated the movement of millions of dollars' worth of international transactions connected to Iran's program of proliferation and/or support for terrorism.³²⁰

The Bank of Kunlun, a state-owned bank, continued to be one of the main conduits at the heart of China's trade with Iran. However, the Bank of Kunlun recently shifted policy and informed clients

315 Chen, "Chinese Banks Are Accused."

316 Anthony Ruggiero, "Severing China-North Korea Financial Links," Center for Strategic & International Studies, April 3, 2017. [Retrieved online.](#)

317 Financial Crimes Enforcement Network, "Advisory on North Korea's Use of the International Financial System" (Washington, D.C.: U.S. Department of the Treasury, November 2, 2017). [Retrieved online.](#)

318 Christian Berthelsen, "U.S. Considered Blacklisting Two Chinese Banks Over North Korea Ties," *Bloomberg*, April 13, 2018. [Retrieved online.](#)

319 "Chinese Banks Open \$35 Billion in New Financing to Iran," RWR Advisory Group, September 20, 2017. [Retrieved online.](#)

320 "Treasury Sanctions Kunlun Bank in China and Elaf Bank in Iraq for Business with Designated Iranian Banks," U.S. Department of the Treasury, July 31, 2012. [Retrieved online.](#)

that it will no longer process payments that contravene U.S. secondary sanctions on Iran.³²¹ Chinese commercial banks undoubtedly do not want to risk disconnection from the international banking system by transacting with Iran.

China continues to facilitate Iran's skirting the current round of sanctions. In particular, it is believed imports from China will be facilitated by trade-based value transfer including barter trade. Iranian businessmen and brokers are very active in China. There is also a large Chinese trading presence in Iran. Undoubtedly, these brokers will use smaller transactions to continue the Iranian/Chinese trade. Similar to previous rounds of sanctions, many of the deals will be cleared by Iranian safari or a network of exchange shops. Safari is linked to the hawala (*havaleh* in Iran) underground financial system. *Havaleh* has been used for centuries. It operates much the same way as the Chinese *fei-chien* or flying money system of underground finance. Credits and debits are routinely settled via a trade-based counter-valuation process that is practically immune to outside scrutiny.

321 Maziar Motamedi, "Policy Change at China's Bank of Kunlun Cuts Iran Sanctions Lifeline," Bourse & Bazaar Foundation, January 2, 2019. [Retrieved online.](#)

Conclusion and Recommendations

China plays an outsized role in transnational crime mirroring its growth as an international superpower. The country's rapid economic development has been a catalyst for advancements across a variety of industries as well as lifting 800 million people out of poverty over the last few decades. At the same time, however, the country has expanded its influence in a broad array of transnational crime areas including trafficking, narcotics and IP theft, as well as illicit financial flows.

There are two significant aspects to consider when evaluating transnational crime and IFFs in China: the factors that drive and/or facilitate these illicit activities, along with how and when the country responds to these activities.

In regards to the factors contributing to China's rise in global crime, internal dynamics within the country—economic, political, social, and cultural—are major drivers and/or facilitators of transnational crime and IFFs. Economically, innovation in industries such as manufacturing, computer technology, and pharmaceuticals have also translated to gains in transnational crime. Illicit actors have taken advantage of these improvements, using the technical advancements to easily produce counterfeit goods as well as manufacture synthetic drugs and precursor chemicals. However, the regulation and oversight of these sectors have not kept abreast with the technical progress, and illicit actors, both “traditional” and corporate, have taken advantage of both.

In addition, the policies that opened up China's economy have also meant that illicit actors in China as well as Chinese consumers of illicit goods have access to new markets. Connected to this is the growth of China's burgeoning middle class, who now have greater disposable incomes. This has meant greater buying power, which, in terms of transnational crime, has turned to increased demand for illicit goods such as illegal wildlife products like ivory and rhino horn. Increased wealth, coupled with the country's currency controls, has escalated the amount of illicit capital flight from China. These flows often move through informal channels, such as via underground banking which often facilitates criminal activities, especially money laundering.

Politically, by far one of the clearest drivers of transnational crime in China is state-sponsored forced labor. Beijing has sanctioned the use of forced labor as a tool in the punishment and/or rehabilitation of citizens seen as being recalcitrant such as drug addicts, extremists, political activists, religious offenders, and minor criminals. In the case of Turkic-speaking Muslims in Xinjiang who China views as extremists, Beijing has instituted forced labor programs both inside and separate from the region's internment camps as part of their “rehabilitation” programs.

