Non-prosecution compliance system opens a new stage of compliance system establishment for Chinese enterprises

In April 2021, the Supreme People’s Procuratorate issued the Plan on Carrying out the Pilot Program of Corporate Compliance Reform (the “Plan”), officially launching the second phase of the pilot program. The first phase has been rolled out in Shanghai, Jiangsu, Shandong, Guangdong, and other places since March 2020. At the Fourth Session of the 13th National People’s Congress held this year, Chief Prosecutor Jun Zhang reported the pilot program to the National People’s Congress.

The Plan defines the Pilot Program of Corporate Compliance Reform as “for criminal cases involving enterprises, the procuratorates, while making decisions not to arrest, not to prosecute, or to propose a lighter sentence based on the system of ‘imposing lenient punishments on those confessing to their crimes and accepting punishments’, shall supervise and urge the enterprises involved to make compliance commitments pursuant to the crimes and cases in question, and to actively rectify and implement commitments, for the purpose of promoting corporate compliance and law-abiding operations, reducing and preventing corporate crimes, and making progress on the political, legal, and social fronts.”

The preceding paragraph describes what the Corporate Compliance Non-Prosecution System with Chinese characteristics is, and such characteristics entail, among others, “non-arrest compliance”, “non-prosecution compliance”, “lenient sentencing recommendations based on compliance”, and “lenient punishment recommendations based on compliance (administrative penalty recommendations)”. Procuratorates perform their duties by factoring corporate compliance into conviction and sentencing, transforming punishments to corrections. This will surely be conducive to advancing the establishment of corporate compliance systems in China. The Supreme People’s Procuratorate blazed the trail with the launch of Compliance Non-Prosecution System, a move that will drive other judicial and supervisory agencies towards building corporate compliance systems, and jointly achieve the comprehensive social governance. The value of corporate compliance has once again been strongly demonstrated.

Since the beginning of the 21st century, Chinese companies have become increasingly aware of “compliance” as they find themselves struggling with legal barriers amid the “Go Global Strategy” and stuck with corporate-level battles in the context of the Sino-U.S. trade war. Since 2017, the State Administration for Market Regulation (Standardization Administration), the State-owned Assets Supervision and

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1 The Supreme People’s Procuratorate: “The Supreme People’s Procuratorate issued a work plan to promote the in-depth development of the pilot reform of corporate compliance in an orderly manner in accordance with the law. The scope of the second phase of the reform pilot was expanded to 10 regions including Beijing and Zhejiang.” https://www.spp.gov.cn/xwfbh/wsfbt/202104/t20210408_515148.shtml?ZhCZs3cBrx6S=1618479382950#1 (last visited on April 16, 2021).
Administration Commission, the National Development and Reform Commission and other ministries and commissions have successively issued corporate compliance management guidance, signaling the upgrading of “compliance establishment” from corporate behavior to government-guided efforts. In the past two years, judicial organs’ exploration of a system of corporate compliance non-prosecution has led to a new stage of corporate compliance establishment. In the new stage, compliance establishment will no longer be a passive implementation, but an intrinsic need; it is no longer optional, but a mandatory demand that must be fulfilled.

I. Pilot Areas and Typical Cases of the “Non-Prosecution Compliance System”

In fact, “compliance non-prosecution” is still not a true “system” and has been put into practice very recently. However, the Supreme People’s Procuratorate has placed a special emphasis on “compliance non-prosecution”, and such official endorsement will undoubtedly be an important driving force for its implementation. In this article, “compliance non-prosecution” is referred to as a “system” for convenience.

The Supreme People’s Procuratorate’s first phase of the pilot program of the “corporate compliance non-prosecution system” was carried out in six procuratorates in Shanghai, Jiangsu, Shandong, and Guangdong.²

The second phase of the pilot program was confirmed in April 2021 and involves ten provinces and direct-administered municipalities, including Beijing, Liaoning, Shanghai, Jiangsu, Zhejiang, Fujian, Shandong, Hubei, Hunan, and Guangdong. The procuratorates carrying out the pilot system are determined by the above-mentioned provincial-level procuratorates, with each province or municipality selecting 1 to 2 procuratorates for the pilot system. Compared with the first phase, the scope of the second phase has been greatly expanded.

