

Original Paper

Tax Compliance Non-Prosecution: Logical Foundations,
Application Review, and Integrated Pathways—A Perspective
from the Greater Bay Area in China

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Abstract

Compliance non-prosecution serves as a criminal incentive mechanism aimed at encouraging private enterprises to strengthen internal management and prevent criminal conduct, representing a proactive response to modernizing crime governance centered on cooperative justice. As a significant economic engine, the Greater Bay Area in China would benefit from an integrated tax compliance criminal system to support tax compliance within enterprises involved in legal disputes, promoting their sustainable development. Given the unique characteristics of tax-related cases, the Greater Bay Area should establish a tax compliance criminal procedure led jointly by legal and prosecutorial authorities. This procedure should categorize cases by severity into discretionary non-prosecution and conditional non-prosecution, thus creating a unified standard that integrates governance and prevention in tax compliance rectification. Additionally, an interconnected tax compliance cooperation mechanism should be established within the Greater Bay Area. Such unified regulations on tax compliance non-prosecution would strengthen collaboration in tax enforcement, enhance the standardization, fairness, and transparency of criminal tax compliance procedures, and ultimately improve both enforcement efficiency and judicial authority.

Keywords

Greater Bay Area, tax, criminal compliance, non-prosecution, compliance rectification

1. Problem Statement

Since the 18th National Congress of the Communist Party of China, efforts to modernize the national governance system and enhance governance capabilities have been continuously advanced. The report from the 20th Congress further established “deepening the modernization of the national governance system and governance capabilities” as one of the primary development goals for the next five years. The reform of compliance-based non-prosecution for enterprises involved in criminal cases exemplifies the national governance approach within the criminal justice system, representing an experimental implementation of consultative justice in the field of criminal offenses.

In March 2020, the Supreme People’s Procuratorate launched pilot programs in six grassroots procuratorates, including those in Zhangjiagang, Jiangsu, and Bao’an, Shenzhen, aimed at advancing compliance reform for enterprises involved in legal cases and extending judicial functions into the domain of social governance. In April 2021, a second phase of pilots was initiated across ten provinces, including Beijing, Liaoning, Shanghai, and Guangdong. By April 2022, the compliance pilot program had expanded nationwide. As of September 2023, procuratorial authorities across China had handled a total of 7,815 corporate compliance cases. Between March 2020 and December 2021, one-third of non-prosecution cases involving corporate compliance in the ten pilot provinces were related to tax offenses.

The Greater Bay Area (GBA), China’s first region formally recognized at the national level as a bay area, includes two Special Administrative Regions along with nine cities in Guangdong Province: Guangzhou, Shenzhen, Zhuhai, Foshan, Huizhou, Dongguan, Zhongshan, Jiangmen, and Zhaoqing. The GBA is a major driver of China’s regional economic growth. Private enterprises form a significant part of the local economy and constitute a critical source of tax revenue for local governments. The development of these private enterprises directly impacts local tax revenue and economic growth. At the same time, the GBA is a region with a high incidence of tax-related cases involving private enterprises, placing pressure on law enforcement agencies and creating instability in the business environment, which in turn affects economic development in the region.

Establishing a tax compliance non-prosecution system suited to the GBA’s unique characteristics is essential for guiding enterprises involved in tax-related cases to strengthen tax compliance and prevent tax offenses. Such a system aligns with the GBA’s goals of enhancing governance capacity and effectiveness, promoting policy coordination and regional cooperation, and advancing economic integration.

While compliance non-prosecution is still in its pilot phase, national-level policies remain limited to guiding opinions. Many pilot regions have issued local compliance guidelines for enterprises involved in legal cases, based on the nine-department guiding opinion, with some regions even developing field-specific compliance guidelines. For example, the Liaoning Provincial People’s Procuratorate and other agencies issued the *Opinion on Establishing a Compliance Inspection System for Enterprises Involved in Criminal Cases*, which includes a few specific rules related to tax compliance. In

Shenzhen's Pingshan District, the *Guideline on Criminal Compliance for Biopharmaceutical Enterprises* was introduced in response to the area's status as a national biopharmaceutical base, with a high concentration of such enterprises. Additionally, the Haidian District People's Procuratorate and the Haidian District Federation of Industry and Commerce in Beijing jointly published the *Compliance Rectification Guide for Enterprises Involved in Tax-Related Offenses*. Although the guide has some limitations, it provides valuable references for developing specialized tax compliance guidelines in other regions.

Local guidance facilitates the in-depth implementation of the enterprise compliance reform pilot program at the local level, providing clearer and more specific case-handling directions for enterprises involved in legal cases. It also helps to standardize the actions of local governments and relevant departments, ensuring the orderly and fair conduct of the compliance reform pilot program for enterprises involved in criminal cases.