China's household registration system—*hukou*—is intended to manage the country's population, maintain social stability and deliver social services, among other objectives, however it can also place internal migrant workers in a vulnerable position where they may end up in informal employment which puts them at a higher risk of exploitation.

The one-child policy implemented by China in 1980 was designed to slow down the country's rapid population growth, however its impacts extend much deeper throughout society. Coupled with a cultural preference for males, the decades-long rule has led to a massive gender imbalance, with approximately 30 million more males than females in the country. These “surplus males” have con-

tributed to the phenomenon of bride trafficking, particularly cross-border, where women and girls are deceived into marriage or are forced into labor or sexual exploitation after marriage.

Another factor in transnational crime is the cultural importance of traditional Chinese medicine (TCM), which has spawned a multi-billion-dollar global industry. While TCM is a legitimate system of medicine that has existed for millennia, it overlaps with the illegal wildlife trade due to the use of wildlife in different medical treatments. Beijing strongly backs the industry both at home and abroad and allows for the farming of wild species for TCM. This support legitimizes demand and allows for illegally-obtained animals and products to be laundered through the legal trade.

In regards to the country's response to transnational crime, China is relatively unique in that the leading determinant in the effectiveness of its response to transnational crime is political will. Many countries that experience high levels and/or a variety of transnational crime often experience one or more capacity challenges—technical, technological, financial, human, etc.—with their response, particularly developing and emerging market countries. Everything considered, Beijing has the capacity to deal with much of the transnational crime that occurs within the country, particularly given the fact the China is an authoritarian state.

Therefore, political will, or the lack thereof, is a major determinant of when and how Beijing responds to transnational crime as well as IFFs: China's response by and large depends on the perceived domestic impacts. If Beijing perceives the crime to have serious domestic impacts, such as threats to national health and security, it will respond swiftly and severely. This can be seen in how the country handled the cultivation and consumption of opium and the (illicit) trade in wildlife for consumption following the outbreak of COVID-19.

If Beijing does not perceive a specific type of transnational crime to have serious domestic consequences, it will typically not take any effective and/or sustained policy or enforcement actions to combat it. Beijing customarily will only respond to transnational crimes that have “minor” domestic impacts if there is significant international pressure. However, even then, the response has often been symbolic rather than a genuine attempt to curtail the activity, particularly if it involves key sectors or industries.

Felbab-Brown succinctly sums up China's pattern of response in regards to the regulation of and enforcement in certain important “domains”, writing:

The following pattern emerges: The government of China at first tends to deny the existence of a problem. Under international or strong domestic pressure, it eventually moves to tighten regulation. But its enforcement tends to be limited and subverted by powerful vested interests of industry representatives, officials of line ministries charged with regulating or promoting the industry, and government officials. Geostategic interests also trump other considerations, such as enforcement of regulatory compliance.³²²

This has been evidenced in the scheduling of fentanyl and precursor chemicals, the regulation of the pharmaceutical and chemical industries, the ban on ivory and the policies around wildlife farming, the continued use of forced labor as a tool for rehabilitation and/or punishment, weak IP rights and

322 Felbab-Brown, *Fentanyl and Geopolitics*, 3.

enforcement, as well as enforcement against counterfeiting focusing primarily on the sale of counterfeit goods rather than their manufacture. In addition, depending on the actor and type of crime, China may treat an offense as more of an administrative issue rather than a criminal one.

Understandably, a multitude of recommendations can be made on how to better combat China's transnational crime and IFFs, both by China itself as well as other countries. The following are "macro" recommendations focused on some of the major changes China could make to improve its response to these illicit activities along with recommendations for the U.S. and other countries in combatting transnational crime and IFFs from China.

Recommendations for China

Improve the regulation and oversight of the pharmaceutical and chemical manufacturing industries. This could include strengthening the Guidelines for Standardization of Enterprises' Management of Non-Pharmaceutical Precursor Chemicals to require mandatory reporting to a national-level authority, such as the NNCC. This should include all illicit behaviors rather than allowing the companies to handle most cases in-house and only report "severe" cases to local-level authorities. One option is requiring all companies that manufacture and/or distribute pharmaceutical or chemical components related to narcotics and precursor chemicals to register with and receive licensing from the NNCC. Among other things, this would move oversight from the local level, which may face issues of corruption or conflicts of interest, to the national level.

