China: The Corruption Problem Child

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If your company operates in China, I have one piece of "free" advice – conduct an anti-corruption audit and do it now.

Almost one-third of the FCPA criminal cases involve bribery in China. The scenarios are very familiar: a US company enters into a joint venture with a Chinese partner, or a US company establishes (or acquires) a Chinese subsidiary.

Bribery is built into the Chinese economy. It is a remnant of the communist system in which bribery or the "black" market was a way of life. Government employees expected and demanded bribery to provide basic services and/or products. That same mentality pervades the Chinese economy. Foreign companies are attracted to China for lucrative profits. But entrance and operation in the Chinese economy requires bribery of government officials.

Foreign companies entering into China get caught up in bribery in several typical scenarios:

1. **State-Owned Enterprises** – Approximately 70 percent of China's wealth is owned by the Chinese government. In some cases, the government's ownership is hard to identify. In the health care sector, almost all hospitals are owned by the government and every employee at the hospital is a "foreign official" under the FCPA. The pervasive role of the government in the economy means that companies have to be extremely careful when dealing with Chinese companies and customers to make sure that there is no government ownership, and if there is government ownership, making sure that no improper payments are made to "foreign officials."

2. **Bribery of Public-Private Joint Ventures** – The Chinese government, through state-owned enterprises, is involved in numerous joint ventures with foreign companies, many of which involve significant industries such as automobiles and oil/energy. Foreign companies that supply the joint venture have to be careful because purchasing by the joint venture usually involves layers of public-private employees, and expectations of payments for products to be considered, evaluated and ultimately recommended for purchase by the joint venture.

3. **Gift Cards** – China thrives on the exchange of gifts and especially gift cards. These are not the $25 Barnes and Noble variety but tend to be more significant – anywhere from $100 to $5000 equivalents. Chinese sales staff know that they need to distribute gift cards to government customers and they frequently do so without regard to anti-corruption controls. Chinese managers know that foreign companies will focus on this practice. It is an issue of immediate concern for any foreign partner in China and an area ripe for bribery. Compliance officials needs to tackle this issue and gain control of the gift card process. Chinese managers and employees resist such controls because they know that such gift giving is essential to business. They need to understand that compliance officers

are not out to end the practice but to gain control, protect the company and document the compliance steps need to ensure compliance.

4. **Pre- and Post-Merger Compliance** — many companies enter China by acquiring a local company. It is a high risk move because bribery may be part of the existing business operation. It is a real challenge to change that mentality. If a company acquires a local Chinese company, it must be aggressive in changing that culture through training, communication and close supervision of local oeprations. It is not acceptable to depend on existing internal controls — a China-specific program is needed to make sure there are no easy ways to obtain money for bribes or gift cards.

China is a challenge. Any company that is operating in China is either ignoring potential violations or working diligently to devise and implement meaningful anti-corruption controls.