In the nine mainland cities of the Greater Bay Area (GBA), intercity transactions among enterprises have become common, and local tax enforcement and criminal justice cooperation are closely integrated. However, these nine cities are distributed across three free trade zones and one special economic zone, where, despite a generally unified tax system, specific policies vary to some extent. Differences particularly exist in standards for classifying similar tax-related cases and in tendencies toward treatment and penalties. Coordinating tax compliance non-prosecution regulations across the mainland cities of the GBA can improve work efficiency, conserve judicial resources, and provide equal and consistent opportunities for enterprises involved in tax-related cases within the compliance non-prosecution framework.

Additionally, the GBA's unique structure of "one country, two systems, and three customs zones" results in varying degrees of differences in tax structures, tax administration, and judicial systems. With the ongoing advancement of the compliance non-prosecution pilot program in mainland China, collaboration in tax-related criminal compliance among the three regions in the GBA is increasingly essential. Although the pilot program does not currently extend to the special administrative regions, the economic interconnection among the three areas and the growth in cross-border transactions make collaboration in tax-related criminal compliance inevitable. This requires cooperation not only in tax administration but also among judicial authorities across the three jurisdictions in the GBA.

2. Logical Foundations of the Compliance-Based Non-Prosecution System for Enterprises Involved in Legal Cases

2.1 Multi-Agency Collaborative Governance as the System's Starting Point

Four key national-level documents currently provide guidance on compliance procedures for enterprises involved in legal cases. In June 2021, nine departments—including the Supreme People's Procuratorate (SPP) and the Ministry of Justice—jointly issued the *Guiding Opinions on Establishing a Third-Party Supervision and Evaluation Mechanism for Enterprise Compliance in Cases Involving*

Criminal Offenses (Trial). In January 2022, these nine departments released the detailed *Implementation Rules* for this guiding opinion, followed by the *Provisions on the Selection and Management of Third-Party Professionals in the Enterprise Compliance Supervision and Evaluation Mechanism (Trial)* issued by the Third-Party Mechanism Management Committee. In April 2022, the nine departments jointly issued the *Measures for Compliance Construction, Evaluation, and Review of Enterprises Involved in Criminal Cases (Trial)*. Collectively, these guiding documents provide direction for establishing a compliance-based non-prosecution system for enterprises in China, forming the logical foundation of this framework.

The reform for compliance-based non-prosecution is led by the SPP in collaboration with the Ministry of Justice, Ministry of Finance, Ministry of Ecology and Environment, State-Owned Assets Supervision and Administration Commission, State Taxation Administration, State Administration for Market Regulation, All-China Federation of Industry and Commerce, and China Council for the Promotion of International Trade. This collaborative governance framework reflects the principles of co-construction, co-governance, and shared responsibility in tax governance, embodying the need for multi-departmental coordination in compliance reforms for enterprises involved in criminal cases.

The guiding documents establish a “Third-Party Supervision and Evaluation Mechanism for Enterprise Compliance” to specify the applicable entities and conditions for the mechanism, clarify the responsibilities of various participants in the compliance process, and set up mechanisms to prevent illegal or corrupt practices. Specifically, the core participants in the compliance non-prosecution process include the enterprise involved, the People’s Procuratorate, the Third-Party Mechanism Management Committee, and the third-party supervision and evaluation organization selected by the committee. Auxiliary participants include relevant government departments and the regulatory authorities overseeing the enterprise. According to the guiding opinions, the third-party supervision and evaluation mechanism for enterprise compliance is led by the People’s Procuratorate, which is responsible for reviewing and deciding whether a criminal case involving an enterprise qualifies for the third-party mechanism. The Third-Party Mechanism Management Committee, formed by the nine departments, selects a third-party organization to evaluate, supervise, and inspect the compliance rectification outcomes of the enterprise, with the inspection results serving as a key reference for the People’s Procuratorate in case handling.

2.2 Guilty Plea as the Basis of the Compliance System

The guilty plea system was first introduced in the 2018 *Criminal Procedure Law*, allowing leniency in substance and procedural simplicity when a suspect voluntarily admits guilt, sincerely expresses remorse, and accepts punishment. This system, applied at stages including investigation, review, prosecution, and trial, embodies a balanced approach to criminal justice, improving efficiency and mitigating social conflict. The compliance guidelines integrate the guilty plea system into the compliance framework for enterprises involved in criminal cases, resulting in a functional shift in its application. A guilty plea not only serves as a prerequisite for leniency but also becomes a necessary

condition for an enterprise to initiate the third-party mechanism.

The compliance-based non-prosecution process can only commence if the enterprise or individual involved acknowledges guilt and accepts punishment. On this basis, the enterprise must be capable of maintaining regular business operations and commit to establishing or enhancing a compliance program, thereby qualifying and voluntarily opting to use the third-party mechanism. In this context, the guilty plea and leniency system requires the enterprise to sign a statement of guilt and punishment acceptance, effectively establishing an “agreement” between the prosecution and defense. The compliance-based non-prosecution process embodies the governance concept of “consultative justice,” wherein the state and the enterprise involved communicate and negotiate through a dialogic judicial model. This process represents an exploratory shift from “adversarial justice” to “consultative justice” within the compliance framework.