As a reform pilot program, the implementation rules and operating methods will be tested first by the participating procuratorates under the guidance of the Supreme People’s Procuratorate. The author’s research reveals that most of these procuratorates has published specific measures in the form of internal documents to implement the pilot system.³


³ Examples includes the “Opinions on Establishing a Compliance Inspection System for Criminal Enterprises” jointly formulated by ten agencies including the Liaoning Provincial Procuratorate and the Liaoning Provincial Municipal Supervision Bureau, and the “Provisions on the Selection and Management of Persons (Trial)” issued by the Shenzhen Baoan District Justice Bureau. The former provides more comprehensive measures for the implementation of the "corporate non-prosecution compliance system", and clearly stipulates the subject and content of compliance inspections of different types of crimes, which serve as significant references; the latter establishes detailed guidance on the “independent monitoring person”, a specific third-party supervision mechanism.
In addition to implementing the “corporate compliance non-prosecution system” at the organizational and institutional level, certain areas have also tested the application of the system in handling specific criminal cases. Typical cases published by the Supreme People’s Procuratorate include:

In an environmental pollution case of a chemical machinery company and its management handled by the Zhangjiagang City Procuratorate of Jiangsu Province, the prosecutors supervised and urged the enterprises involved in the case to establish a compliance regime. After the regime passing the inspection and evaluation of entrusted personnel from environmental protection, taxation, emergency management and other departments, the company went through a public hearing participated by the district government, public security organs, people supervisors, the Federation of Industry and Commerce, and lawyers. The attendees of the hearing unanimously formed a non-prosecution decision.

In a case involving employees of a technology company suspected of bribing non-state employees handled by the Shenzhen Nanshan District Procuratorate, while making a decision not to prosecute, the procuratorate urged the company to establish an anti-commercial bribery compliance system and restart its filing procedure for listing.

II. Application of the “Non-Prosecution Compliance System”

Compliance non-prosecution did not originate in China, but in Europe and the United States. The Federal Sentencing Guidelines formulated by the U.S. Federal Sentencing Commission in 1987 stipulates that, if a company has established an effective compliance program, criminal penalty can be reduced. The U.S. Department of Justice subsequently issued Prosecutor’s Manual according to the aforementioned guidelines, for the first time explaining the specific requirements for prosecutors to apply compliance non-prosecution or deferred compliance prosecution, which laid a practical foundation for its application in other jurisdictions. The UK’s Crimes and Courts Act 2013 stipulates the deferred compliance prosecution in criminal cases, which is similar to the U.S. deferred prosecution rules. Since then, Canada, Australia, Singapore and other countries have also established a deferred prosecution system.4

In China, it was not until 2015 that the “first case of non-prosecution for compliance” occurred, i.e., the case of a company forging special value-added tax invoices and fictitious mortgages handled by the Daishan County Procuratorate of Zhejiang Province. In this case, the company involved made compliance rectification and issued a “Self-Inspection and Rectification Commitment Letter” in exchange for the prosecutor’s decision not to prosecute. At present, the Supreme People’s Procuratorate’s two-phased pilot program signify that “compliance non-prosecution” has entered a systematic and institutionalized stage.

As an important new judicial measure, the active promotion by the Supreme

Procuratorate has also been widely responded to by the scholars and lawyers. The *Law Journal* set up a special column, inviting scholars to discuss corporate compliance non-prosecution in the first issue of 2021. Combining judicial exploration and academic viewpoints, the author interprets the application of the system as follows:

A. Application Scope of the Non-Prosecution Compliance System

*Firstly, the non-prosecution system for corporate compliance applies not only to corporate crime cases, but also to individuals involved in the criminal cases as corporate operators.*

In the current practice, most procuratorates launching the pilot system have stipulated that in addition to crime-related enterprises, the compliance non-prosecution system also applies to business operators, managers, and other key personnel. For example, the *Opinions on Establishing a Compliance Inspection System for Crime-Involved Enterprises* ("Opinions on the Compliance Inspection System"), formulated by ten agencies including the Liaoning Provincial Procuratorate, stipulates that the compliance inspection system for crime-related enterprises is applicable to crimes committed by entities and crimes committed by key individuals whose crimes are intimately related to the production and operation of the entities, such as business operators, managers, and key technical personnel.

