Corruption War

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Mak Yuen Teen

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The cases in this publication were developed from published sources solely for class discussion and are not intended to serve as illustrations of effective or ineffective management or governance. The interpretations and perspectives in these cases are not necessarily those of the organisations named in the case, or any of their directors or employees.

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PREFACE

On December 23, 2017, Singapore was shaken by news that Keppel Offshore & Marine (KOM), a wholly-owned subsidiary of Keppel Corporation, had reached a global resolution with criminal authorities in the United States, Brazil and Singapore under which it will pay a US$422.2 million penalty for bribery-related offences in Brazil. The fine was one of the ten largest ever under the Foreign Corrupt Practices Act (FCPA) of the United States.

However, it was not only the size of the penalty that came as a shock. It was also the fact that it involved a government-linked company from Singapore, a country well known for its low level of corruption. Adding to the shock were the revelations that the illegal payments had been going on for 13 years and that they were made with the knowledge or approval of senior KOM executives, some of whom were also senior management in Keppel Corporation.

Since 2012, CPA Australia and I have collaborated in publishing an annual collection of corporate governance case studies which I edit from cases written by BBA (Accountancy) students in my Corporate Governance and Ethics and Corporate Governance and Risk Management courses at the NUS Business School, National University of Singapore. So far, six volumes have been published. Some of these cases involve issues of bribery and corruption (including money laundering). In light of the KOM scandal, I decided to publish a special collection of cases on this topic. Most of these cases have already been published in the six volumes. I have made minor changes to some of them. There are two new cases, both involving Singapore companies. One is the Keppel case. This case is longer than the other cases as I decided to publish the full version rather than the abridged version as we have been doing for other cases. I also wrote substantial parts of this case myself. This case has an earlier companion case, the Petrobras case, also included here. That earlier case was written when Keppel was mentioned as being possibly implicated, but before it truly unravelled for the group. The other new case is the “Fat Leonard” case about bribery involving the U.S. Navy Seventh Fleet and a Singapore-based company.

Unlike the case studies published in the annual case collections, I have decided not to include discussion questions. I thought it is best to have open and free flow discussion of issues around the cases.

In addition to case studies, I have over the years also written several articles on bribery and corruption in The Business Times and on my website. A selection of them has also been included.

I hope you find the cases and articles interesting and useful.

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June 2018

ARTICLES

Beware the Risks from Corruption

By Mak Yuen Teen

Published in the Business Times on 4 September 2009

Over the last few years, governments and businesses around the world have been busy coping with one major risk event after another – financial crises, Sars, tsunami, terrorism, and pandemic flu. Although often ill-prepared for them, the response is usually swift. But perhaps the most insidious risk we continue to face – a kind of background risk – is corruption risk.

As the Chairman of Transparency International puts it:
"In the poorest countries, corruption levels can mean the difference between life and death, when money for hospitals or clean water is in play. The continuing high levels of corruption and poverty plaguing many of the world's societies amount to an ongoing humanitarian disaster and cannot be tolerated. But even in more privileged countries, with enforcement disturbingly uneven, a tougher approach to tackling corruption is needed."

We are much more likely to under-react to corruption risk than to a global financial crisis or a terrorist act. However, "slow-burning" risks such as corruption and climate risks are just as dangerous, and perhaps even more so. The "boiling frog" story provides a good analogy. If a frog is placed in boiling water, it will jump out. However, if it is placed in cold water which is slowly heated, it will not sense the danger and will be cooked to death. Similarly, we will usually react quickly to a financial crisis or a terrorist attack, but we may be slowly boiled to death by corruption risk.

Corporations which have been caught in major corruption scandals would undoubtedly find that illegal behaviour had been occurring over a period of time, without them realising it or appreciating its severity. They may have ticked all the boxes in the Sarbanes-Oxley Act, and other rules and codes, without realising or addressing unethical or illegal behaviour taking place within their organisations.

When I taught an executive MBA course in corporate governance and ethics a few years ago, a senior executive working in a multinational firm shared with me that while his company had a code of ethics which it told its employees to uphold, it also set extremely short-term goals for country management to gain market share and achieve profitability, even in markets where illegal payments were the norm. Given the choice of losing a job or bonus in the short term versus the possibility of being found out for making illegal payments to secure contracts, it is very easy for managers in the field to put profits before ethics. I have heard such stories many times.

According to Transparency International's Corruption Perceptions Index (CPI) 2008, Singapore is ranked No. 4 amongst 180 countries, only behind Denmark, New Zealand and Sweden as having the lowest levels of public sector corruption. However, Singapore does not perform quite so well on another of Transparency International's indices – the Bribe Payers Index (BPI). This index ranks 22 major exporting economies on the propensity of their firms to bribe abroad and for this index, we are ranked only ninth.

Together, the CPI and BPI suggest that while our public sector is largely corruption-free, some of our companies doing business abroad may not be quite so. It is morally wrong to pay bribes. It has serious humanitarian consequences. And increasingly, it is suicidal to do business this way.

Lower ethical expectations

There are signs that we may have lowered our ethical expectations and standards over time. Just consider the unethical business practices of some businesses here – for example, timeshare and those selling electronic products in certain shopping centres in Singapore – which rely on misrepresentation and often harassment to make sales.

I do not recall that it was ever this bad. Since some of our businesses behave this way unchecked here, it seems reasonable to assume that some will behave in similar or worse ways overseas, and that their behaviour will be subject to even less scrutiny.

Ironically, we may be backsliding on ethics at a time when our hard-earned reputation for high ethical standards should pay the most dividends. Globalisation has opened up many opportunities, but has also made risk management more challenging for many companies.

In September last year, New Zealand's largest company, Fonterra, reported that it had to write off NZ$139 million (S$135 million) of its investment in its 43 per cent-owned joint venture, San Lu, for the cost of product recall and loss of San Lu's brand value over the melamine milk powder scandal. In December last year, it was reported that Siemens AG, the German global juggernaut, agreed to pay more than US$1 billion in fines in Germany and the US to settle corruption charges relating to dubious payments to secure business across the company and in several countries.

Recently, Telenor, the Norwegian telecommunications giant, was accused of breaching its ethical procedures because one of the sub-contractors of its subsidiary in Bangladesh was alleged to be using child labour. This may seem a bit like when my third cousin misbehaves, my father gets scolded. There are many examples of multinational companies being caught out by ethical or legal violations, both within their own organisations, or along their supply chains, which nevertheless hurt them.

Whether we like it or not, when it comes to business practices, the "accountability tree" may have more branches than one's family tree, and accountability may extend far wider than one can imagine.

Today, the risks faced by an organisation often reside outside the organisation – with its suppliers, business partners and customers. This, together with regulations such as the Sarbanes-Oxley Act and Foreign Corrupt Practices Act in the US, mean that international companies are changing the way that they manage risks. Indeed, one might even ask if enterprise-wide risk management is wide enough.

It is now increasingly common for multinationals to be concerned about the standard of ethics and compliance of their suppliers and business partners. More have developed supplier ethics policies and incorporated ethical considerations into their supplier qualification systems. Multinationals often impose their codes of conduct on other partners across the supply chain.

Raising standards

This trend can only accelerate. Such developments mean that even unlisted small to medium enterprises which do business with multinationals will need to raise their standards of ethics, governance and compliance.

There are even changes in the way that organisations manage risks with their customers. Of course, most companies would already have procedures to assess the creditworthiness of their clients, but more are adopting more comprehensive risk assessment of their clients, as part of their client acceptance process. Reputable service providers now realise that they have to "choose their customers" because customers also bring risks, beyond credit risk. These risks are perhaps most evident in the case of regulated services such as an independent audit, where audit failures can impose huge financial and reputational damage on the auditor, as in the case of Arthur Andersen in the Enron case.

Consider how one major accounting firm assesses the risk of its clients as part of its client acceptance process. A key factor that is considered in its risk assessment process is the characteristics and integrity of the management of the prospective client. The firm obtains background information on a prospective client for the purposes of determining whether the personal and business reputations of the prospective client and their principal owners and officers are such whom the firm is willing to become associated with.

Where there is a change in principal owners and management of an existing client, such background information is also required to assess whether to continue to accept or retain the client.

Some of the factors which are considered to increase the risk associated with a prospective or existing client include management's involvement with illegal or questionable activities; frequent changes in banks, lawyers, or auditors; significant personal difficulties in the lives of management; management's willingness to accept unusually high levels of risk; recent significant or unexpected changes in management; and inexperienced management.

The nature of the prospective client's business, its organisation and management structure and the business environment in which it operates are some of the other factors considered as part of its risk assessment.

Another professional services firm – not an accounting firm – now requires its consultants to assess the integrity of its clients (in addition to creditworthiness) before deciding whether to take on the client. As part of its client acceptance policy, it requires consultants to assess whether taking on the client could be expected to have a negative impact on the firm's reputation or brand, and also whether the consultant is aware of any investigation or legal action against the client or its management that could have a negative on the firm's reputation or brand.

Risks associated with poor ethics, governance and compliance will threaten the survival of our companies if they do not learn to accept them as part of the new business reality and put in place measures to address them. It's a wave heading towards us and will impact even our small to medium sized companies which do business globally. They either catch this wave and ride over it, or it will sweep them away.

Apple Case Throws Spotlight on Corruption

By Mak Yuen Teen

Published in the Business Times on 26 August 2010

Last year, I wrote a commentary titled ‘Beware of corruption risks’ (BT, Sept 4) where I argued that Singapore companies may not be paying enough attention to corruption risks when they do business overseas and that global companies are increasingly focused on risks residing along the supply chain.

I cited the Bribe Payers Index published by Transparency International, which ranks 22 major exporting economies on the propensity of their firms to pay bribes when doing business overseas, where Singapore was ranked only ninth.

I said that the risks associated with poor ethics, governance, and compliance will threaten the survival of our companies which do business with international companies – including our small- and medium- sized enterprises – if they do not accept them as a new business reality and put in place measures to address these risks.

Recent news reports about the bribery charges and the civil lawsuit against Apple’s global supply manager, Paul Devine, has put the spotlight on three Singapore, and several other, Asian companies which are suppliers of Apple’s iPhone and iPod accessories.

The three Singapore companies identified in the legal action are JLJ Holdings, Lateral Solutions, and Fastening Technology. Paul Devine is accused of colluding with Andrew Ang, a former business development of JLJ’s wholly owned subsidiary, Jin Li Mould Manufacturing Pte Ltd, whereby Mr Devine would provide suppliers with confidential Apple business information to help them win business with Apple in exchange for money. Mr Ang was also indicted in the criminal charges.

While the actions so far are directed against Mr Devine and Mr Ang, and not against the companies, there will undoubtedly be concerns about the processes that these companies have in place for managing corruption risks, which could have a drastic business impact on them.

The stockmarket reaction to the news for JLJ, which is listed on Catalist, provides some indication of the potential business impact (the other two Singapore companies are private companies). On Thursday, Aug 12, the day before the arrest of Mr Devine in the US, the closing share price of JLJ Holdings was 23 cents.

Almost seven million shares were traded that day and more than 25 million shares were traded on the day of his arrest, compared to a daily volume of less than 850,000 shares for the month prior to that. JLJ announced on Aug 16 that its subsidiary had been mentioned in the indictment and civil suit.

By Aug 20, the closing share price had almost halved to 12 cents. The market reaction is not surprising because Apple is a major customer of JLJ. In its offer document dated July 6, 2009, pursuant to its listing, it stated that for FY2008, 'Apple and Apple intermediaries' accounted for 82.5 per cent of JLJ's revenues.