However, due to the transformed role of the guilty plea in the compliance process, the results of leniency are often delayed and uncertain. Whether an enterprise ultimately receives a non-prosecution decision depends on whether its compliance efforts meet effectiveness standards and whether any fraudulent practices were used to deceive the evaluation process. A guilty plea alone does not guarantee leniency; it merely creates the possibility of lenient treatment.

2.3 Prosecutorial Discretion and Discretionary Non-Prosecution as Institutional Foundations

The compliance-based non-prosecution system for enterprises involved in criminal cases in China remains in its pilot phase, with implementation guided primarily by the opinions of nine departments, and has not yet undergone legislative codification. This system is an innovative approach within the current legal framework, where pilot procuratorates explore “compliance-based non-arrest” or “compliance-based non-prosecution” mechanisms based on prosecutorial discretion. Initially, after a case is transferred from the public security bureau to the People’s Procuratorate, the procuratorate reviews it to determine if it qualifies for the third-party mechanism. If the case meets the requirements, the mechanism is activated. Subsequently, the procuratorate reviews the evaluation process and conclusions of the third-party organization. Although the third-party mechanism management committee also has an obligation to review the evaluation conclusions, the procuratorate, as the judicial authority responsible for handling the case, holds the final discretionary power to decide on non-prosecution.

Thus, the compliance-based non-prosecution system is both led by and fundamentally reliant on the discretionary powers of the procuratorate. The legal foundation for compliance-based non-prosecution can be traced to the discretionary non-prosecution provisions in China’s *Criminal Procedure Law* and the exemption from criminal punishment provisions in the *Criminal Law*. Article 177 of the *Criminal Procedure Law* allows discretionary non-prosecution for minor offenses with statutory penalties of less than three years. Article 37 of the *Criminal Law* provides that minor criminal offenses not requiring penalties may be exempt from punishment. These provisions grant the procuratorate discretion in deciding whether to prosecute cases that do not require criminal penalties or may be exempted from

punishment. The flexibility inherent in discretionary non-prosecution allows it to serve as an important vehicle for the procuratorate's social governance function. Essentially, compliance-based non-prosecution falls within the scope of conditional non-prosecution, achieving the effect of conditional non-prosecution with compliance requirements.

2.4 Corporate Compliance Rectification and Third-Party Oversight as System Safeguards

The primary objective of the compliance-based non-prosecution system is to encourage enterprises to operate lawfully and in compliance with regulations. Non-prosecution is contingent upon the effective implementation of the compliance commitments made by the enterprise involved. Traditional criminal penalties with a punitive deterrent focus have proven insufficient for effectively addressing corporate crime, thus giving rise to the compliance-based non-prosecution process. To achieve lenient treatment and ultimately avoid prosecution, enterprises within this program must establish feasible compliance plans and conduct effective compliance rectification. Compliance rectification for the enterprise involves developing a specialized compliance rectification plan, enhancing internal governance structures, and more.

To ensure effective implementation of compliance rectification by enterprises, the compliance-based non-prosecution system includes a mechanism for third-party oversight. This oversight is conducted by third-party supervision and evaluation organizations composed of professionals such as lawyers, accountants, and tax advisors, who supervise the enterprise's compliance process. Initially, the third-party organization evaluates the feasibility, effectiveness, and comprehensiveness of the enterprise's static compliance plan, offering feedback for amendments and establishing the compliance observation period. Additionally, they conduct periodic or ad hoc assessments of the enterprise's compliance progress during the observation period. Upon completion of the observation period, the third-party organization performs a comprehensive evaluation of the effectiveness of the enterprise's specialized compliance rectification plan and related compliance management systems. The conclusions of these evaluations serve as critical reference points for the prosecutorial authority in its final discretionary decision-making.

Through compliance rectification and third-party supervision, the compliance-based non-prosecution system enables enterprises involved in criminal cases to address systemic gaps, rectify management vulnerabilities, and strengthen governance structures, thereby reducing the likelihood of future violations or similar criminal conduct.

3. Examination of the Applicability of Compliance-Based Non-Prosecution for Tax Compliance in the Greater Bay Area

3.1 Constraints on the Initiation of Compliance-Based Non-Prosecution in Tax Cases

3.1.1 Sentencing Characteristics in Tax Cases as a Limiting Factor

The sentencing characteristics of tax-related cases restrict the initiation of compliance-based non-prosecution. Tax compliance in criminal cases intersects the fields of tax law and criminal law, and common offenses include tax evasion, fraudulent issuance of VAT invoices, and fraudulent claims for export tax rebates, with the fraudulent issuance of VAT invoices being the primary offense. Both fraudulent issuance of invoices and tax fraud are considered serious crimes. Prior to the issuance of the *Interpretation on Several Issues Concerning the Application of Law in Handling Criminal Cases Endangering Tax Administration* by the Supreme People's Court and the Supreme People's Procuratorate, cases involving amounts over 2.5 million RMB were subject to a minimum sentence of 10 years. During the review and prosecution phase, procuratorial authorities generally do not initiate compliance rectification procedures for cases that may result in sentences of over 10 years. The legal basis for compliance-based non-prosecution in minor cases stems from Article 177 of the *Criminal Procedure Law* and Article 37 of the *Criminal Law*, which allow discretionary non-prosecution in minor criminal cases.

