China’s creation of a National Supervisory Commission, passed into law on 20 March 2018, marks the birth of a powerful new state body with broad powers to tackle bribery and abuse of office throughout the public sector. This potentially spells a major change in the legal and regulatory landscape for foreign companies and investors operating in mainland China. In the near term, this could constitute an increase in risk as the scope of anti-corruption investigation and enforcement changes, and potentially broadens, considerably. However, the Commission’s establishment may also spell a move towards an institutionalization of President Xi Jinping’s anti-corruption drive. This may justify cautious optimism if the changes resolve some of the uncertainty associated with Xi’s campaign in the medium to long term.

The National Supervisory Commission will oversee a network of local supervisory commissions across the country, three of which have been operating since late 2016 under pilot programs in Beijing, Shanxi and Zhejiang. Its establishment will effectively transform what has been a two-track anti-corruption regime into a single-track system overseen by the Commission. Under the previous two-track regime, the Central Commission for Discipline Inspection (CCDI) – the Chinese Communist Party’s internal watchdog – investigated corruption within the party under a remit of handling “discipline violations”, as outlined in the Chinese Communist Party constitution. The Supreme People’s Procuratorate, China’s state prosecutor, has meanwhile overseen the investigation of corruption that fell outside the CCDI’s remit, as well as prosecuting cases investigated both by the CCDI and by provincial and local procuratorates across the country.

The National Supervisory Commission is expected to combine the anti-corruption resources of the CCDI with the investigative and prosecuting functions of the Procuratorate. The Commission will investigate corruption throughout the public sector, including, for example, employees of public educational institutions and industry associations. It is also expected to have an increased focus on the source of corrupt payments, rather than mainly investigating the officials receiving them, as has been the primary focus until now. Public sector corruption that fell outside the CCDI’s purview was previously investigated by the procuratorates and many expect the establishment of the Commission to herald an intensification and expansion of such investigations.

In addition to handling both investigations and prosecutions, the Commission will have the power to enforce corruption-related orders, issue subpoenas, detain suspects and freeze assets. Such powers were
previously held by other institutions, including law enforcement and the Procuratorate. The Commission is also expected to remove some inefficiencies associated with the outgoing system, such as inconsistent rules on the admissibility of evidence between the CCDI and the Procuratorate.

The establishment of the Commission has been cast by the Communist Party as representing an institutionalization of Beijing’s anti-corruption campaign, which until now has been characterized by its ad hoc and campaign-driven nature. This is a shift that has been discussed for years and it has long been widely recognized that China’s anti-graft system needs to be more institutionalized. However, given the Commission’s broad powers and few signs it will be any more transparent than its predecessor, it remains to be seen what implications this purported institutionalization will have for foreign companies other than perhaps further limiting the opportunity for local officials to influence investigations internally.

The establishment of the National Supervisory Commission and what is essentially a broadening and streamlining of China’s anti-corruption drive means firms doing business or investing in China will urgently need to review aspects of their mainland Chinese operations. Whilst the Commission is not charged with investigating people in the private sector, foreign companies are at increased risk of being implicated if some aspect of their China business falls within the purview of an investigation into a public servant. Furthermore, the expected shift in focus to the source of corrupt payments means that if any third parties are engaged in corrupt behavior in their conduct on behalf of a company, there is an increased risk that the company itself will be held liable. This may be the case even if the firm is wholly or partially unaware of such behavior. Even companies that consider themselves to be operating strictly by the book would be wise to consider whether any of their current ways of doing business – in particular the engagement of third parties – could be interpreted as bribery under the new Commission.

Much remains to be seen regarding how the new Commission will operate, who it will target and how it will change the compliance environment for foreign firms operating in China. In the short term, it may constitute a degree of additional anti-corruption risk, primarily due to investigations being conducted differently and under an expanded purview. Such a shift could prove disruptive until it becomes clear specifically what has changed.

Foreign entities will need to closely monitor how the new changes play out and how anti-corruption investigations and enforcement differ under the Commission from the way they have been conducted until now. It also means that there is greater need than ever for companies to conduct meaningful and in-depth due diligence into their business partners, agents and other third parties. There is, however, room for cautious optimism that once overseas companies and investors have adapted to the new regime, the Commission could mark a move towards an institutionalization of China’s crackdown on graft. If so, it could make navigating anti-corruption laws and regulations more systematic and more predictable.

Nothing is foolproof, but the right mixture of prevention and sustained vigilance will go a long way towards keeping predators at bay—and out of the corner office.

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About our firm

Nardello & Co. is a global investigations firm with experienced professionals handling a broad range of issues including the FCPA/ UK Bribery Act and other corruption-related investigations, civil and white collar criminal litigation and arbitration support, asset tracing, strategic intelligence and political risk assessment, computer forensics, and reputational due diligence. Our clients include the world’s leading law firms and financial institutions, Fortune 500 and FTSE 100 companies, high-net-worth individuals and family offices, governments, NGOs, sports organizations and academic institutions. With offices in New York, London, Washington DC, Atlanta, Hong Kong, Tokyo, Milan and Dubai, Nardello & Co.’s professional staff includes former US federal prosecutors, US and international lawyers, former general counsels of multinational corporations, former cyber-crimes law enforcement, senior officials from the US Department of Homeland Security and intelligence operatives, licensed investigators, research analysts, journalists, financial crime specialists, forensic accountants and computer forensic experts.

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