Even if JLJ and the other companies do not directly face legal action, there is a real risk that they could lose not only Apple as a major customer, but other companies as well. In fact, it remains to be seen whether the market has fully absorbed the potential impact of this case.

Like many other international companies, Apple has a code of conduct for its suppliers, which sets out its expectations of suppliers in terms of ethics, and social and environmental responsibility.

In relation to ethics, it states that it expects suppliers to be 'committed to the highest standards of ethical conduct when dealing with workers, suppliers and customers'.

It also states that suppliers 'shall not engage in corruption, extortion or embezzlement in any form' and they 'shall not offer or accept bribes or other means to obtain an undue or improper advantage'. Apple expects its suppliers to have systems in place to implement the code.

In March this year, Apple published its 'Supplier Responsibility' progress report based on 102 facilities it audited in 2009. Interestingly, one of the areas of focus in its 2009 audits was the protection of foreign contract workers by its suppliers, something which is close to home for our companies.

One would expect that with the alleged corruption involving Asian suppliers, Apple will pay even more attention to corruption risks when it audits suppliers.

One would also expect that other international companies which do business with the companies named in the action would place the latter under greater scrutiny because of concerns of legal and reputation risks that these suppliers will bring to them.

If they are not satisfied that there are systems to manage such corruption risks, the most drastic action they can take is to sever business ties with the companies.

Recently, I did a study with an NUS business student, Genna Poh, on the practices relating to the code of ethics, whistleblowing programme, and supplier selection of the Fortune Global 50 companies.

We used public information, including those published on the websites of these companies. We found that 49 of these companies has a company code of conduct/ethics (the exception is a Russian company), and that 36 per cent of these codes specifically mentioned that suppliers are also expected to comply with the company code.

We also found that 46 per cent of these companies had a separate code for their suppliers, and 20 per cent of the companies require suppliers to comply with both their company's code and a separate code for suppliers.

Because we rely on public information, our study probably underestimates the extent to which these companies are focusing on the conduct of their suppliers.

Beyond these 50 companies, I also know from anecdotal evidence that many other companies, such as Apple, are also increasingly focused on ensuring that their suppliers uphold high standards of conduct when doing business.

The case involving JLJ and the other Singapore companies is a sobering reminder of the importance of managing corruption risks when Singapore companies do business with international companies.

The consequences of not paying attention to ethical, social, and environmental issues and putting in place systems and processes for managing them could be catastrophic for the companies.

This episode has also put an unwanted spotlight on Singapore companies, as most of the news reports on the case have specifically mentioned the three Singapore companies. If Singapore companies do not do more, it could also damage Singapore's hard-earned reputation for low corruption and a high standard of ethics.

Further Questions in Apple Bribery Case

By Mak Yuen Teen

Published in the Business Times on 25 April 2012

Tomorrow, JLJ Holdings Limited is convening an extraordinary general meeting (EGM) to seek shareholders' approval to change its name to Jubilee Industries Holdings Limited.

According to its circular to shareholders, this is "in line with the Group's increased presence in Malaysia through its key wholly-owned subsidiary Jubilee Manufacturing Sdn Bhd". It added that "the Directors believe that the proposed change of name will allow the Company to leverage on Jubilee Manufacturing's brand name".

Earlier, on March 30, JLJ had announced that the name of its subsidiary, Jin Li Mould Manufacturing Pte Ltd, had been changed to Jubilee Industries (S) Pte Ltd.

The name changes by JLJ Holdings in its short history as a listed company come after JLJ Holdings and Jin Li Mould became ensnared in a bribery scandal involving an Apple global supply manager, Paul Devine.

JLJ Holdings was incorporated and listed in 2009, with an IPO price of 27 cents per share. Jin Li Mould became a wholly-owned subsidiary of JLJ. Jacky Chua, the founder of Jin Li Mould, became executive Chairman of JLJ and executive director of Jin Li Mould. In 2008, Apple accounted for 82.5 per cent of JLJ's total revenues.

Indeed, in response to pressure from lobby groups to identify its key suppliers, Apple named Jin Li Mould among its list of 156 key suppliers in January this year.

The documents filed by Apple in its civil lawsuit against Devine, which is publicly accessible online, provides a detailed account of the alleged bribery scheme and made a number of claims. The following are some of the highlights of the allegations:

In October 2006, Devine collaborated with Andrew Ang, an assistant manager of Jin Li Mould, whereby Devine would supply confidential Apple information to Jin Li Mould and five other Asia suppliers. In return, Devine received kickback payments from the suppliers. Ang served as the middleman between Devine and the suppliers and shared in the kickback payments. Ang is the nephew of Jacky Chua, the then executive Chairman of JLJ.

In April 2009, Ang resigned. According to the court documents, Devine then emailed Chua a proposal to continue making payments to Devine. Devine and Chua allegedly agreed that Jin Li Mould would pay Devine US$700,000 over a five-month period. In June 2009, Devine thanked Chua for the payment of US$90,000 and informed him that the outstanding balance owed was US$310,000 and Jin Li Mould shares worth US$400,000. On the same day, Devine allegedly emailed Chua and Andric Ng (JLJ's CEO) pricing information from a Jin Li Mould competitor. It was alleged that Jin Li Mould paid a total of US$1 million to Devine.

Before the alleged bribery scandal became public, JLJ's last closing price was 23 cents per share. Today, its shares remain at the level immediately after the scandal broke, hovering at around 12 cents.

What is of concern are the actions of certain key officers, and the dearth of communication from the company about the steps it is taking to address the serious issues and to prevent recurrences. Let's look at the actions of some of the key officers.

On Aug 12, 2010, Chua sold 10 million shares at 15 cents per share through married trades with seven unrelated individuals. Bearing in mind that Devine was arrested on Aug 13 in the United States, and that both Chua and his nephew Ang are mentioned in the court documents, questions arise regarding the timing of the sale of shares by Chua – even though the share sales slightly preceded the arrest of Devine on Aug 13.

On Aug 16, 2010, Tan Soon Liang, a non-executive director of JLJ, also reduced his shareholdings in JLJ from 2 per cent to 1.19 per cent. That same day, JLJ issued an announcement which acknowledged the civil and criminal suits in the US and reassured investors that there was "no clear adverse impact on JLJ's business with Apple".

It is unclear whether Tan sold his shares before or after JLJ's announcement. Even if the benefit of the doubt is given to Tan, the key officers were selling shares while the company was reassuring investors about the lack of a negative impact on the company.

What followed was a series of other announcements to the market. On Aug 18, 2010, JLJ reiterated: "Neither (JLJ) nor Jin Li Mould nor any other member of the Group is a party to any suit by Apple or the subject of any indictment whatsoever".

On Aug 19, 2010, the company announced that Chua had stepped down as executive Chairman. Its announcement stated: "Andrew Ang is the brother in law of the Company's Executive Chairman. In order to facilitate the impartial review of all activities relating to the Apple Claim that may involve the Company and its subsidiaries, the Company's Executive Chairman has also voluntarily relinquished all executive duties in the Company for the time being."

The CEO, Andric Ng, did not step down from his role. JLJ justified it as follows: "There has been no evidence to suggest that (he) had knowledge of or was involved in the alleged payments related to Apple's civil suit." Today, Ng remains as the CEO.

The company needs to do much more to reassure investors because, as mentioned above, the court documents filed in the US have alleged that Ng was included in an email from Devine which provided pricing information from one of Jin Li Mould's competitors.

On Aug 24, 2010, JLJ announced that Foo Say Tun was appointed as the new Non-Executive Chairman. The company also mentioned that the company, Chua and Ng are “co-operating with CPIB in its investigations”. A Steering Committee comprising Foo, Tan and two other independent directors of JLJ was also formed to look into the bribery case.

On Nov 8, 2010, the company made the announcement that “neither Jin Li Mould Manufacturing Pte Ltd nor any of the Company’s subsidiaries had, at any point, made payments to Devine personally and/or Devine’s ‘vehicles’ referred to in Apple Inc’s civil suit”.

On June 1, 2011, the company announced that Chua has resigned from the board “on his own accord to pursue personal interest”.

Apple has been under great pressure to hold its suppliers to account. It audits them each year and takes actions against those which violate its supplier code of conduct.

This is especially so if Apple feels that a supplier has a poor ethical culture that is pervasive and that inadequate corrective actions had been taken. If JLJ loses Apple as a customer, it would be catastrophic for JLJ.

Business with other customers will also be at risk. This may be a real threat to the business continuity of JLJ. Changing the names of the companies involved is unlikely to make a difference.

I believe that at the JLJ’s EGM tomorrow, shareholders ought to ask a lot more questions about this episode and the potential impact on the company. They deserve a lot more answers than what the company has given so far.

JLJ Name Change Not End of Saga

By Mak Yuen Teen

Published in the Business Times on 13 March 2013.

In August 2010, I published the first of two commentaries on JLJ Holdings, a Catalist company which was embroiled in a bribery scandal ("Apple case throws spotlight on corruption", BT Aug 26, 2010). The scandal involved Andrew Ang, a former business development manager of JLJ's wholly owned subsidiary, Jin Li Mould Manufacturing, who was accused of bribing an Apple global supply manager, Paul Devine. Ang has since disappeared and Devine has been indicted in the United States.

I pointed out that even though the actions at that time were directed against Devine and Ang, and not against the companies involved, there was a real risk that JLJ could lose not only Apple as a major customer, but other companies as well, because Apple and other global companies are focusing on ethics and compliance of their suppliers. I was hoping that the company would be forthcoming about the potential impact of the case on its relationship with Apple and other companies. I feared the worst was yet to come for JLJ's shareholders, even though the stock price had already been halved.

The company maintained through its announcements that "neither (JLJ) nor Jin Li Mould nor any other member of the group is a party to any suit by Apple or the subject of any indictment whatsoever" and "neither Jin Li Mould Manufacturing Pte Ltd nor any of the company's subsidiaries had, at any point, made payments to Devine personally and/or Devine's 'vehicles' referred to in Apple Inc's civil suit".

In April last year, JLJ called for an EGM to be held on April 26 to change its name from JLJ Holdings Ltd to Jubilee Industries Holdings Ltd.

I published the second commentary the day before the EGM, where I described how court documents in the US had revealed that after Ang left the company, Devine and Jacky Chua, the then executive Chairman of JLJ, allegedly continued the bribery scheme. Devine allegedly e-mailed Chua and Andric Ng Boon Leng (JLJ's CEO) pricing information from a Jin Li Mould competitor.

I also mentioned that, at around the time of the arrest of Devine and just days before JLJ's announcement linking the alleged bribery to the company's staff, Chua sold 10 million shares. Further, on Aug 16, 2010, the day of this announcement, Tan Soon Liang, a non-executive director of JLJ, also reduced his shareholdings in JLJ from 2 per cent to 1.19 per cent.

In its announcement, JLJ said that there was "no clear adverse impact on JLJ's business with Apple". In other words, the key officers were selling shares while the company was reassuring investors.

Chua resigned shortly after, but the CEO, Ng, did not. JLJ said "there has been no evidence to suggest that (he) had knowledge of or was involved in the alleged payments related to Apple's civil suit". This is despite US court documents showing that Ng was copied in an e-mail from Devine which provided pricing information from one of Jin Li Mould's competitors. Even if Ng did not know of the bribe, surely he would have known that an Apple manager sending pricing information from JLJ's competitor to JLJ is highly irregular and unethical.

The company did not explain the basis for its statement about Ng, given the evidence which was produced in the US court. One would have expected the steering committee and the legal advisers it had appointed to look into the case to have uncovered this evidence – if my students writing a case study on the company could find it on the Internet! The company's continued retention of the CEO under such circumstances raises serious questions about the tone at the top and whether any lessons have been learnt.