When the Supreme People’s Procuratorate issued the Plan, it pointed out that the implementation of pilot program of non-prosecution for compliance is to protect the legitimate rights and interests of private entrepreneurs and is a necessary step when the person in charge of the enterprise involved in the case is not arrested, prosecuted, or imposed sentences on. The non-prosecution system for corporate compliance should not only be applied to crimes committed by entities, but also to crimes committed by individuals related to the production and operation of the entity, including corporate managers, operators, and directly responsible personnel.

*Secondly, in the pilot program, the corporate compliance non-prosecution system is generally applicable to minor cases with less than 3 years of imprisonment, but it can also affect sentencing for some severe cases.*

For example, Article 6, Section 1 of *Opinions on the Compliance Inspection System* stipulates that the compliance inspection system is applicable to cases where corporate responsible personnel may be sentenced to imprisonment of less than three years, criminal detention, surveillance, or a criminal fine.\(^5\)

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\(^5\) Article 6 Paragraph 1 of the “Opinions on Establishing a Compliance Inspection System for Enterprises Involved in the Crime”: “The compliance inspection system applies to crime-related enterprises when the following conditions are met: (1) the enterprise or personnel involved in the crime are first offenders or incidental offenders; (2) The facts of the crime are clear, and the evidence is reliable and sufficient; (3) The directly responsible person in charge and other directly responsible persons may be sentenced to fixed-term imprisonment of less than three years, criminal detention, surveillance, or a criminal fine according to law; (4) The company and the directly responsible executives and other directly responsible personnel involved in the crime have no objection to the main facts of the crime and voluntarily plead guilty and admit penalties.”
Meanwhile, Article 6, Section 3 of *Opinions on the Compliance Inspection System* also stipulates the application conditions for cases that may impose imprisonment ranging from 3 to 10 years.⁶

At present, some scholars have discussed the application of the compliance non-prosecution system in severe criminal offenses for which the culprits may be sentenced to more than three years. Professor Ruihua Chen’s view is that for large and medium-sized companies that are qualified to implement special compliance management systems, “even if they are suspected of serious crimes, procuratorates can still apply conditional non-prosecution to them, carry out compliance investigation and supervision, and make a decision not to prosecute”⁷. Even for serious crimes where “compliance non-prosecution” may not be applicable, other compliance incentives can be provided, such as “providing lenient sentencing recommendations or suggesting to reduce the fines”⁸.

The author understands that the compliance non-prosecution system is not only applicable to misdemeanor cases, but also to felony cases, but what the application entails in either type of cases is different. In misdemeanor cases, procuratorates can decide “not to arrest” or “not to prosecute”, whereas in felony cases, procuratorates can propose a “lenient sentencing” or “lenient administrative penalties”.

**Thirdly, the types of crimes to which the non-prosecution compliance system can be applied.**

At present, some procuratorates launching the pilot system have enumerated the types of crimes to which the compliance non-prosecution system can apply. The cases eligible for the system include, but not limited to, commercial bribery, crimes of disrupting market order; crimes of producing and selling fake and inferior products; crimes relating to taxation; local financial organized crimes; crimes of banking and insurance companies; crimes of environmental pollution; crimes of destroying natural resources; and crimes of smuggling.

**B. The Party and Timing to Initiate the Compliance Non-Prosecution System**

**Firstly, the Supreme People’s Procuratorate’s Plan clarifies that only procuratorates are allowed to initiate compliance non-prosecution. However, other government**

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⁶ Article 6 Paragraph 3 of the *Opinions on Establishing a Compliance Inspection System for Crime-Involved Enterprises*: “The directly responsible persons in charge and other directly responsible persons shall be sentenced to fixed-term imprisonment of not less than three years but not more than ten years in accordance with the law. If an accomplice in a joint crime, or the directly responsible person in charge or other directly responsible person has a meritorious service, the compliance inspection system may be applied.”


agencies, especially public security agencies, can make recommendations in the application of the system.