Since the launch of the compliance reform pilot program, decisions for compliance-based non-prosecution in tax cases have consistently cited the provisions on discretionary non-prosecution in these two laws as their legal foundation. Although national guidelines do not explicitly exclude serious crimes from compliance procedures, early pilot cases suggest that non-prosecution is largely applied to minor offenses. In the absence of explicit guidance and without a clear legal basis, initiating compliance procedures for serious crimes poses a judicial risk for procuratorial authorities. Publicly available tax compliance non-prosecution cases generally involve tax amounts between 100,000 and 500,000 RMB, with a few cases exceeding one million RMB, but usually less than 2.5 million RMB. These cases typically involve mitigating factors such as voluntary surrender, tax repayment, and admission of guilt. In some regions, serious tax offenses with statutory penalties of 10 years or more are addressed through a compromise approach: the enterprise is exempted from prosecution, while the corporate executives are prosecuted. However, this method fails to meet the intended purpose of compliance-based non-prosecution, which is to protect private enterprises and entrepreneurs. The nine-department guideline explicitly states that the non-prosecution procedure applies to both enterprises and individuals, and a bifurcated approach does not achieve the goal of safeguarding private entrepreneurs by avoiding unnecessary arrests and prosecutions, thereby ensuring the normal operations of private enterprises.

As of March 20, 2024, the newly enacted *Interpretation on Several Issues Concerning the Application of Law in Handling Criminal Cases Endangering Tax Administration* raised the threshold for serious tax crimes in invoice fraud cases, increasing the threshold for sentencing to 10 years from a tax amount

of 50,000 RMB to 100,000 RMB, and redefining serious cases as those involving amounts of 5 million RMB rather than 2.5 million RMB. These adjustments significantly reduce the proportion of invoice fraud cases classified as serious crimes, facilitating the initiation of compliance procedures. However, in the Greater Bay Area, particularly in Guangzhou and Shenzhen, a significant proportion of invoice fraud cases still involve amounts exceeding 5 million RMB.

Historical Context of Severe Penalties in Invoice Fraud and Tax Fraud. Since invoice fraud and tax fraud were incorporated into the *Criminal Law* in 1997, the maximum statutory penalty for both offenses has been the death penalty, reflecting a period when strict punishment was necessary to combat significant threats to national tax revenues. Although the *Criminal Law* has undergone several amendments, the maximum penalty for these offenses remains life imprisonment. More importantly, sentencing for invoice and tax fraud offenses is based on the invoiced amount rather than the actual tax amount defrauded, meaning the invoiced amount may not reflect the actual extent of tax fraud. The current sentencing criteria for invoice fraud and tax fraud offenses are somewhat outdated, with penalties disproportionately severe compared to the nature of the crime. Given that criminal legislation does not explicitly define the constitutive elements of invoice fraud, and that the protected legal interests in such cases remain ambiguous, evaluating the conditions for compliance-based non-prosecution of tax-related offenses solely through traditional minor-major crime standards is unfair to enterprises involved. As economic and social conditions evolve, as well as the purposes behind invoice fraud, a historical perspective should be taken into account when considering the applicability of compliance-based criminal procedures in cases of invoice fraud and tax fraud.

3.1.2 The Precondition of Guilty Plea as a Constraint on the Applicability of Procedures in Tax Cases

One of the conditions for the application of the compliance-based non-prosecution procedure is that the enterprise and its representatives must plead guilty and accept punishment. In tax-related offenses, the primary consequence for the enterprise and its responsible individuals is the loss of tax revenue for the state. When applying for compliance-based non-prosecution, the procuratorial authorities will consider whether the enterprise has fully paid the outstanding tax, late payment fees, and fines. However, in practice, a significant portion of cases involving tax evasion or the issuance of fraudulent invoices arise from genuine transactions in which the enterprise is unable to obtain the required VAT invoices for tax deductions, rather than from the intent to gain substantial profits. Additionally, some cases of invoice fraud involve enterprises that act as intermediaries to issue invoices for others, often for a small “invoice issuance fee,” without reducing the actual tax payable.