On April 30, 2012, JLJ (now called Jubilee) issued an announcement responding to my commentary and to another BT report and maintained that "the company has, in fact, kept shareholders and other stakeholders updated on this matter".

Well, get ready for the concluding chapter to this messy saga. On Jan 28, 2013, Jubilee issued a profit warning that it was expected to report a net loss for the year ended Dec 31, 2012, due mainly to lower revenues.

On Feb 27, it announced that its annual revenues had declined by 28.5 per cent compared with the previous year, with a net loss of $1.819 million against a $142,000 profit.

It finally disclosed the "Apple" impact on its business, with a loss of $16 million in revenues from Apple – greater than its total drop in revenues of $15.9 million. Although Apple missed analysts' revenue estimates last year, its revenues still increased from 2011.

It appears that Apple – Jubilee's largest customer by far – is reducing its business with Jubilee.

On March 7, Jubilee announced that Ng was resigning "on his own accord to pursue personal interest".

Although the company's share price has in recent days recovered to as high as 16 cents after falling to a low of 9 cents – with Chua disposing of a further 13 million shares through married trades on March 8 – and it may be difficult to imagine that things can get any worse, they just might.

The company has, in my view, failed to take serious proactive steps to really get to the bottom of the scandal from the outset – its failure to explain its retention of the CEO despite the evidence presented being a case in point.

I believe that the disclosures by the company throughout the entire episode were defensive and left a lot to be desired. There are questions as to whether listing rules and securities legislation have been breached. Whether the company will survive should be a real concern to shareholders.

It may also be time to ask whether the sponsor-based regime for Catalist companies is serving much purpose in protecting shareholders' interest. As required under this regime, all announcements by JLJ/Jubilee have been accompanied by the following statement: "This announcement has been reviewed by the company's sponsor, PrimePartners Corporate Finance Pte Ltd … for compliance with the relevant rules of the Singapore Exchange Securities Trading Limited … The sponsor has not independently verified the contents of this announcement."

In my view, such boilerplate statements serve little purpose and may give shareholders a false sense of assurance. In recent discussions with some directors and senior management of Catalist companies, their feedback was that the sponsor may be helpful in the first year or two, but thereafter is more of an additional cost if the company has put in place proper systems and people.

Perhaps it is time for SGX to review this regime, particularly if sponsors are only helping companies to comply with the letter, but not the spirit, of its rules.

Plausible Deniability and Graft by MNCs

By Mak Yuen Teen

Published in The Business Times on 21 May 2014

The report "Police charge former China head, 2 execs of GSK with corruption" (BT, May 15) suggests that GlaxoSmithKline's (GSK) bribery and price-fixing scandal in China may be more than a case of some rogue Chinese executives acting on their own. When four Chinese executives from GSK were first accused in July last year of bribing officials and doctors to boost sales and raise drug prices by funnelling up to three billion yuan (S$602 million) through travel agencies, GSK quickly distanced itself from the actions of the executives and called the allegations "shameful".

According to GSK, "certain senior executives of GSK China who know our systems well appear to have acted outside of our processes and controls which breaches Chinese law" (The Guardian, July 22, 2013). Andrew Witty, GSK's group CEO, said the drug firm had "no sense" of the "shameful" allegations.

Now, Mark Reilly, the former British head of GSK China, who stepped down from his position when the allegations first surfaced, has been accused of ordering his subordinates to form a "massive bribery network" that forced up drug prices and created more than US$150 million of illegal sales (The Independent, May 17, 2013). If the allegations against Reilly are true, direct involvement in the scandal has moved up the chain of command in GSK.

Of course, Reilly is still a long way from GSK's group headquarters based in the UK. Reilly reports to Abbas Hussain, president of Europe and Emerging Markets & Asia Pacific, who is part of the corporate executive team of GSK.

Despite the protestations of Mr Witty that the firm did not know about the alleged illegal actions of the executives, questions remain as to whether he and the board ought to have at least asked some probing questions when GSK China was reporting strong sales growth over the years preceding the scandal.

Corruption level

When the scandal was first reported last July, one online comment responding to the group CEO's denial of knowledge of the wrongdoing was rather blunt:

"Did you wake up from a 10-year nap yesterday? I'm shocked. Shocked. Of course they have zero tolerance for getting caught. In corporate speak, now it is about CYA. Usually the senior executives know what is going on, but they will turn a blind eye to the activities. They will congratulate the China office executives for the fantastic sales and profit and growing market share. But if the XXXX hits the fan, they suddenly can see the illegal practices by their China executives, ask for their resignation, make public apology, etc. Very smooth CYA. But this is typical corporate culture in most companies."

China has long been known for a culture in which drug companies make payments to doctors, since physicians rely on rewards for writing prescriptions to offset meagre salaries. Further, according to the Corruption Perceptions Index published by Transparency International, China was ranked 80th out of 176 countries in 2012, 75th out of 183 in 2011 and 78th out of 178 in 2010 in pubic-sector corruption. In terms of the World Bank Governance Indicators, China's Control of Corruption ranking has been consistently in the bottom 30 per cent (in contrast, Singapore is consistently in the top 10 per cent).

Just a year before the scandal broke in China, GSK had paid a record US$3 billion fine for misselling drugs in the United States, in a legal action which spanned more than four years. According to a report in The Guardian (July 25, 2012), GSK "had lavished entertainment on doctors, such as golf lessons and fishing trips, to entice them to promote its medicines".

In the face of well-known corruption in the industry in China and in China more generally, did senior management and the board ask how those high sales growth were achieved? Or were Reilly and the China executives just assumed to be aware of GSK's business code and comply with it? Was it a case of "don't ask, don't tell"?

This reminds me of a true story a former senior executive of a multinational corporation (MNC) shared with me. Following the Asian financial crisis in 1997, there was pressure in Asia on working capital. For the MNC concerned, "working capital" really meant debtors. A bonus plan was introduced rewarding a reduction in debtors.

One of the countries in the region had the lowest debtor days in the group globally. They achieved that by subcontracting debt collection to a firm owned by the military. At a Main Board budget review, a director asked "how do you achieve such a great debtor performance?" The CEO looked at the director and said: "Before I answer, are you sure you want to know?" There was a long silence, the question was never discussed and the meeting moved on.

The funny side was that one debtor did contact the regional office and asked if it was really necessary for the debt to be collected by soldiers in an armoured car! It is doubtful that such debt collection methods fit with the espoused values of the company.

MNCs today are extremely complex with business operations dispersed around the world and conducted through a web of subsidiaries, joint ventures, associates, special-purpose vehicles and other business structures.

Perhaps the board and senior management back in group headquarters really cannot be expected to know what is going on - or at least the complex chain of command provides them with a "plausible deniability" defence when things such as the GSK scandal occur. But should only the executives such as Reilly take the fall while senior management and the board escape accountability?

When companies such as GSK and many others do business in some of the most corrupt countries in the world where it is well known that paying bribes to get business is common, can they really claim that they did not know what was going on? Should they not have exercised more scepticism when their subordinates are reporting strong growth in markets well known for corruption?

While Reilly and the China executives cannot be excused from wrongdoing if the allegations are indeed true, MNCs often put their employees in an untenable position by expecting them to deliver strong financial results over a short time period in markets which are well known for corruption. Further, they are expected to comply with a business conduct code which says all the right things about zero tolerance for bribery, corruption and other forms of unethical behaviour on the one hand (like GSK does), while being incentivised to pursue aggressive growth through pay for performance plans, and buffeted by a fear for their career if they do not deliver, on the other.

In fact, GSK has an impressive 29-page document setting out its anti-bribery and corruption programme which was updated in 2010, following the introduction of the UK Bribery Act.

Difficult markets

How many CEOs and boards of MNCs have thought about the dilemmas that people such as Reilly and the China executives face when doing business in difficult markets such as China?

They would do well to read the blogs of Richard Bistrong, a former vice-president for international sales at Armor Holdings, who worked undercover for the authorities and spent 21/2 years as a government witness. Bistrong was jailed for conspiring to bribe officials to win contracts from the United Nations and several foreign countries. In a blog dated May 13, 2014, called "Rationalising Bribery: Corruption Has No Witness", Bistrong explained that there are usually no witnesses to overseas discussions involving an actual or potentially corrupt transaction

Usually, frontline sales, marketing and business development personnel travel alone overseas and meetings with agents or clients, including public officials, also usually occur without anyone else present. A close relationship usually develops between an overseas employee and intermediaries in the country, and the cultures in many countries lead to a great deal of social interaction outside of work hours.

In his own case, casual discussions often led to the agents explaining "in barely masked language" that they were paying bribes to win contracts. This put him in a dilemma. Should he withdraw from all transactions and inform the company's legal and compliance department?

As he explained: "For a sales, country manager, or marketing person, it is more than just walking away from a transaction, it means walking away from the entire third-party relationship. For these employees, there are not just short-term financial consequences, but also the loss of all future deals, sometimes with regional implications . . . if the C-Suite preaches compliance but the sales incentive package awards 'winning the sale' above all else, how will that employee determine whether management wants compliance or sales?"

With China determined to stamp out corruption, and Narenda Modi and his Bharatiya Janata Party winning the Indian elections on the back of a strong anti-corruption platform, the risks of executives of MNCs operating in these two major economies becoming Reillys will escalate considerably.

Countries where corruption has been accepted as part of the culture can suddenly change course with a regime change. The same thing could happen in African countries such as Nigeria where corruption is known to be high.

Executives who are in those countries are like playing a game of "pass the parcel", except it is more like a ticking time bomb. When the music stops, the executives who happen to be in charge will become the next Reillys.

It is time for senior management and boards of MNCs to stop hiding behind business conduct codes and anti-corruption and compliance programmes and a "plausible deniability" defence, and address more fundamental questions about the benefits and costs of doing business in highly corrupt countries, their business practices, and how they reward, retain and promote their employees.

Truth About Bribery, Corruption Risks

By Mak Yuen Teen

Published in The Business Times on 17 September 2014

I first got to know Richard Bistrong when he contacted me after my commentary in The Business Times on the GlaxoSmithKline (GSK) bribery scandal ("Plausible deniability and graft by MNCs", BT, May 21, 2014), in which I had quoted from his blog.

Richard had served time in prison after a conviction for bribery when he was working for multinationals and also cooperated with the authorities in covert and overt operations as part of his plea bargain.

In July, I met Richard, who lives in New York, over dinner in Midtown Manhattan while I was there on a business trip. Over the course of our conversation, it was clear that companies and individuals can learn a lot from Richard about how and why bribery happens when doing business overseas and what can be done to minimise such risks. We agreed that I would do an interview with him via email.

On Oct 28, I will be moderating a roundtable discussion on "Bribery and Corruption in Foreign Jurisdictions", which is part of the SIAS 5th Corporate Governance Week and Richard will be participating via live video feed to share his views.

Prof Mak: Richard, thank you for agreeing to share your experience. Can you first tell us a little bit about yourself?

Richard: First, Professor Mak, I wanted to thank you and The Business Times for allowing me to address your community through this interview. I grew up in the New York metropolitan area, received my BA (Foreign Affairs) from the University of Rochester, which included studies at the Institute for European Studies in Vienna, Austria.

I then attended the University of Virginia where I received my MA in International Relations. Career-wise, I literally "grew up" in the Defence and Law Enforcement supply industry, through a fourth-generation family business, started by my great-grandfather in 1888, and which was sold in 1992.