According to the current Plan, procuratorates can initiate the compliance non-prosecution procedure. However, for the purpose of implementing the system and from the perspective of the comprehensive social governance, the responsibility to urge the companies involved in the cases to strengthen compliance management and to improve the modernization of social governance doesn’t just lie with procuratorates. Other public authorities, such as courts, judicial administrative authorities, public security authorities, supervisory authorities, and other competent authorities and supervising authorities, as well as individual representatives, can also propose to apply the “compliance non-prosecution compliance system” in specific cases pursuant to the laws and regulations.

Especially, the investigative agencies other than the procuratorate can initiate the “compliance non-prosecution system”, because at present, the public security organs are responsible for docketing and investigating most of the corporate criminal cases. When procuratorates intervene, the companies or individuals concerned may have been subject to compulsory investigation measures, which gives rise to the unwanted consequence of “destroying an enterprise”. Therefore, it is very necessary to start the procedures of “compliance non-prosecution system” as early as possible during the investigation stage.

Professor Ruihua Chen puts forward the procedures he has developed to address this concern: first, the public security agencies may promptly transfer the case to procuratorates for review and confirmation after they have made a decision to docket a case against a suspected criminal enterprise and found that the case meets the conditions of the compliance non-prosecution system; second, public security agencies can also incorporate corporate compliance mechanisms into its investigation process.

Secondly, certain regions launching the pilot system require local procuratorates to initiate compliance inspection procedures within 30 days after the date of the case being transferred for review and prosecution, but for companies willing to adopt the system, they should initiate the procedures as soon as possible.

Regarding the timing to initiate the compliance non-prosecution procedures, the Supreme People’s Procuratorate’s Plan only clarifies that it should be combined with the rules of the system of leniency for guilty pleas and punishment acceptance, procuratorial suggestions, and non-prosecution proposals, and does not specify a deadline. The Opinions on the Compliance Inspection System limits the initiating time to 30 days after the date of transfer for review and prosecution.

The author understands that, as mentioned above, in addition to the review and prosecution by procuratorates, public security agencies, supervisory authorities and other agencies can also make suggestions to apply this system in accordance with the law before the case is reviewed and prosecuted, especially in the investigation stage. Therefore, if a company is willing to adopt the system, an assessment should be conducted as soon as possible, so as to apply the compliance non-prosecution system in the early stage of investigation.
C. Inspection and Implementation of Corporate Compliance Establishment

The “compliance non-prosecution system” is a conditional non-arrest, non-prosecution, or a leniency system. It is a combination of the non-prosecution system and corporate compliance. The condition precedent is that the company is willing to carry out compliance establishment and accept inspection and supervision. Therefore, the key to the implementation of the system is how to carry out corporate compliance and how to establish a compliance system that meets the requirements of the regulatory agency after a procuratorate agrees to apply the system.

1. Compliance inspection period

At present, certain procuratorates carrying out the pilot system have set the compliance inspection period for crime-involved companies at 3 to 5 months, while some have set it at 6 months to 1 year or even longer. Based on the consideration of “legitimacy of the reform”, the time limit of the compliance inspection period mainly depends on the provisions of China’s Criminal Procedure Law on the review and prosecution period, and the procuratorates seek the longest possible inspection period within the statutory time limit in order to leave enough time for an effective compliance supervision.

2. Compliance supervision

An effective compliance supervision is the key to the implementation of the compliance non-prosecution system, and to some extent determines the success of this reform. The cases have shown that compliance supervision is not carried out by procuratorates alone. The trend now is to engage external supervisory experts. The participation of lawyers and other professionals is also necessary.