Despite this, the amount of late fees and fines in tax-related offenses is typically high, making it challenging for small and micro-enterprises to fulfill these requirements. According to China’s *Tax Collection and Administration Law*, late fees are charged daily at a rate of 0.05% of the overdue tax amount. Administrative penalties for tax violations generally range from 50% to 500% of the tax amount, as specified by this law. Furthermore, the *Invoice Management Regulations* establish administrative penalties for all invoice-related violations, with penalties based on the total invoiced

amount rather than the tax amount involved. In Guangdong Province, for instance, the discretionary standards for invoice-related violations in the tax system specify fines between 300,000 and 500,000 RMB for cases where the total invoiced amount exceeds 1 million RMB. Although the forthcoming *Central and Southern Regional Tax Administrative Penalty Discretionary Standards* will reduce the penalty threshold to 200,000 RMB, the upper limit remains unchanged (Note 1). At the standard VAT rate, an enterprise with a fraudulent tax invoice amounting to 100,000 RMB would reach a total invoiced amount of 1 million RMB, resulting in penalties that are disproportionate to the degree of violation. The high costs associated with late fees and fines make it difficult for many enterprises to bear the financial burden, thus constraining the initiation of compliance procedures in tax-related cases.

3.2 Inadequate Compliance Observation Period and Its Impact on Tax Compliance Rectification

3.2.1 Compliance Observation Period Restricted by Criminal Procedure Timelines

The timelines of criminal procedure constrain the observation period for compliance rectification. Once the People's Procuratorate approves a non-prosecution application for compliance by an enterprise, the enterprise must submit one or more specific compliance plans to the third-party organization, specifying a commitment timeline for completion. As the compliance reform policy has not yet received legislative authorization from the National People's Congress Standing Committee, the criminal compliance process for enterprises in current pilot programs is considered part of the prosecutorial review process. Consequently, the compliance observation period set by the Procuratorate is subject to the review and prosecution timeline specified in the *Criminal Procedure Law*, meaning that the compliance observation period generally cannot exceed the prosecutorial review period.

According to China's *Criminal Procedure Law*, the maximum review period for prosecution is 45 days. Even with two possible extensions for supplementary investigation by the public security authorities, the maximum review period is six and a half months. In typical cases published by the Supreme People's Procuratorate, the longest compliance observation period is six months, and the shortest is two months. For available tax compliance non-prosecution decisions in the Greater Bay Area, many cases lack clear information on the compliance observation period. Given that the compliance observation periods are generally short, most enterprises find it challenging to achieve meaningful compliance and are often only able to fulfill the formal requirements on paper.

In cross-border cases, the compliance observation period may need to be extended. For example, in cases involving fraudulent issuance of VAT invoices under the "two-invoice system" in the pharmaceutical industry, companies transition from "low-invoice" practices to "high-invoice" practices. Previously, intermediary companies in the chain would issue invoices that created "sales expenses" or "commercial bribes." However, under new practices, pharmaceutical companies now issue service, consulting, or advertising invoices through affiliated pharmaceutical consulting companies to offset the impact of "high-invoice" transactions. Many of these consulting firms are essentially subsidiaries of the pharmaceutical companies. Given the Greater Bay Area's unique position, if an enterprise and its affiliated companies operate across the three jurisdictions within the area, compliance observation

becomes more complex. Short observation periods are evidently inadequate for such enterprises to meet the required standards of compliance rectification.

3.2.2 Specialized Nature of Tax Compliance Rectification

Tax compliance rectification in enterprises involves addressing numerous specific elements to mitigate and prevent tax violations. Key areas of tax compliance risk include dual-contracts, off-the-books accounts, commingling of public and private funds, separation of invoices and goods in transactions, misuse of general invoices for pre-tax deductions, and abuse of tax incentives. Accounting violations and tax violations are often interlinked and difficult to separate completely. Consequently, tax compliance is inherently based on accounting compliance, and a tax compliance management system must be built upon a foundation of accounting compliance.

The *Compliance Case Handling Manual for Enterprises Involved in Criminal Cases* by the Supreme People's Procuratorate provides a model compliance rectification plan for small enterprises involved in fraudulent issuance of VAT invoices, illustrating the integration of financial and tax compliance. The plan includes three main sections: identification and assessment of criminal tax-related legal risk points, establishment of a specialized tax compliance management system, and system application. The risk identification and assessment section lists 16 risk points. The specialized tax compliance management system covers six parts: roles and responsibilities of compliance management, risk identification and monitoring, violation response and compliance improvement, and guidelines for tax compliance management. The system encompasses detailed requirements for organizational structure, departmental management, company bookkeeping, procurement and reimbursement management, warehouse management, and ERP financial system management. Additionally, the sample compliance management system includes specific policies for tax risk management, financial management, and invoice management.

In essence, tax compliance rectification for small enterprises becomes a systematic corporate governance project. However, in the compliance management implementation plan's timeline, all the above rectifications are scheduled to be completed within five months. Such an extensive corporate governance effort is challenging for small and medium enterprises (SMEs) to implement effectively within the allotted time. Other limitations in SMEs, beyond time constraints, may also hinder them from achieving substantive compliance. A search of Guangdong Province's tax compliance non-prosecution decisions in the Alpha database indicates that most cases involve SMEs. However, these decisions generally lack information on the compliance rectification process. Given the Supreme People's Procuratorate's extensive compliance guidelines, SMEs without the resources for comprehensive compliance implementation may struggle to achieve even basic paper compliance. These issues ultimately impact the intended goals of compliance-based non-prosecution, reducing the preventative effectiveness of compliance rectification.