I then worked for a public safety uniform manufacturer as the Director of Retail Operations, and in 1995 I took a sales Vice President role in what was a small manufacturer of bullet-resistant armour, which at the time was in bankruptcy. In 1998, at the same corporation, I was appointed Vice President of International Sales. By then, the company had emerged from bankruptcy, and was now a large, successful, and publicly traded multi-national company that distributed and manufactured military and law enforcement products on a global basis.

From 1998 to 2007, I traveled overseas approximately 250 days a year, and was posted to live and work from the UK twice during that period. So, I was literally traveling the world most of the time and was rarely "off the road". It was also during that time when I first confronted international bribery in my work as an international sales executive.

Prof Mak: What were you charged with? What penalties were imposed on you? Tell us a little bit about your cooperation with the authorities.

Richard: In early 2007, I was terminated by my prior employer and shortly thereafter, I was contacted by the Justice Department through my attorney and given the opportunity to proffer. I then started cooperating with US Federal Law Enforcement. My cooperation lasted five years. This cooperation was part of a Plea Bargain with the United States Department of Justice, whereby I pleaded guilty to one count of conspiracy, including violating the anti-bribery and books and records provisions of the FCPA (Foreign Corrupt Practices Act).

In addition, in exchange for cooperating with a number of UK enforcement agencies, both covert and overt, I was given "Immunity from Prosecution" by the UK Revenue and Customs Prosecutions Office, which covered issues of illegal conduct that took place while I was residing and working in the UK.

During that period of covert cooperation, I assisted those agencies in understanding how bribery and other export violations occurred and operated in international sales. My understanding is that my covert cooperation was one of the longest in terms of time and scope, for a white-collar criminal investigation.

In the summer of 2012, I was sentenced as part of my US Plea Bargain, and served fourteen and a half months at a Federal Prison Camp, and released in December 2013.

Prof Mak: It sometimes seems that individuals almost slip into breaking the law without really being conscious of it. Can you share with us how it happened in your case? In other words, did you intentionally break the law or was there a way you rationalised the activities?

Richard: I totally rationalised it. But to be clear, I bribed, I knew it was illegal, and I wasn't thinking at all about the consequences. And I just want to reaffirm, I am in no way trying to justify what was illegal conduct.

Rationalising bribery, in my case, was not a struggle. Many of the illegal conversations I had took place far away from the home office and corporate management. In fact, during my travels, when the talk turned to corruption, the only people present were myself and the agent or intermediary. Thus, given my remote location, the lack of "witnesses", and the fact that the company was pleased with my personal and divisional sales performance, I felt that there was little chance I would ever get caught.

These circumstances are common in international business, and that is a part of the challenge for those at the front line of international commerce and the compliance professionals who are tasked with helping them to be both successful and compliant. Much of the conduct, like my own, is covered with secrecy and takes place at remote locales with little or no oversight.

I realise that for those responsible for anti-bribery compliance, the choice between corruption and compliance is as simple as "walk away". But in reality those choices become more difficult when front line international business groups are being compensated with lucrative compensation plans, as is often the case.

When those incentive plans are indexed to personal performance in corrupt regions, as opposed to group or divisional performance, the anti-bribery message can get distorted, diluted, or in the worst case, discarded, as those on the front line now might think of compensation and compliance as a "zero sum" game. It is a dangerous situation for all involved when someone starts to consider compliance as "bonus prevention" and starts pondering, "what does management really want, compliance or sales?"

Let us remember, public multinational companies don't as a rule tolerate sales decreases, and in the international arena, where sales in many regions are highly centralised and unstable (along with poorly trained procurement personnel and confusing procurement procedures), with a "win-big, lose-big" impact, the pressure to perform and deliver on a quarterly basis is intense. Add to that the illusion that bribery has no victims, or worse, that it is a "win-win", to those at the front lines of international business, myself included (at the time), making the decision to rationalise corrupt behaviour may not be as difficult or as black and white as one might think.

Prof Mak: The recent GSK case and other cases involving multinationals seem to suggest that bribery and corruption is still common today? Do you think things have got better?

Richard: That is an interesting and complicated question. I do think that bribery and corruption are being better addressed through anti-bribery corporate compliance programmes, but my belief is that many of the forces that shape what I call the "perfect storm of rationalising bribery" remain in effect. In other words, where compliance becomes only a "set of rules and procedures", I think the impact of an anti-bribery programme is limited. Even the Chief Medical Officer of GSK discussed in an interview with Reuters, how business practices need to be reviewed and that GSK will need to consider building "a new sales model designed to eliminate sharp marketing practices".

I think that is the kind of thinking, where an organisation realises that the business strategy itself might be a red flag for bribery, that a true anti-bribery ethic and aversion to corruption can start to take effect among front line personnel. When that happens, I think there is significant and sustainable progress.

In addition, I think in the context of how compensation impacts compliance, human resources might want to take a greater role in looking at the bonus plans in territories which have a reputation for corruption. The challenge of compensation and compliance does not call for a "one size fits all" model.

While I realise that HR has a great voice in most compliance programmes, including training, documentation, etc, I have not read much about bringing HR into the discussion of individual and group compensation planning with a focus on territorial reputation.

A businessperson who has regional responsibility in Scandinavia, as an example, should not have the same compensation bonus structure as someone who is responsible for South America.

Again, from my perspective, taking a look under the hood of bonus plans for international personnel is a critical link. Thus, I think HR has to ask, are the ends of achieving bonus in line with the means of compliant behavior in achieving those goals.

Prof Mak: In many cases where bribery and corruption is involved, senior management and the board would often say that they did not know what was happening and that employees ought to know that they have zero tolerance for corruption. Do you think senior management and the board need to take more responsibility for what goes on in cases involving bribery and corruption?

Richard: I wonder how many companies, including C-Suite personnel as well as those who serve on the relevant Board committees, are looking at the business strategy itself as a potential red flag of corruption. I call attention to business strategies and growth forecasts in regions that have reputations for corruption, and ask if anyone is asking when those targets are achieved - "how did we get there?". Or, is it all high-fives? How many times can a company, as we have recently seen in the pharmaceutical industry, keep saying, "it's all about the rogue employees" without finally looking inward to analyse potential inherent red flags buried within corporate business strategies and regional growth plans.

Thus, from my perspective, the Boards and senior management need to start looking at anti-bribery and anti-corruption (ABAC) starting with an analysis of business strategy, growth forecasts and compensation plans.

They need to ask if all those programmes are aligned with their ABAC programmes, and to unwind those plans where contradictions exist, and where they are leaving it to front line employees to decide "what does management really want, compliance or sales?"

For a Board or senior management to say "they didn't know", and to default to the "rogue employee" communication plan, might work or be appropriate for an individual enforcement issue, but does it really address potential systemic inconsistencies within the business as a standalone ABAC issue?

In my opinion, international front line teams need compliance tools for how to manage the risk challenges in the field beyond the compliance paradigm of "don't do it". The dynamics of international sales are complicated, and they have regional peculiarities. The people dealing with those issues in their territories need solutions that address and incorporate those challenges, both globally and regionally.

Prof. Mak: What are you doing now?

Richard: Well, that is evolving. I have had a broad and extensive career as an international sales executive along with an extended term as a law enforcement cooperator for multiple governments, including the US and UK. Accordingly, I currently view my blog, website (www.richardbistrong.com) and speaking invitations as vehicles to engage with compliance and business professionals on current anti-bribery issues and challenges.

I do this by sharing my own perspectives and inviting that of others. I hope that by welcoming outside comment and discussion that I might ascertain if the sum of my experience brings any value by complementing the current level of anti-bribery debate and practice.

Furthermore, I look at this as a long-term process. I am employed in my community, working on a weekly basis to satisfy and exceed my court ordered community service, so I see this very much as an effort to find a long term voice in the compliance community.

What really interests me is how I can help organisations, academia and industry groups with current and real anti-bribery challenges, especially as they impact those operating in overseas markets.

Prof Mak: Thanks very much, Richard. See you in October.

Richard: Thank you and I look forward to seeing you "on the video" at the SIAS 5th Corporate Governance Week in October!

If the Board Doesn't Ask, the Board Wouldn't Know

By Mak Yuen Teen

Published on governanceforstakeholders.com on January 5, 2018

When things go badly wrong, such as in the recent Keppel Offshore and Marine (KOM) scandal, which has resulted in a US$422 million penalty being imposed, a common response of the board of directors is: "We did not know".

Readers may be interested in this article I wrote in 2014 about "plausible deniability" which is posted on my website

In the article, I related a story, which I have reproduced here:

> *"This reminds me of a true story a former senior executive of a multinational corporation (MNC) shared with me. Following the Asian financial crisis in 1997, there was pressure in Asia on working capital. For the MNC concerned, "working capital" really meant debtors. A bonus plan was introduced rewarding a reduction in debtors.*
>
> *One of the countries in the region had the lowest debtor days in the group globally. They achieved that by subcontracting debt collection to a firm owned by the military. At a Main Board budget review, a director asked "how do you achieve such a great debtor performance?" The CEO looked at the director and said: "Before I answer, are you sure you want to know?" There was a long silence, the question was never discussed and the meeting moved on.*
>
> *The funny side was that one debtor did contact the regional office and asked if it was really necessary for the debt to be collected by soldiers in an armoured car! It is doubtful that such debt collection methods fit with the espoused values of the company."*

I am not saying that this scenario happened in the KOM corruption scandal and that the Board asked and then did not want to know the answer. One of the main points of my article is that often times, the Board would not ask the awkward questions, particularly when things are going smashingly well. Who wants to be the wet blanket on the board who asks: "How do we win all these contracts in an industry that is so rife with corruption in a country that is rated so poorly on transparency and corruption-type indices?". There are reports out there that look at corruption risks by industry sectors and countries and putting the two together should suggest that O&M and Brazil = very high corruption risks. I may be accused of 20/20 hindsight but I have written about this for several years now, warning about the corruption risks when our companies venture overseas. There's also a cautionary lesson about avoiding groupthink on boards and the value of having someone who is prepared to ask the tough questions – or even questions that may be seemingly stupid.

In the Business Times article today “Keppel scandal holds lessons for Singapore Inc” (January 5, 2017), there is an interesting comment about the “entire economic group” concept under Brazilian law whereby a group will be held responsible for any wrong-doing committed by any company owned by it. In other words, it does not matter if a parent company in Singapore sets up a wholly-owned subsidiary, which then sets up another subsidiary overseas, which then sets up a joint venture, which then engages a third party who then pays bribes. In fact, that’s sort of how this happened in the present case. The separate legal entity, often used to “ringfence” a company’s risks, does not really work. In fact, even if the “entire economic group” concept does not apply, anti-corruption laws in various countries, including US and UK, does not allow companies to circumvent their rules just by creating a chain of separate legal entities, or using subcontractors or third parties to pay bribes. I have been surprised by senior executives who have admitted to making “facilitation payments” through third parties and said they do not believe in paying bribes! We call them “facilitation payments” because “bribes” is a dirty word.

Chris Bennett and I wrote a report on the governance of company groups that discusses the issues faced by companies and directors in a company group situation. It offers a framework for starting to think about the challenges and mitigating measures but by no means provides all the answers. Readers can access the report from here:

http://governanceforstakeholders.com/wp-content/uploads/2014/06/governance-co-groups.pdf

What Does Integrity Really Mean?

By Mak Yuen Teen

Published on governanceforstakeholders.com on January 15, 2018

Last week, following a rather eventful few weeks in Singapore with news of the bribery scandal and the US$422 million fine paid by Keppel Offshore & Marine (KOM), I dragged my wife along to watch "Molly's Game". This is a movie starring Jessica Chastain, Idris Elba and Kevin Costner. I say "dragged" because it is not the type of movie we usually watch in the cinema – more the type we would watch on Bluray at home or I would do on my long-distance flights. But we both ended up enjoying it a lot.