In an environmental pollution case handled by Zhangjiagang City Procuratorate, which was made public by the Supreme People’s Procuratorate, the district government, public security agencies, people supervisors, the Federation of Industry and Commerce and lawyers jointly participated in the post-supervision evaluation hearing. The Opinions on the Compliance Inspection System also stipulates that for compliance inspection cases which procuratorates make a decision not to proceed with, procuratorates shall engage administrative supervision agencies, lawyers, accountants, tax agents and other professionals in a comprehensive review of the compliance establishment of the crime-involved enterprises. In the Regulations on the Selection and Management of Individuals for the Independent Monitoring of Corporate Criminal Compliance (tentative), the Shenzhen Baan District Justice Bureau states that “the independent monitor of corporate criminal compliance refers to a law firm entrusted by a suspected enterprise to investigate, plan, and supervise the criminal compliance of the enterprise”.

Now, there are three main modes of corporate compliance supervision:

The first mode is led by procuratorates, who shall take the lead in hiring professional institutions as external supervisors. The Shenzhen Nanshan District Procuratorate adopts this mode.

The second mode is the independent monitor mode (professional supervision mode).
An enterprise involved in the case hires external professional institutions such as law firms, accounting firms, or certified tax agents to serve as independent monitors in accordance with the requirements of procuratorates. The Shenzhen Baoan District Procuratorate adopts this mode.

The third mode is the supervision of the administrative department mode. Procuratorates entrust the administrative department of the government or the sub-district or township government where the enterprise is located as the inspection agency. The People’s Procuratorate of Ningbo City, Zhejiang Province adopts this mode.

3. Compliance Agreement and Commitment

In general, for an enterprise that meets the applicable conditions, procuratorates will sign a compliance supervision agreement with the enterprise, and in some places, a compliance commitment is required. The content of the compliance supervision agreement generally includes, among others, the enterprise undertaking the obligation to cooperate in the investigation, compensating the victims or paying a fine; the enterprise developing a compliance plan; the supervision mode of the corporate compliance plan; the regular reports required by the compliance plan; the agreement inspection period; the application of inspection results and the legal consequences of a breach of the agreement. Currently, no consensus has been reached on the nature of the agreement.

4. Compliance establishment plan

An effective compliance establishment plan recognized by procuratorates is the primary prerequisite for enterprises to obtain leniency such as non-prosecution. The Opinions on the Compliance Inspection System requires: “the compliance plan should target the suspected crimes of the enterprise, comprehensively sort out the problems and loopholes in the corporate internal governance structure, rules and regulations, and personnel training that triggered the crimes, to formulate comprehensive compliance management regulations, to establish an effective compliance organization system, and to improve the risk prevention and response mechanisms to effectively prevent the recurrence of the crimes.”

5. Compliance report

Compliance reports include the “Compliance Implementation Report” submitted regularly during the implementation of the compliance plan, and the “Compliance Evaluation Report” issued at the end of the compliance review period. The former is provided by the company with the assistance of professionals to the supervisory authorities or independent supervisors on a regular basis and is subject to supervision during the process; the latter is a comprehensive assessment and evaluation of the company’s compliance establishment and the implementation of compliance agreements conducted by the regulatory agencies after inspection. The opinion will serve as a basis for procuratorates to make a decision on whether to prosecute.

6. Review and decision

After the inspection period, procuratorates will conduct a review and make a final
decision after the regulatory agency issues an evaluation opinion. Generally, if the company involved in the crime has completed compliance system establishment as required and there is no violation of the requirements of the regulatory agreement during the inspection period, procuratorates shall make a decision not to prosecute the company involved and the directly responsible persons in charge or other directly responsible individuals. Procuratorates may also propose a lenient and mitigated punishment in the cases in which the prosecution is required; and procuratorates may propose a lenient treatment for administrative punishments that need to be imposed.

In accordance with the transparency requirements of the compliance non-prosecution compliance, when procuratorates make a final decision, it should generally make the decision public and invite administrative agencies, professional institutions or other supervisory bodies to participate.