3.3 Ambiguities in the Evaluation Mechanism and Their Impact on Achieving Compliance Rectification Objectives

3.3.1 Ambiguity in Evaluation Bodies

According to national-level guidelines, upon the completion of the compliance observation period, third-party organizations are responsible for conducting a comprehensive review, evaluation, and assessment of the final compliance outcomes of the enterprises involved in criminal cases. The results of these evaluations serve as an important reference for the People's Procuratorate in making final decisions. Based on publicly available information, the professional personnel within third-party organizations for compliance assessment in Guangdong Province largely consist of practitioners from law firms, accounting firms, tax advisory firms, universities, or specialized consulting companies, with very limited representation from administrative agencies, and virtually no participation from professionals within tax authorities. This composition issue also exists within local third-party organizations in Shenzhen and other mainland cities in the Greater Bay Area.

In tax compliance rectification for enterprises, it is necessary to cease all tax-related violations, as well as pay outstanding taxes, late fees, and fines. Determining whether these actions have been properly implemented requires confirmation from tax authorities. The process also involves the imposition of criminal fines by the procuratorial authorities during the prosecution review phase, raising issues regarding the principle of "no double punishment" (*nonbis in idem*) and the coordination between the tax and judicial authorities. The supervision of tax compliance rectification should ideally be jointly conducted by both procuratorial and tax authorities. Therefore, the absence of tax authorities within the evaluation bodies hampers effective communication and implementation of compliance rectification efforts.

3.3.2 Ambiguity in Evaluation Standards

While the offenses involved in tax-related cases and the focus areas of compliance rectification vary, tax compliance still requires an integrated approach to financial and tax compliance. Currently, neither national-level guidelines nor available information on compliance in non-prosecution cases provide specific standards for granting lenient treatment through non-prosecution when an enterprise achieves compliance through a guilty plea and rectification. Additionally, there is no guidance on whether partial compliance achievement would result in different levels of rectification incentives. Enterprises that consider applying for compliance rectification lack a clear basis for estimating the costs and anticipated outcomes of rectification, the level of incentives they might receive for rectification, and the potential litigation interests they would forfeit by choosing compliance rectification.

The determination of whether an enterprise's compliance rectification meets the necessary standards is solely evaluated by the third-party organization after the observation period concludes. However, the lack of predefined, specific standards and tiered incentives for varying levels of rectification completion may lead to arbitrary and uncertain evaluations of compliance outcomes. In the Greater Bay Area, the entities involved in tax-related cases are mainly small and medium enterprises (SMEs), which

often have limited financial resources. If the anticipated incentives for compliance rectification are not realized, these enterprises may forfeit the litigation benefits they might have obtained while also incurring significant costs for unpaid taxes, late fees, and fines. This situation not only hinders the achievement of compliance rectification goals but also adversely affects the continued operation of these enterprises.

3.3.3 Post-Evaluation Supervision

The ambiguity in evaluation mechanisms is a common issue within the compliance-based non-prosecution framework and also applies to tax compliance non-prosecution in the Greater Bay Area. According to the *Review Measures* issued by the Nine-Department Office, if an enterprise's compliance construction meets the effectiveness standard, the People's Procuratorate may refer to the evaluation conclusions to decide on non-prosecution, propose lenient sentencing, or issue prosecutorial recommendations for lenient treatment or disciplinary action to the relevant authorities.

However, even if an enterprise obtains a non-prosecution decision based on effective compliance rectification, it is still uncertain whether the compliance plan can be effectively integrated into the enterprise's management system, transitioning from a formal compliance plan to a practical, ongoing governance mechanism. Without sustained external supervision, achieving a true culture of compliance within the enterprise and preventing recidivism remain challenging, thereby undermining the overall effectiveness of compliance-based non-prosecution.

4. Integrated Pathways for Compliance-Based Non-Prosecution in Tax Cases within the Greater Bay Area

4.1 Establishing a Jointly Led Compliance Procedure by Courts and Procuratorates for Tax-Related Criminal Cases

Currently, the compliance-based non-prosecution system in China is still in an exploratory phase, with the nine-department *Guiding Opinions* not yet involving the People's Courts, and the compliance non-prosecution process primarily occurring during the prosecution review phase. However, in principle, a checks-and-balances structure exists between the judiciary and the procuratorate, forming a triangular relationship among prosecution, defense, and adjudication, which balances power. Allowing the procuratorate to exclusively control the compliance-based non-prosecution process interrupts the information flow during the prosecution review phase, leading to an expanded scope of prosecutorial discretion that disrupts the balance among the parties involved.

