

# Managing Corruption and Fraud Risks

*...with Chinese Characteristics*



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## The Environment ....

- *To Get Rich is Glorious!* 让一部分人、一部分地区先富起来
- Moral value and business ethics not part of education system
- Monopoly of power – selective enforcement
- Lack of media ‘oversight’ – minor improvement in recent years
- Law enforcement doesn’t prioritize ‘white collar’ issues
- Importance of ‘*guanxi*’ and ‘face’
  - *And Fear ...* The hesitation to report someone doing something wrong



### But 'it takes two to tango'....

Behavior of multinationals in the world's fastest growing market leaves them open to malfeasance

- Policies & training take back seat to recruitment / growth / profits
- You can't enforce a policy staff are not conversant with!
- Poor internal controls – *the chop*
- High turnover in outside managers – managing 'up'
- No screening of staff, vendors, etc.
- Empower local employees with limited experience and relatively low salaries
- Aggressive targets

# China Risks

## The 3 'C's that keep China managers awake at night....

**Corruption**

**(Official &  
Commercial)**

**Compliance  
&  
Conflicts of Interest**

*PRC AUTHORITIES / COURTS ARE OFTEN LITTLE USE IN ADDRESSING THESE ISSUES, AS THEY ARE OFTEN SIMPLY VIEWED AS INTERNAL COMPANY CONTROL / MANAGEMENT ISSUES*



# Corruption – Commercial

- To some extent, kickbacks are a basic local business norm - “everyone wins” attitude
- Rarely subject of successful legal action – authorities view them as internal company control issues
- Most common in purchasing department heads and other decision maker roles
- Also found in HR, Finance, Sales....to a greater or lesser extent
- Function of lax legal environment, lack of internal oversight & relatively low salaries
- MNCs that wish to combat commercial corruption must provide extensive ethics codes, re-train employees, establish complaint mechanisms, and take deliberate action against transgressions



## Actively Protecting Corporate Interests in China

EMPLOY

**Screen** – staff, partners, vendors...no such thing as too much diligence

THE

**Train** – intensively ‘re-educate’; create an ethical expectation from outset ...while always keeping cultural and local legal differences in mind

“S.T.A.R.S.”

**Audit** – financial, compliance & general security records and practices

CONCEPT

**Repeat** – whenever problems or doubts surface, repeat above steps once more

**System** – have a robust compliance system involving ethics codes, hotlines, disclosure rules, etc.

# Case Study

- **Problem:** Allegations senior management had been receiving kickbacks
- **Solution:**
  - lifestyle analyses of the four employees named in the letters;
  - a forensic audit of the employees' computer hard drives
  - and comprehensive background checks of supplier companies believed to have retained links with a senior manager previously dismissed for receiving kickback payments.
- **Result:** Identification of non-disclosed investment by two senior managers and identification of collusion with suppliers
- **Subsequent implementation of an internal controls system, including :**
  - random discreet external audits of existing suppliers;
  - background checks on new suppliers and new senior management;
  - publicizing fraud/compliance hotlines;
  - ethical training workshops to increase staff and management awareness of relevant regulations.

# An international consultancy