The movie, based on a true story, is about a former professional skier, Molly Bloom, who ended up running an underground poker empire for Hollywood celebrities, business tycoons, sports stars and, unknown to her, the Russian mob. At the end of the movie, I turned to my wife and said "Actually, the movie is about integrity." Whatever one might think about poker or gambling, we can see that Molly was trying to do the right thing.

Molly's poker empire got started after her boss asked her to help out on his underground high-stakes poker game with these rich folks. Soon, the boss changed the rules. He felt that she was making enough from tips and did not want to pay her wages for her day job. Then he tried to cap her tips. And then he cut her off. So she started her own high-stakes poker game.

In running her poker empire, she tried hard to stick to the rules. She sought legal advice about whether what she was doing was in accordance with the law. Yes, she made mistakes. She started taking drugs to deal with the stress and lack of sleep. She took a cut of the pot to operate as the bank, which broke the law. She probably should have engaged a better lawyer to advise her as to whether she was breaking the law. But, at the end, she was prepared to do the right thing and face the consequences when she could have cut a deal which would have cost her much less personally. She took responsibility. [As a digression, the judge's questions at the start of her plea hearing near the end of the movie reminds me of the public transcript of Jeffrey Chow's plea hearing for KOM].

Fundamentally, integrity is about doing the right thing when nobody is watching and even if it costs you personally. Some people can do the right thing even under the most adverse circumstances while others find convenient excuses without even trying to do the right thing. Many people will do the right thing because they are afraid of being caught. That's not integrity. That's just *kiasi* (literal meaning – "afraid of death").

The KOM bribery scandal was like fixing the poker game to make sure you win or to improve your odds of winning. It's much, much more than paying a "facilitation fee" to make sure that your permit application is not stuck in some government bureaucracy or your goods are not held up in a port somewhere. Bribing to win contracts is downright dangerous. Imagine if someone pays a bribe to get a contract to build an oil rig and then cut corners. Or a bridge. Or an apartment complex. Once it is discovered that a contract was won by unfair means, questions about whether the job was done to appropriate standards would inevitably arise.

If you read Animah Kosai's article "Keppel, The Story of a Bribe" published by The Anti-Corruption Digest on January 10 about the bribery in the US$1 billion P-61 project, KOM executives allegedly worked to conceal the bribe from KOM's U.S. joint venture partner McDermott International, which they knew may have a problem with paying bribes because of their familiarity with FCPA. Further, part of the bribes went to a Petrobras employee responsible for the bidding process. It was not just a simple act of bribery, but an elaborate scheme designed to gain an advantage for KOM and a betrayal of trust of the JV partner. And this is just for one project. One can only hope that this saga does not scare away reputable KOM partners especially since it did not involve just some "rogue employee".

The word "integrity" has been so cheapened today that it has lost its meaning. Business and political leaders often use the word even when they clearly don't have it. Companies, universities and organisations claim it as a core value. A common refrain from those in business is that in some countries and in some sectors, one *has to* pay bribes. There is *no choice*, they say.

There is always a choice – one can always walk away. One cannot say that he has integrity if he just pays when it's necessary to get deals. Or when it's the common business practice.

If a company or someone chooses to pay bribes, it is their choice and they should face the consequences if they are caught. But they should not brazenly proclaim that they have integrity if they do so. That's just hypocrisy.

CASE STUDIES

JLJ Holdings Limited: Poisoned by Its Rotten Apple

Case Overview

On 6 July 2009, JLJ Holdings launched its Initial Public Offering (IPO) of 19 million shares at S$0.27 each. The shares were highly popular and sold out fully. However, just a year later, the company's popularity turned into infamy when a global supply manager of Apple was arrested and charged with bribery. One of JLJ's employees was also indicted for his active involvement in the bribery scheme. This case can be used to discuss issues such as the impact of corruption-related risks on companies, measures that company can take to mitigate such risks; the role of the board in setting the right tone; and how the board should deal with the investigation and communication of a corruption scandal.

The History of JLJ Holdings Ltd

JLJ Holdings was first incorporated as a private limited company under the Singapore Companies Act on 18 March 2009. On 19 May 2009, it was converted into a public limited company.

The history of JLJ can be traced back to July 1993, when Jin Li Mould was founded by JLJ's Executive Chairman Chua Kim Guan and his group of friends. It targeted the niche market for Mould Design and Fabrication (MDF), where Chua saw immense growth potential. Despite its size and limited resources, Jin Li Mould quickly built a reputation for high quality standards in its services and capabilities. In 1997, it secured a contract with Hewlett Packard. This was soon followed by a supply contract with Apple in 2001, paving the way for a profitable long-term business relationship.

In 2003, Chua identified business opportunities in China and commenced operations in Jiangsu province with the establishment of EMold Kunshan, with Chua as its sole shareholder.

"Growth in Tandem with Apple"

By 2008, Jin Li Mould was heavily involved in the production of components for a majority of Apple's products, including the iPod and iPhone range of devices, and the Macintosh range of personal computers. To meet the increasing demand from Apple, EMold Kunshan eventually focused on producing Apple-related components. Its close proximity to Apple's outsourced manufacturing facilities in China enabled it to provide more efficient support for Apple's operations.[1] This business relationship with Apple proved to be crucial for the group of companies. Between 2006 and 2008, revenues derived from contracts with Apple grew from 70.8 per cent of total revenue to 82.5 per cent of total revenue.[2]

As Apple posted a record US$1.21 billion net profit for Q2/FY2009, coupled with forecasts that the global consumer electronics market will be worth US$260.7 billion by 2012,[3] expectations were high for the continued growth and performance of Chua's companies. In Chua's own words,

"Given our well established relationship with Apple, we are well positioned to ride on the continued growth in tandem with the global demand for Apple products". [4]

JLJ's Initial Public Offering

In November 2008, EMold Holdings was incorporated and acquired the entire issued share capital of EMold Kunshan from Chua. A series of share swap agreements then saw JLJ acquiring the entire equity interest of Jin Li Mould, EMold Holdings, and EMold Plastics from Chua. The restructuring exercise thus resulted in JLJ becoming the holding company of the Group.

On 6 July 2009, JLJ launched its Initial Public Offering (IPO) of 19 million placement shares at S$0.27 each to much excitement. These placement shares were fully subscribed by institutional and private investors, raising S$5.1 million for the company.[5] On 10 July 2009, JLJ's shares made their debut on the Singapore Exchange Catalist board at S$0.26 each, with public investors holding 15.4 per cent of JLJ's issued share capital.

With proceeds raised from the listing, JLJ was now ready to execute the plans for expansion at EMold Kunshan, Jubilee and Jin Li Mould over 2010 and 2011, and to explore new opportunities in the automotive and medical devices industry.[6]

The Birth of a Fraudulent Scheme

After listing, revenues from contracts with Apple continued to be the key driver of growth in the Group, particularly through business dealings involving Jin Li Mould. A key party that facilitated Jin Li Mould's partnership with Apple was Paul S. Devine, a Global Supply Manager (GSM) at Apple, and an employee of Apple since 2005. Devine was involved in selecting suppliers of materials for Apple's iPhone and iPod earphones, and in his capacity as GSM, had access to confidential company information and also Apple's private third-party information.

In October 2006, Devine collaborated with Andrew Ang, an assistant manager of Jin Li Mould, to devise a scheme where Devine would supply confidential Apple information to Jin Li Mould and five other Apple suppliers in Asia. The confidential information exchanged included product forecasts, pricing targets, product specifications, and data obtained from Apple's business partners.[7] The information enabled these five suppliers to gain an upper hand against competing suppliers in bids for contracts with Apple. In return, Devine was to receive kickback payments from the suppliers, determined as a percentage of the businesses they did with Apple.[8] Ang agreed to serve as the middleman between Devine and the suppliers. For his role, it was agreed that Ang would share the total sum that Devine received in kickback payments.

From October 2006 to August 2010, Devine communicated with Ang through his personal Hotmail and Gmail accounts on his Apple-supplied laptop. Certain code words were used to avoid any suspicion in case others chanced upon their correspondence – the code word "sample" was used to refer to a kickback payment. "Consulting services" contracts were also structured with one of the suppliers involved, so as to mask the nature of the kickback payments.

How Devine Concealed the Kickback Payments

To receive the kickback payments, Devine instructed the suppliers to make payments via wire transfer to a bank account that was opened under his wife's name. Increasingly worried that accumulation of a large sum of money in one account would attract the attention of banks or regulatory authorities, Devine then set up multiple bank accounts in countries around Asia under his wife's name, and directed some payments to those accounts. He also made it clear to the suppliers involved that each wire transfer payment must not exceed US$10,000. In an email sent to a supplier in October 2007, Devine wrote,

"I still haven't received Sept payment. Can you check with your Accounting Dept? Please do not send the Sept and Oct payment together in one wire transfer. Anything over $10,000 wired could draw too much attention."[9]

At the same time, Devine also received payments directly from some suppliers and their agents. Between them, Devine and Ang coordinated meetings in Asia to exchange payments. In an email from Devine to Ang on 22 January 2008, it was 'business as usual' for the two,

"We probably have to meet in Macau for the samples (i.e. payments)."[10]

Devine undertook significant measures to conceal the scheme he had devised with Ang. He eventually set up a company, CPK Engineering Corporation, and opened bank accounts using the business name. The accounts were used to collect the kickback payments, which were then redirected to his personal account. This covered his tracks by disguising the source, ownership and nature of the payments received. Throughout the scheme, the kickbacks were distributed among at least 14 bank accounts held in his wife's and CPK's names in the US, South Korea and Singapore.[11]

When the Cat Got Out of the Bag

Until this point, Devine had his kickback payments while Ang shared in those kickbacks. Everything seemed smooth sailing until April 2009, when Ang resigned from Jin Li Mould. To continue this scheme, Devine contacted Chua, and entered into an agreement with Chua to maintain the covert agreements. In an email to Chua in June 2009, Devine wrote,

"I will continue to provide [Jin Li Mould] with information & opportunities to keep your business growing."[12]

He then thanked Chua for a US$90,000 payment and reminded him of the outstanding balance owed of US$310,000 cash and US$400,000 worth of Jin Li Mould shares.[13] This was immediately followed by an email containing price information from a Jin Li Mould competitor.

The scheme finally broke apart in April 2010,[14] when Apple launched a probe into Devine's actions. A Microsoft Entourage database of emails and a cache of Hotmail and Gmail messages on Devine's Apple-supplied laptop were uncovered. The email messages contained payment details, as well as correspondence with Ang, Chua and other suppliers that contained confidential Apple information. It was also discovered that Devine had demanded and received over a million dollars of illicit payments, throughout his five years in Apple.

In August 2010, Apple filed a civil suit against Devine. Among the allegations made against Devine was a breach of his duty to Apple regarding the obligation to report "real or apparent conflicts of interest, actions that may compromise relationships or confidential and proprietary information, lack of impartiality between suppliers, reciprocity and self-dealing". These terms were contained in the Business Conduct Policy that Devine had signed when he joined Apple in 2005. His scheme with Ang was a clear violation of these duties. Steve Dowling, Apple's spokesman, expressed the company's displeasure,

"Apple is committed to the highest ethical standards in the way we do business and we have zero tolerance for dishonest behaviour inside or outside the company."[15]

The civil suit by Apple was soon followed by an investigation involving the FBI and IRS. Ang's involvement and the identification of him as an employee of Jin Li Mould raised questions about the role that JLJ had in the scheme, and cast an "unwanted spotlight" 16 on JLJ and the other Singapore companies named in the suit.