The involvement of courts in criminal compliance procedures could resolve these issues and broaden the applicability of criminal compliance in serious cases. In the practice of compliance-based non-prosecution reform, criminal compliance procedures are gradually extending into the courts, with some local courts and procuratorates jointly establishing procedural rules for compliance-based non-prosecution. This allows enterprises involved in criminal cases to apply for compliance at the trial stage if they have not done so during the prosecution review phase. Given the nature of tax-related

criminal cases, which frequently involve serious offenses, extending the compliance procedure beyond the prosecution review phase can facilitate more thorough compliance rectification by the enterprises involved, potentially leading to reduced penalties or even acquittals at trial. The longer timeline of the trial phase also provides enterprises with more time to prepare payments for taxes, late fees, and fines.

The *Court of Second Instance* decision in a case involving a construction company in Wuhu, Anhui Province, where an enterprise and its controller submitted a compliance rectification application and completed rectification during the appeal stage, ultimately exempted the enterprise from criminal penalties. This case offers a valuable reference for designing a tax compliance non-prosecution framework within the Greater Bay Area.

In a joint compliance procedure for tax-related criminal cases in the Greater Bay Area, specific standards for division of labor and cooperation should be clearly established. Three main categories of cases should be targeted: (1) serious cases with significant amounts at stake, where the enterprise has submitted a compliance application and achieved rectification at the prosecution review phase, but is still prosecuted due to the severity of the offense; (2) cases where the enterprise submitted a compliance application and prepared a compliance plan during the prosecution review phase, but failed to meet the compliance standards due to financial constraints preventing timely payment of taxes, late fees, or fines; and (3) cases where the enterprise has shown no intent for rectification at the prosecution review stage but submits a compliance application at trial.

For the first two types, the procuratorate should take the lead, and once the case reaches court, leniency should be applied as stipulated. For the third type, the court should assume primary responsibility. The core concept of enterprise compliance reform is co-governance; regardless of the leading party, third-party organizations should be engaged, with the lead party reviewing their assessment conclusions to provide a final evaluation of the effectiveness of compliance rectification. Tax authorities should play a central role in compliance assessment, either as members of the third-party organization or as administrative authorities, to provide professional oversight of compliance rectification plans and outcomes. This collaboration between the courts, procuratorate, and tax authorities would enable a thorough assessment of enterprises involved in tax-related offenses, emphasizing both punishment and prevention, and promoting the standardized development of small and medium enterprises (SMEs) in the Greater Bay Area.

4.2 Establishing a Dual System of Compliance-Based Non-Prosecution Types to Match the Severity of Offenses

As previously discussed, the legal basis for compliance-based non-prosecution can be traced to discretionary non-prosecution under Article 177 of the *Criminal Procedure Law* and exemptions from criminal punishment under Article 37 of the *Criminal Law*, both of which apply only to minor offenses. Most legal scholars argue that non-prosecution for serious crimes may violate the principle of legality and could be viewed as a form of leniency that tolerates criminal behavior. While some compliance practices have extended to non-prosecution for serious crimes, certain local jurisdictions restrict

compliance rectification in cases where the statutory sentence exceeds ten years.

In tax-related criminal cases, serious crimes are often handled separately in practice. For example, in a case involving a company that issued fraudulent VAT invoices, causing over 1.2 billion RMB in tax losses to the state, the procuratorate prosecuted several individuals directly responsible while simultaneously initiating a conditional non-prosecution process for the company. Fraudulent VAT invoice cases are prevalent in tax-related criminal cases, and sentencing is often based on the invoiced amount rather than the actual tax loss, meaning the invoiced amount does not necessarily reflect the true financial harm to the state. Therefore, a tax compliance non-prosecution framework in the Greater Bay Area should consider the social harm of each case, establishing a dual system of discretionary and conditional non-prosecution to match the severity of the offense.

Specifically, the framework should: (1) establish threshold tax amounts for discretionary and conditional non-prosecution based on the characteristics of tax-related cases in the Greater Bay Area, and refine the criteria for applying compliance-based non-prosecution. Discretionary non-prosecution should apply to minor tax-related offenses, while conditional non-prosecution should apply to more serious cases involving larger tax amounts. For VAT invoice fraud, the applicable type of compliance-based non-prosecution should be determined based on the extent of harm to state tax revenue rather than the sentencing standards defined in the *Criminal Law*; (2) link the conditions for the two types of compliance-based non-prosecution to the effectiveness of the enterprise's tax compliance rectification, applying the corresponding type of non-prosecution according to the level of compliance achieved. This structure addresses the limitations of a single discretionary non-prosecution model, which is particularly suited to cases involving large tax amounts; and (3) for cases where compliance rectification is initiated at trial, or cases where compliance rectification remains incomplete within the observation period set during the prosecution review phase but shows progress by the trial phase, the court could incentivize the enterprise by imposing a non-custodial penalty.