Work to harmonize China's list of scheduled and banned drugs and precursors with international partners. Equally important is to enact class-wide controls on narcotics, such as was done with the scheduling of all fentanyl-like drugs, in order to prevent producers from evading the ban by tweaking chemical formulas.

Design and enact legislation solely focused on human trafficking. It is important to ensure that the law covers all forms of trafficking (sexual, labor, etc.) as well as all of the acts (recruitment, transport, transfer, etc.) and means (force, coercion, deception, etc.) as defined in the Palermo Protocol and punishes them equally. In addition, the law must equally treat men and women as victims, with additional weight given to crimes committed against minors (i.e., anyone under the age of 18) regardless of gender.

End the use of forced labor as a tool for re-education and legal punishment. This includes its use of detention centers, the "labor training programs" connected to the internment of ethnic minorities such as in Xinjiang and Tibet, as well as the acceptance of any North Korean citizens sent by the DPRK government.

Revise the "first to file" system. Modify relevant IP and trademark legislation, moving from giving protection to those individuals or entities that "file first" to giving protection to those who first came up with the invention.

Focus on manufacturers. Increase enforcement against individuals and entities that manufacture counterfeit goods or items that infringe on IP rights, including strengthening financial and criminal penalties. Enforcement actions in recent years have largely focused on the sale of counterfeit goods, such as on e-commerce platforms.

End the farming of any/all endangered and threatened species. China should institute a blanket ban on the farming of any CITES-listed species, regardless of the intended destination of the animal or product (e.g. consumption, TCM, etc.). The legal trade in endangered/threatened species legitimizes the demand, can incentivize poaching and creates a channel through which illegally-sourced goods can be laundered, among other issues. On a related note, China should harmonize its List of Wildlife under Special State Protection with the CITES Appendices.

Ban the use of wildlife in TCM. There are 70 wild species used in different TCM medical treatments, however there are alternative plant and mineral ingredients that can be used. As Beijing has long backed the TCM industry, both domestically and abroad, it should ban the use of any wild species in TCM as well as actively engage with the TCM community to promote and enforce it.

Recommendations for the U.S.

Hold countries accountable for weak pharmaceutical and illicit chemical controls. Explore policies to hold accountable countries that fail to sufficiently regulate the legal trade in pharmaceuticals and precursor chemicals used to produce illegal narcotics, including fentanyl and its analogs, as well as adequately implement and enforce such laws/regulations.

Hold China accountable for abuses in Xinjiang. Continue to use targeted sanctions and all diplomatic tools available to hold those responsible for the human rights and forced labor abuses in Xinjiang accountable.

Develop a national strategy to combat counterfeiting and IP theft. Develop voluntary, consensus-based technical standards, best practices, and guidelines for the private sector and institutes of higher education so that they can design, adopt and deploy strategies to combat counterfeiting and IP theft.

Study the illicit financial flows related to wildlife trafficking. Conduct a study on the illicit financing and proceeds related to wildlife trafficking, including an overview of the role of professional launderers and gatekeepers, the convergence of wildlife trafficking with other transnational crime, and the national security implications.

Continue to make combatting corruption a high priority in the U.S. national security strategy. Corruption is a major facilitator of transnational crime and illicit financial flows, undermining national, economic, and environmental security in the U.S. and abroad. The U.S. Government must continue to curb corruption and its deleterious effects by modernizing, coordinating, and resourcing efforts to fight corruption; curbing illicit financing; and holding corrupt actors accountable, among others.

Target the individuals, entities, and countries facilitating financial crimes and money laundering. Apply economic and other targeted financial sanctions with respect to individuals and entities engaged in financial crimes and money laundering, particularly trade-based money laundering. In addition, explore policies to hold accountable countries that fail to sufficiently investigate financial crimes and money laundering and/or provide adequate responses to requests for financial investigations information.

Study the role of Chinese professional money laundering networks. Conduct a study on the role of Chinese professional money laundering networks in laundering the proceeds of transnational crime and corruption.

Study the IFFs between China and Afghanistan. Conduct a study on the financial activities of China and Chinese entities in connection with the finances of Afghanistan and the Taliban, including an assessment of the activities undertaken by the People's Republic of China and Chinese-registered companies to support illicit financial networks in Afghanistan, including those related to natural resources.

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