JLJ's Shares Plunge

On the day of Devine's arrest, 25.6 million shares of JLJ were traded compared to an average daily volume of about 496,000 shares over the previous month. In a filing to the Singapore Exchange (SGX) on 16 August 2010, JLJ acknowledged the civil and criminal suits in the US that "apparently named" Ang, and sought to reassure investors that there was no clear adverse impact on JLJ's business with Apple.[17] On 18 August 2010, it filed another statement with the SGX to reiterate that,

"Neither (JLJ) nor Jin Li Mould nor any other member of the Group is a party to any suit by Apple or the subject of any indictment whatsoever".[18]

Despite repeated assurances and claims of no involvement, these did not stop the downward spiral in JLJ's share price. In the days after Devine's arrest and the indictment, JLJ had to request for a trading halt twice – first on 19 August and then again on 24 August. By 19 August 2010, JLJ's share price had fallen to S$0.12, and hit a low of S$0.10 at the market close on 30 August 2010.

Management Reshuffle

On 19 August 2010, Chua voluntarily relinquished his duties as Executive Chairman when the Corrupt Practices Investigation Bureau (CPIB) started investigations into the case. A statement by JLJ filed with the SGX stated that, "Andrew Ang is the brother in law of the Company's Executive Chairman. In order to facilitate the impartial review of all activities relating to the Apple Claim that may involve the Company and its subsidiaries, the Company's Executive Chairman has also voluntarily relinquished all executive duties in the Company for the time being."[19]

Meanwhile, CEO Ng Boon Leng did not step down from his role. JLJ explained that,

"There has been no evidence to suggest that (he) had knowledge of or was involved in the alleged payments related to Apple's civil suit."[20]

Five days later, on 24 August 2010, Foo Say Tun, who sat on the board of a few listed companies in Singapore, was appointed as the new Independent Non-Executive Chairman of JLJ.[21] With no indication on whether Chua's relinquishing of duties was merely a temporary arrangement, Foo was to lead JLJ through its present difficulties.

JLJ Claims No Involvement in Kickback Scheme

Following its independent investigations, JLJ filed an announcement with the SGX on 8 November 2010, claiming that,

"On the facts known to the Company, which have been reviewed and confirmed by the Company's Audit Committee and Chief Financial Officer, neither Jin Li Mould Manufacturing Pte Ltd nor any of the Company's subsidiaries had at, any point, made payments to Devine personally and/or Devine's 'vehicles' referred to in Apple Inc's civil suit."

While Ang's whereabouts remained unknown, JLJ emphasised that Ang was a former employee of Jin Li Mould who had left since 28 May 2009. An operations manager at JLJ pointed out that "(Ang) had not been with (JLJ) for over a year and (everyone was) unaware of his whereabouts."[22]

Devine Pleads Guilty to Criminal Charges

On 28 February 2011, Devine finally pleaded guilty to wire fraud, conspiracy and money laundering. The scheme that Devine "(defrauded) Apple of its money, property and right to his honest services" reportedly cost Apple over US$2.4 million.[23] Under his plea agreement, Devine agreed to surrender about US$2.28 million of his proceeds from the scheme, and will potentially face up to 20 years in prison.[24] However, Ang's whereabouts remains a mystery.

JLJ's Financial Performance after the Bribery Scandal

JLJ's net profit attributable to shareholders for the financial year ending 31 December 2010 showed an impressive 847.2 per cent year-on-year growth compared to the previous period, increasing from S$0.3 million to S$2.9 million. Revenue grew 6.6 per cent, from S$60.1 million to S$64 million. JLJ's financial results continued to remain strong in the first half of 2011, with net profit attributable to shareholders increasing 3.2 per cent and revenues growing 14.9 per cent compared to the previous corresponding period. On 30 December 2011, the last trading day of the year, JLJ's share price closed at S$0.08. Whether the bribery scandal will have a long-term impact on JLJ remains to be seen.

Sun Hung Kai: Brothers (Up) in Arms

Case Overview

In early March 2011, Sun Hung Kai Properties (SHKP) received the 2011 Asiamoney Best Corporate Governance in Hong Kong accolade.[1] A few weeks later, the Independent Commission Against Corruption (ICAC) launched an investigation into SHKP for involvement in bribery. Soon after, SHKP made headlines in Hong Kong regarding the arrest of the billionaire brothers, Raymond and Thomas Kwok. The news caused SHKP shares to plunge the most in 14 years, losing US$4.9 billion in market value.[2] This case can be used to discuss issues such as corporate governance in the context of family-controlled businesses; board composition and director independence; as well as bribery and corruption.

Background of Corporate Governance in Hong Kong

In 2011, Hong Kong broke the record to become the first Asian financial centre to top the World Economic Forum's fourth annual Financial Development Report, surpassing the U.S. and the U.K. Hong Kong's position as an international economic and financial centre has been attributed to its exemplary corporate governance.[3]

With Hong Kong's various authorities and regulatory bodies emphasising transparency and accountability for listed companies, Hong Kong was ranked second by Asian Corporate Governance Association for corporate governance among 11 Asian countries in 2012, trailing closely behind Singapore.[4] Hong Kong also has the reputation of being one of the world's least corrupt countries. Transparency International ranks Hong Kong at No. 12 out of 182 countries.[5] One reason for this is the presence of the ICAC, which acts independently of government. Nevertheless, it is common for the government and big businesses to work closely together. In fact, the government's single biggest source of revenue is from land sales to property developers.[6]

The Story of Sun Hung Kai Properties

SHKP was founded in 1963 by Kwok Tak Seng, together with Fung King-Hei and Lee Shau Kee. SHKP's core business is the development of property for sale and investment. SHKP is also involved in complementary business activities related to hotels, property management, construction and insurance, and has investments in telecommunications, information technology, transportation, infrastructure and other businesses. In 1972, SHKP became publicly listed on the Stock Exchange of Hong Kong.[7]

Over the years, SHKP became the world's second-largest property company with a market capitalisation of US$32 billion. Together with its rival Cheung Kong (Holdings), they dominate Hong Kong's home-building and office- development industries. During FY2011, SHKP recorded revenues of HK$62,553 million (approximately US$8,038.1 million), an increase of 88.4 percent over FY2010.[8]

Awards and Accolades

In a poll conducted by Asiamoney in 2011, SHKP emerged in the top position for Best Corporate Governance in Hong Kong. In attaining this recognition, SHKP had portrayed an outstanding image of upholding high standards of corporate governance in the company. On top of that, SHKP has received several other corporate governance awards from FinanceAsia and Corporate Governance Asia over the years.[9]

Ownership Structure

The Kwok family is one of Asia's most powerful families. The Kwoks, with estimated wealth of US$18.3 billion according to Forbes magazine, ranked locally in wealth only behind Asia's richest man, Li Ka-Shing, founder of Cheung Kong. The brothers and their family are ranked as the 27th richest in the world. The three brothers, Walter Kwok, Thomas Kwok and Raymond Kwok, as well as their mother Kwong Siu-hing, sat on the board in 2011.[10]

Kwong Siu-hing was the largest shareholder of the company with a shareholding of 42.17 percent in 2011, through the control of the family trust set up by the late Kwok Tak Seng,[11] who founded the company in 1963. The three brothers also had deemed interest in the family trust, which meant that there was an overlapping of shareholdings among the family.

The Board

As of 30 June 2011, the Board of Directors was made up of 18 Directors (excluding the alternate Directors), out of which 7 were executive directors, 7 were non-executive directors and 4 were independent directors.[12] There were four board committees – Executive Committee, Audit Committee, Remuneration Committee and Nomination Committee. Among the Non-Executive Directors were former executives of SHKP such as Walter Kwok and Michael Wong. Although there were 18 directors in 2011, Chairman Kwong Siu-hing was instrumental in many of the company's decisions and had great control by virtue of her shareholding and status in the family.

Board Diversity

Another characteristic of the Board was its lack of female representation other than the Chairman. In addition, a large percentage of the Board members had similar backgrounds, either in the banking or property industry. For example, Woo Po-shing was concurrently a director of Henderson Development Limited,[13] which is also a leading Hong Kong property developer, while Yip Dicky Peter and Donald Leung were from the banking industry.

Independent Directors

One of the independent directors, William Fung, concurrently held a non- executive directorship with HSBC bank. Based on the shareholding disclosed, HSBC Nominee Bank was the second largest shareholder with over 42.09 percent of the SHKP's shares being held in its name. SHKP held the view that William Fung was independent by virtue of the fact that William Fung did not control the HSBC Trustee's voting decision.[14].

In addition, the independent directors also sat on numerous boards. As disclosed in the 2011 Annual Report, Richard Wong sat on a total of 7 boards; another independent director Li Ka-cheung also sat on a total of 7 boards and William Fung sat on 8 boards.

Family Dispute

In 2008, animosity started breeding in the Kwok family when Walter had an intimate relationship with a female confidante, Ida Tong, which rocked the relationship with his brothers. The brothers had felt that Ida was exerting undue influence on the company. Subsequently, Walter, who had been Chairman since 1990, was ousted with claims of him being unfit to serve the board, and his mother, Kwong Siu-hing, then took over as Chairman from May 2008 to December 2011. Raymond and Thomas claimed that their eldest brother Walter had bipolar affective disorder and was unable to fulfil his duties. In a court order seeking to prevent his removal, Walter denied his brothers' claims. To further exert their power over Walter, Kwong Siu-hing, as head of the Kwok household, took him out of the family trust in 2010.[15] In December 2011, Raymond and Thomas were appointed as joint chairmen of SHKP.[16]

The Kwok family dispute had not been resolved ever since. Traces of the family dispute, which led to the removal of Walter Kwok as the Chairman and Chief Executive of the company,[17] were evident in the 2011 Annual Report. Walter Kwok disclosed that he "had recently been given certain information about his share interest in the Company which he found to have serious discrepancy with what his understanding is and that his share interest in the Company is under dispute".[18] His failure to attend any board of directors' meeting in 2010 and 2011 and the lack of involvement in sub-committees of the Board reflected minimal interest in the company affairs.

"King Strategist"

Rafael Hui Si-yan, whose nickname is "King Strategist", had been friends with Thomas Kwok and Raymond Kwok since childhood through family connections. According to sources close to the family, he was also trusted by the Kwoks' mother. In 2005, Rafael Hui was appointed as the Chief Secretary for Administration for Hong Kong, which is the second highest position of the Hong Kong Government. Upon taking up office, Rafael Hui declined to move into the colonial mansion on Victoria Peak reserved for the chief secretary. Instead, he chose to stay in his luxurious 5,000 square feet apartment, situated in the Leighton Hill complex, a Sun Hung Kai development. Rafael Hui pledged to pay HK$160,000 (US$20,600) per month in rent to remain in the apartment.[19] That decision sparked criticism that Rafael Hui would be placed in a position of conflict of interest in his public role because of his dealings with the Kwok family. As Chief Secretary, Rafael Hui's connections with SHKP came under public scrutiny after he took on an oversight role of the billion-dollar project, West Kowloon cultural district, which SHKP had bid for. Over the years, Rafael Hui provided both political and business advice to SHKP.