III. Suggestions for Enterprises

A. Conduct in-depth study of the policy and seize the opportunities from the beginning of the reform.

Corporates should realize that the establishment of a corporate compliance system in exchange for non-prosecution or other leniency is a favorable opportunity and they should seize the opportunities from the current judicial reform. Companies involved in certain crimes should study the specific implementation methods of local procuratorates’ compliance non-prosecution system as soon as possible and try the best to obtain opportunities to adopt the system. Even companies outside the current two areas rolling out the pilot system should study the system, because it is likely that the system will expand its reach. Moreover, the “first case” of this kind occurred in 2015, which means that the system can be applied regardless of whether there are pilot programs.

B. Submit the application as soon as possible and don’t wait till the review and prosecution stage.

According to current judicial practice, the power to initiate the compliance non-prosecution system belongs exclusively to procuratorates, but this does not mean that companies involved in crimes do not have the right to express their opinions during the initiation of the system. Therefore, companies willing to adopt the system should actively seek the opportunity and submit an application as soon as possible. In particular, in order to avoid the relevant compulsory property disposal measures that adversely affect the business operations during the investigation stage, it is necessary to cooperate and sign the Statement of Recognition of Guilty and Punishment and other documents in advance.

C. Applications can be submitted through different channels to protect the legitimate interests of the companies.

After evaluation, if an enterprise potentially involved in crimes believes that the compliance non-prosecution system can be applied to itself, it should apply to procuratorates at different stages of the case. It can apply to procuratorates during the review and prosecution stage, or it can apply to procuratorates, public security agencies,
etc. during the investigation stage. Of course, the company can also submit their intention of adopting the system through statutory channels to the relevant administrative agencies, the Federation of Industry and Commerce, or the local People’s Congress, the CPPCC (Chinese People’s Political Consultative Conference) and its representative members and special supervisors.

D. To invite the professionals to participate in the process, especially the development and implementation of compliance plans.

As a judicial measure still in the trial and reform stage, the interpretation and assistance of lawyers and other professionals is undoubtedly necessary. Lawyers and other professionals should participate at least in the stages such as the analysis and evaluation of corporate crimes, the application for the compliance non-prosecution system, the drafting and review of compliance agreements and commitments, the development and implementation of compliance plans, the participation in compliance supervision, the drafting and review of compliance reports, the communication with relevant agencies including procuratorates and the participation in criminal proceedings, etc.

Among them, the most important factor in the entire process is how to formulate an effective compliance plan, to ensure that it is implemented in accordance with regulatory requirements, and to get the approval from procuratorates and other regulatory agencies or supervisors. Enterprises should work with a professional team that has practical experience in handling corporate compliance matters in civil, administrative, and criminal procedures to carry out the compliance program.

E. Enterprises should develop compliance plans as soon as possible regardless if it is involved in any criminal matter or not.

The value of a compliance system lies in the establishment of compliance-oriented corporate values. Against the current international and domestic regulatory background, Chinese companies should take extra precautions and start developing compliance systems as soon as possible. Chinese corporate managers should realize that compliance system has become an intrinsic and necessary requirement for companies. Compliance bears essential importance for expanding business in the future. The sooner the establishment of compliance system, the greater chances companies have in getting an upper hand in the future competition.

Although the feedbacks on the pilot program are still unknown and the establishment of institutional the compliance non-prosecution system is still under exploration, there have been cases that have prevented corporate responsibility through a good compliance system in China⁹.

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⁹ In the case of the crime of illegally selling citizens' personal information [first trial: (2016) Gan 0102 Xing Chu No. 605; final trial: (2017) Gan 01 Xing final No. 89] in the People’s Court of Chengguan District, Lanzhou City, Gansu Province, the court held that considering that Nestlé has established a compliance system and has adopted the compliance measures, and that the behavior of the company's employees is not a manifestation of the will of the company, the case is not a company crime case, and Nestlé does not constitute a company crime.
Especially when China’s compliance non-prosecution system is still at the initial stage, companies that take the lead in establishing compliance plans will have the leading advantage and will be more likely set an example, conducive to guiding relevant agencies to establish compliance standards that are in line with the company’s own situation. Moreover, since more and more compliance requirements and regulatory policies will be enacted, establishing a compliance management system as soon as possible will help companies to deal with the impact of a greater wave of strict and intensive regulatory requirements.

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