In sum, the procedural differentiation in non-prosecution types enables tax-related enterprises in the Greater Bay Area to pursue tailored tax compliance rectification, offering them an opportunity for renewed development. The application of discretionary non-prosecution does not inherently require participation in a compliance system, but linking compliance-based non-prosecution with conditional non-prosecution aligns with the internal logic of the system itself.

4.3 Establishing a Unified Standard for Compliance Rectification to Integrate Governance and Prevention

Enterprise compliance reform not only emphasizes protection of private enterprises but should also focus on punishment and crime prevention. However, in practice, the lack of clear sentencing incentives, inadequate observation periods, and vague evaluation standards for compliance rectification have limited the effectiveness of compliance reform. Given the technical complexity of tax compliance rectification, a pathway focusing on “compliance risk identification, specialized compliance management, and targeted management elements” should be established. In light of the large number of

SMEs in the Greater Bay Area and the fact that tax-related enterprises are often small or micro-sized, a risk-based tax compliance management system tailored to SMEs is necessary. Small and micro enterprises, in particular, tend to have less mature management systems and are therefore more prone to tax-related violations.

The Greater Bay Area should design specific measures targeting the root causes of criminal conduct, aiming to eliminate systemic risks by incorporating basic compliance elements, establishing compliance departments, appointing compliance officers, and improving internal management. On this foundation, specialized tax compliance elements should be developed:

(1) Establish a Tax Compliance Risk Identification System. Identify high-risk fields associated with tax-related offenses, including VAT fraud, tax evasion, and fraudulent export tax rebates, to focus on specific risks that could lead to repeated offenses. Risk identification should cover areas such as off-the-books accounts, separation of invoices and goods in transactions, and general invoice deductions, with general guidance and key risk factors outlined.

(2) Introduce Differentiated Tax Compliance Management Elements. Tailor compliance management based on the size of the enterprise, the offense, and its severity, incorporating training, communication, and anonymous reporting mechanisms to prevent recurring issues. Guidelines should also allow the compliance observation period to exceed the prosecution review period for serious cases, ensuring adequate time for effective rectification.

(3) Establish a Graded Standard for Compliance Rectification Effectiveness. Implement a three-tier grading system (fully compliant, partially compliant, non-compliant) for enterprises based on compliance achievements, with each tier linked to corresponding sentencing incentives. Only enterprises achieving full compliance would receive the final incentive of non-prosecution.

(4) Sign a Tax Compliance Agreement Between Third-Party Organizations and Enterprises. Following the compliance observation period, third-party organizations, along with tax authorities, should assess the compliance level achieved by the enterprise. This would mitigate arbitrary evaluations, allowing enterprises to estimate the costs and outcomes of compliance rectification, thereby improving the likelihood of successful rectification.

4.4 Establishing a Collaborative Mechanism for Tax Compliance across the Greater Bay Area

The integration of cross-border transactions within the Greater Bay Area has promoted coordination among tax systems, yielding notable progress. While compliance-based non-prosecution reform does not directly apply to the special administrative regions (SARs), the mainland's policies indirectly influence them. The tax system differences among the three regions affect the recognition and handling of tax violations, and the variances in tax administration impact procedural responses to tax offenses.

Given the Greater Bay Area's distinct legal framework, a collaborative tax compliance mechanism is necessary to address shared challenges in fraudulent VAT issuance and tax evasion. Key components of this mechanism include:

(1) Cross-Border Jurisdictional Cooperation for Tax Violations. Establish unified jurisdictional arrangements for tax violations committed by mainland enterprises in SARs and vice versa.

(2) Collaborative Oversight Following Compliance-Based Non-Prosecution Initiation. In cross-border cases under mainland jurisdiction, third-party organizations evaluating compliance rectification should work closely with SAR tax and judicial authorities.

(3) Mutual Recognition Mechanism for Investigations of Tax Violations across Judicial Systems. Facilitate data sharing and mutual recognition of case files, evidence, and transferred cases among the three regions to improve efficiency.

(4) Establishing a Tax Data Center for Cross-Border Compliance Monitoring. Develop a monitoring platform using big data to oversee tax compliance across cross-border enterprises, guiding compliant operations and ensuring the rehabilitative effects of compliance-based non-prosecution.

5. Conclusion

As a vital component of China's industrial layout, the Greater Bay Area plays a critical role as both an economic growth engine and a hub for reform and innovation. Unifying tax compliance-based non-prosecution standards across the Greater Bay Area would enhance tax compliance governance for enterprises, strengthen sustainable development for private enterprises, and provide a model for national application. With the extension of compliance procedures to the trial phase, enterprises can achieve mitigated sentencing through tax compliance rectification even if they do not obtain non-prosecution during prosecution review. As the Greater Bay Area has a high incidence of tax-related criminal cases among SMEs, only an integrated tax compliance system can ensure consistent standards, prevent disparate treatment, and reinforce judicial authority in tax compliance cases.

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Note

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