This benefited SHKP greatly as a developer in a city where land supply is regulated by the government.[20]

The Fall

On 19 March 2012, one of the longest serving executive directors, 66 year-old Thomas Chan Kui Yuen, was arrested by the ICAC in connection with a bribery investigation.[21]. Despite this bad news, the shares in SHKP only fell slightly by 2.4 percent. Many analysts attributed the mild market reaction to his retirement age and that the arrest was unlikely to affect the company's long term operations.[22] John Chan, an analyst at Standard Chartered, wrote in a report that investors would only be concerned if the allegations were extended to the company and other senior management.[23]

On 29 March 2012, Joint Chairmen Thomas Kwok Ping Kwong and Raymond Kwok Ping Luen were arrested in connection with bribery involving Rafael Hui. The company's shares were halted from trading shortly after the market opened. When it resumed trading the next morning, its shares plunged by 15 percent. The decline in the stock price and unusually high trading volume were the results of stock downgrading by at least four banks and brokerages, including Citigroup Inc. and Barclays Plc. In addition, Standard & Poor's also placed the company's A+ debt rating on negative credit watch. By 30 March 2012, SHKP's market capitalisation had shrunk by US$4.9 billion.[24]

Just over a month later on 4 May 2012, former Chairman and current non-executive director Walter Kwok was also arrested on suspicions related to an anti-bribery ordinance.[25] On the same day, the company's shares were suspended from trading together with those of its unit SUNeVision Holdings Ltd. By 4 May, SHKP shares had fallen by 17 percent compared to a 2.1 percent decline in the Hang Seng Property Index over the same period. By 28 May 2012, SHKP had lost a fifth of its market capitalisation since the arrests on 29 March 2012.[26]

Even though the ICAC had commenced legal actions against the senior management of SHKP, the company was not a party under any direct legal action. With regards to board and management, two independent non-executive directors were appointed to strengthen the board, and two deputy managing directors were appointed to assist the co-Chairmen as alternate directors in the event of their absence from board meetings. Investors viewed this news positively as was evident from the increase in stock price and trading volume. However, analysts from Barclays, Bank of America Merrill Lynch and CreditSights were still uncertain about the future of SHKP, citing problems of corporate governance and succession planning.[27]

On 13 July 2012, SHKP requested for a suspension of trading of its securities pending the release of an announcement which was price sensitive. On the same day, Thomas Kwok, Raymond Kwok and Rafael Hui were formally charged with offences linked to bribery and misconduct by Hong Kong's ICAC.[28] SHKP resumed trading on 16 July 2012.

The Charges

The charges that the two Kwoks and Rafael Hui faced include providing false information, misconduct in public office, conspiracy to commit misconduct in public office, and offering an advantage to a public servant. In total, it was alleged that Rafael Hui accepted approximately HK$34 million in cash and unsecured loans as well as exclusive rent-free use of two luxury apartments in Happy Valley between June 2000 and January 2009.

According to the ICAC,

- Rafael Hui received "the rent free use of two flats and three unsecured loans totalling HK$5.4 million" from a Sun Hung Kai subsidiary and did not disclose or declare this to Hong Kong government and the Mandatory Provident Fund Authority (MPFA).

- Rafael Hui, during his tenure as Chief Secretary, accepted "HK$5 million from Thomas Kwok for remaining favourably disposed to Thomas Kwok and/or his interests."

- Rafael Hui, during his tenure as Chief Secretary, accepted "HK$4.125 million through a company owned by Hui from SHKP for Hui's remaining favourably disposed to Raymond Kwok and/or his interests."

- Rafael Hui and Raymond Kwok both face "one count of furnishing false information on an invoice to purportedly show that the payment of HK$4.125 million was for settlement of consultancy services provided by Hui."

- Rafael Hui and Raymond Kwok conspired "to offer Hui the annual extensions of an unsecured loan of HK$3 million advanced by the [Sun Hung Kai] subsidiary. . . as a reward for Hui to remain favourably disposed to Raymond Kwok and/ or his interests."

- Rafael Hui, during his tenure as Chief Secretary, accepted "a series of payments totalling HK$8.35 million from Thomas Kwok, Thomas Chan and Francis Kwan for Hui's remaining favourably disposed to Thomas Kwok and/or his interests."

- Rafael Hui, Thomas Chan and Francis Kwan conspired "to offer Hui a series of payments totalling HK$11.182 million from Chan and Kwan as a reward for Hui to remain favourably disposed to Chan and/or his interests."[29]

As of May 2014, the Kwok brothers and Hui pleaded not guilty to the charges, including misconduct in public office and furnishing false information.[30] More charges continue to be added to the case; for instance, Raymond Kwok faces additional charges for conspiracy with Hui to commit misconduct in a public office.[31] The trial is estimated to last until the end of September and possibly into October 2014, and SHKP issued a statement that the case has not and will not affect the company's operations.[32]

In the Public Eye

The SHKP case is seen to be the highest-profile case involving alleged corruption in Hong Kong. This case has attracted great public attention not only because the Kwoks are some of the most prominent, influential and wealthy businessmen in Hong Kong, but also because the arrests coincided with the election of the new Chief Executive of Hong Kong, Mr Leung Chung-ying. Further, with this being the first arrest of anyone who has held such a high post in the government sector, and with the involvement of the Kwok family, it certainly jolted Hong Kong society's view on the relations between the government and private sector.[33]. As mentioned by Joseph Wong, a former senior government official, "this is not good for the image of Hong Kong, which used to have a high reputation for integrity."[34] This incident will only raise more doubts about corporate governance in Hong Kong and the ethics of its senior government officials.

Another concern which surfaced relates to the appointment of Adam and Edward Kwok to the board. Peter Churchouse, Chairman & MD at Hong Kong-based property investment company Portwood Capital, suggested that this appointment may cast some doubt for investors as they may question if Adam and Edward Kwok, aged 29 and 31 respectively, are "really equipped to be running a US$32 billion market cap company at this tender age."[35]

The economic slowdown in China and the uncertain global economic landscape are already starting to affect the property sector in Hong Kong. Now, with the bribery charges and family strife at SHKP, the leadership at SHKP faces a tough challenge of guiding the company out of this corporate governance crisis.

GlaxoSmithKline: The Etiquette of Bribery

"This is shameful. And personally, it is deeply disappointing."
– Andrew Witty, Chief Executive Officer (CEO) of GSK

Case Overview

The business of GlaxoSmithKline (GSK) is a noble one. Its company's mission statement states: "Our mission is to improve the quality of human life by enabling people to do more, feel better and live longer." Yet, the Chinese saying "金玉其 外，败絮其中" (the appearance may look good, but what lies beneath is far from good) seems to aptly describe GSK. The company has been embroiled in many scandals, including the largest healthcare fraud case in the U.S. which required a settlement amounting to US$3 billion.[1] In June 2013, reports emerged alleging that senior executives of GSK China were involved in the bribery of doctors and government officials. This case can be used to discuss issues such as the responsibility of the Board over corporate governance; the obligation of the parent of a company group to properly govern the activities of its foreign subsidiaries; and the difficulties of enforcing good corporate governance in countries where corrupt or unethical practices in the industry may be considered a norm.

China: A Breeding Ground for Corruption?

"Distinguishing between money spent on corruption with money spent on developing relationships can be difficult, as it is a significant part of the way business is done in China." – Lucinda Chow, media commentator[2]

Guanxi is a key part of the Chinese business environment. It is characterised by the formation of close and informal relationships between individuals and institutions with great reliance within the network for support, cooperation and subsequent transactions. Guanxi practices have flourished in China, forming the basis of many transactions entered into amidst lax regulations. The presence of such cultural norms has created much subjectivity in judging the substance of transactions, especially from a legal standpoint.[3]

Despite recent policy revisions in the Chinese regulatory environment, the current system is still perceived as one that lacks fair and consistent enforcement, with a lack of independence in the judiciary process, especially in litigation involving state-controlled organisations.[4]

The Good, The Bad and The Ugly

China's highly regulated environment means that the state fixes the costs of operations. In addition, costs of many medicines are capped, leaving hospitals little room to top up the wages of their staff. A newly-graduated doctor in Beijing earns about 3,000 yuan (US$490) a month including bonuses, approximately the same as a taxi driver.[5] Compensation under the current medical system involves two tiers, where doctors are paid a low base salary and a variable wage, depending on the number of prescriptions made to patients.[6] Bribes are thus seen as essential income supplements, in some cases making up to 80 percent of a doctor's monthly pay,[7] as doctors are unable to survive solely on their salaries.

Notwithstanding tight regulations, the Chinese healthcare system has remained consistently underfunded. With the government reducing public healthcare spending, provision of healthcare services falls largely to the private sector. The autonomy granted to private companies has fuelled opportunities for corrupt practices such as extensive back-door payments to doctors by pharmaceutical firms to ensure doctors prescribe their products.[8]

GSK, The Healthcare Giant

GSK was formed in 2000 following the merger of Glaxo Wellcome and SmithKline Beecham. The company deals mainly in pharmaceuticals, vaccines and consumer healthcare, and is one of the global leaders in healthcare research and development9.

Headquartered in London, GSK is listed on the London Stock Exchange and the New York Stock Exchange. The pharmaceutical giant has an established presence worldwide, with offices in over 115 countries.[10] GSK has sizeable operations in China, with eight subsidiary companies and a total investment exceeding US$500 million.[11]

Despite the challenges of internationalisation, GSK has remained largely profitable throughout, turning in annual net profits averaging £4.32 billion in the last five years.[12]

The People Running the Show

In 2012, the Corporate Executive Team consisted of 16 individuals, led by Chief Executive Officer (CEO) Sir Andrew Witty. The organisational structure was both functional and geographical, where executives either oversaw particular regional units or areas of focus.[13]

The Board comprised of 15 members. Sir Christopher Gent, who had been on the Board for the past nine years and Chairman for over eight years, led the Board. Out of the 15 members on the Board, three directors were executive, with the remaining directors being non-executive. The three executive directors, Sir Andrew Witty (CEO), Simon Dingemans (CFO) and Dr Moncef Slaoui (Chairman of Global R&D and Vaccines), sat solely on the Finance Committee. Out of the three executive directors, Slaoui has been serving for the longest period, at 8 years.[14]

All the 12 non-executive directors were deemed to be independent in accordance with the United Kingdom (U.K.) Corporate Governance Code. In addition, there was also a Senior Independent Director (SID), Sir Robert Wilson, whose role was to 'act as a sounding board for the Chairman and a trusted intermediary for the other Directors',[15] and 'as an additional point of contact for shareholders'.[16] GSK also had a strong female board representation at 33 percent, after the additional appointments of Lynn Elsenhans and Jing Ulrich as non-executive directors in July 2012.[17]

Currently, the Board comprises of six committees, namely the Audit & Risk Committee, Corporate Responsibility Committee, Remuneration Committee, Finance Committee, Nominations Committee and the Corporate Administration & Transactions Committee.

The Board has strived to ensure that its non-executive directors are drawn from a wide range of industries including pharmaceuticals and healthcare, medical research and academia, and retail and financial services, with appropriate experience and global reach.[18]

Corporate Governance In GSK: Actions (Should) Speak Louder Than Words

"We put the interests of patients and consumers first and are driven by our values … in everything we do."
–GSK Corporate Governance Report, 2012

According to GSK's annual report, corporate governance in the company is founded upon the twin tenets of integrity and transparency. All employees in GSK are governed by its code of conduct, which has recently been streamlined and simplified by the company.[19] The code reminds GSK employees to "be mindful of acceptance and provision of entertainment and gifts."[20] Through its guidelines, it also seeks to avoid corrupt practices, while serving as a tool to prevent and detect fraud.

GSK's numerous corporate governance disclosures serve to highlight its tough stance towards bribery and corruption, with the company describing itself as having a "zero-tolerance approach".[21] GSK also has a whistleblowing policy with a global confidential reporting line that allows employees to report suspected cases of misconduct.[22]

All these measures put in place have helped GSK ensure its compliance with the U.K. Code. However, while GSK has corporate governance mechanisms that are detailed, abundant and comprehensive,[23] the enforcement of those mechanisms appears questionable. In 2002, the company came under scathing criticism for its blatant disregard of a whistleblower's claims, amidst allegations of management's attempts to cover up drug manufacturing defects, in what has been described as a "gross failure of governance".[24]

What Lies Beneath the Façade

"I want to make it very clear that we share the desire of the Chinese authorities to root out corruption wherever it exists. We will continue to work together with the MPS (Ministry of Public Security) and we will take all necessary actions required as this investigation progresses."
– Abbas Hussein, GSK's President of Europe, Japan, Emerging Markets

& Asia Pacific (EMAP)[25]

In June 2013, GSK was accused of funneling bribes to government officials and doctors by transferring money through travel agencies. Bribes were allegedly given in the form of arranged travel and cash payments to doctors as "lecture fees", though no training schedule was provided during the trips. The case surfaced when police investigations uncovered that Shanghai Linjiang International Travel Service's annual turnover escalated from millions to hundreds of millions despite low business, and it was later observed that the agency had conducted business dealings with GSK since 2007.[26]

In July 2013, GSK's headquarters in Shanghai was raided, following which a number of GSK China executives were detained. These included two vice presidents, a legal affairs officer and a business development manager, who together reportedly gave bribes of up to RMB3 billion.[27] One of the executives later appeared on state television to confess to the allegations.[28]

Huang Hong, general manager of GSK's operations in China, revealed that GSK set high annual sales growth targets of up to 25 percent, which was 7 percent above the industry growth average. Such high targets coupled with the variable salary structure were alleged to have encouraged "dubious corporate behaviour".[29] The Chinese police then began investigations to find out if GSK indeed had a structured bribery programme, despite GSK's denial and shifting of blame to individual executives who the company said had "acted outside of processes".[30]

Four travel agencies were allegedly used to funnel bribes, some of which also offered sexual favours to GSK's senior executives to preserve business ties.[31] In addition, documents revealed that once GSK had established relationships with doctors, sales staff gave them cash incentives of 100 yuan per prescription, as well as continuing-education credits to help meet hospital requirements.[32] Huang also admitted that GSK had a separate team which was allocated an annual budget of 10 million yuan to maintain ties with key hospital executives.[33] This resulted in doctors relying a high prescription of drugs to raise their incomes. In an interview, Shanghai-based doctor Zhang Qiang revealed that it was customary for doctors in his country to receive hongbao payments from pharmaceutical representatives.[34]

GSK's Response

In response, CEO Andrew Witty ordered Europe, Japan and EMAP President, Abbas Hussein, to lead negotiations with the government, along with a team of senior lawyers and auditors. GSK's internal probe uncovered evidence that the detained executives had received cash through the fraudulent use of special VAT invoices and issued false invoices in violation of PRC tax rules.[35] Ernst & Young was later engaged as an external independent auditor.[36]

Hussein subsequently issued a statement in which he apologised, and communicated that GSK was disappointed by the ethical misconduct of its executives as well as its third-party contractors and agencies. Hussein expressed GSK's desire to cooperate with the Chinese police to root out corrupt practices, and pledged that the company would lower prices to make its medicines more affordable.[37] CEO Witty also expressed his "disappointment" in the event, adding that talks were already in place with U.S. and U.K. regulators.[38]

To tighten governance within the company, GSK appointed one of its top European executives Herve Gisserot, senior vice president for Europe, as the new head of operations in China. Mark Reilly, the incumbent head of operations, was slated to remain as a senior member of the management team. Gisserot was tasked with ensuring minimal disruptions to GSK's China operations amidst the ongoing investigations.[39]

GSK's response drew mixed reactions from the public. According to China analyst Andrew Hupert, the Chinese prosecutors had wanted it to issue a "Chinapology", which was "a brief, to-the-point admittance of guilt and expression of sorrow over one's misdeeds in public."[40]. However, doing so would be a violation of the U.S. Foreign Corrupt Practices Act and the U.K. Bribery Act, both of which governed GSK and were applicable to acts of bribery committed abroad. Faced with this quandary, GSK never fully admitted to its wrongdoings in China.[41]

Impact on Business

GSK has seen its sales in China dip by 60 percent since investigations began in June.[42] Major hospitals refused entry to GSK's sales representatives. In September 2013, rumours surfaced that GSK was considering pulling out of China, a market which generated 3.6 percent of GSK's revenues, despite seeing double-digit sales growth in recent years.[43] A senior industry figure in China revealed that GSK's reason for pulling out of the country could be the size of the fine (potentially £2 billion) it faced, as well as the severance of ties with major local hospitals, leading to increasing difficulty of doing business.[44]

What's Next? The Aftermath of the GSK Fiasco

"We very clearly recognise there is a profound need to earn the trust of Chinese people again. We will take every action to do so."
– Andrew Witty, CEO of GSK[45]

In October 2013, CEO Witty insisted the pharmaceutical giant would not pull out of China despite the lurid corruption scandal that had wiped out two-thirds of its business in the world's second-largest economy.[46] GSK China remains a "multi-hundred million pound business" despite the fall in sales, making it unlikely that this lucrative market will be given up.[47] While the GSK scandal will inevitably increase compliance costs, the industry will look back at this moment as a necessary step forward in the effectiveness of China's healthcare system and the measures they will need to put in place to avoid future recurrences of such incidents.

HSBC: The World's Local (Laundry) Bank

Case Overview

In December 2012, banking giant HSBC was fined US$1.92 billion by the U.S. authorities over allegations of money laundering and partaking in illegal financial activities. This was following the release of a detailed investigation report in July 2012 by the U.S. Senate Permanent Subcommittee on significant lapses in HSBC's counter-terrorism financing systems and anti-money laundering programme. Despite having been issued several warnings to reinforce its anti-money laundering programs over the past seven years, HSBC failed to make the proper adjustments. The US$1.92 billion penalty was at that time the largest fine ever in a case involving a bank and also brought significant reputational damage to the company. This case can be used to discuss issues such as the effectiveness of whistle blowing policies and ethical codes in preventing fraudulent behaviour amongst employees; as well as the relationship between sound internal control and good corporate governance.

The Making of a Fall

"The HSBC settlement sends a powerful wake-up call to multinational banks about the consequences of disregarding their anti-money-laundering obligations."[1]
– Senator Carl Levin[2]

HSBC has over 7,200 offices in more than 80 countries and reported US$20.6 billion of profits before tax in 2012.[3] It was ranked as the world's third largest bank in terms of market capitalisation in 2013.[4]

Although HSBC had a code of conduct and a whistle blowing policy that served as a guide for doing business, its poor compliance culture led to numerous accusations of money-laundering violations over the years.

In the 340-page report produced by the U.S. Senate Permanent Subcommittee on Investigations, it revealed that at the root of HSBC's money-laundering practices was a confluence of factors – structural inadequacies of HSBC's Anti-Money Laundering (AML) Program, as well as the Office of Comptroller Currency's (OCC) failure to enforce regulations to prevent HSBC's wrongdoings.[5] Moreover, the investigation report also illustrated the means through which HSBC's money-laundering practices were carried out - through its dealings in Mexico, bypassing the U.S. Treasury Office of Foreign Assets Control's (OFAC) filters, as well as its persistence in trading with terrorist-affiliated counter-parties.[6]

The Risky Mexico Affiliate

"It was a financial institution with inadequate AML resources, inadequate AML systems and controls; and AML leadership"
– U.S. Senate Committee Report

HSBC USA (HBUS) has correspondent accounts with hundreds of affiliates located in over 80 countries. These accounts can be used for cashing in USD instruments such as travellers cheques, and account for "63% of all US$ payments processed by HBUS."[7] One such affiliate is HSBC Mexico (HBMX), which handled almost US$2 billion in assets and over eight million clients.[8]

Prior to HSBC's acquisition of the Mexican affiliate, the U.S. State Department had already alerted HBUS to the fact that Mexico was a place with "high incidents of drug trafficking" as international money launderers used it as a vehicle to introduce their drug proceeds into the "global financial system."[9] Despite this warning, HBUS still classified HBMX as a "low-risk" affiliate through its country-specific risk assessment process.[10]

Other than operating in a high-risk location, HBMX also had a history of severe AML deficiencies. Its problems included a pervasive lack of Know Your Customer (KYC) information in client files; database of high profile clientele connected to drug trafficking allegations; and a huge backlog of accounts earmarked for closure due to suspicious activities.[11]

"These traffickers didn't have to try very hard...They would sometimes deposit hundreds of thousands of dollars in cash, in a single day, into a single account, using boxes designed to fit the precise dimensions of the teller windows in HSBC Mexico's branches."[12]
– U.S. Assistant Attorney General Lanny Breuer[13]

Since HBUS previously categorised HBMX as a low-risk affiliate,[14] the AML monitoring system failed to detect US$881 million of suspicious dealings.[15]

During the five-year period from 2005 to 2010, the OCC (Office of Comptroller Currency) – whose job is to supervise and regulate national banks[16] - conducted over four dozen AML examinations and highlighted at least "83 AML matters requiring attention."[17] Despite this, the OCC took no formal or informal enforcement actions, thus allowing HSBC's AML deficiencies to fester. Further findings of the investigation also revealed that HBMX were fully cognizant of these money-laundering activities.

Circumventing OFAC Filters[18]

In 2001, HSBC European Union (HBEU) proposed to use its correspondent account with HBUS to clear U-turn transactions involving Iran's Bank Melli,[19] and was approved upon review.[20] HBEU then requested all U-turn transactions to be done via bank-to-bank transfer, and structured to hide the origins of transactions, so that information about the origins would not trigger the OFAC filter.[21] Even though HBUS' Compliance Head rejected this request,[22] HBEU instructed Bank Melli to make "cover payments",[23] which effectively concealed Bank Melli's role in laundering money through HBEU into the U.S. financial system.

"HSBC knew what was going on, but allowed the deceptive conduct to continue"
– Senator Levin

Although HBUS' compliance executives consistently reminded HBUS to require full disclosures of Iranian transactions,[24] HBEU and HSBC Middle East (HBME) repeatedly sent U-turn transactions through U.S. dollar accounts at HBUS without disclosing the Iranian links.[25] Some HBUS officials even pretended that they knew nothing about processing these deceptive U-turn transactions.[26]

Disregarding Links to Terrorism – Al Rajhi Bank (ARB)

ARB has US$59 billion of assets and is the largest private bank in Saudi Arabia.[27] For more than 25 years, HSBC provided ARB with a large variety of banking services, including providing US dollars through a Banknote account. In 2002, U.S. agents revealed that Sulaiman Al-Rajhi, one of the Bank's founders, provided finances to Osama bin Laden's "Golden Chain"[28] terrorist activities.

Because of ARB's alleged terrorism links, the U.S. placed the bank under inspection and included it in the OFAC filter list.[29] Upon subsequent recommendations by HSBC Group's Compliance Chief, HBUS decided to sever ties with ARB in 2005.[30] Just four months after the declaration to terminate business relationships with ARB, HSBC Group Compliance made another announcement that HSBC affiliates were allowed to resume business with ARB.[31] Meanwhile, ARB threatened to stop dealing with HSBC entirely if their Banknote account was not reinstated.[32] Hence, HBUS Compliance approved the recommencement of business between HBUS with ARB in December 2006.

HSBC only decided to exit the business of selling U.S. banknotes[33] after the OCC's criticism[34] in 2010, thus ending its contentious relationship with ARB.

Aftermath – Changes In HBUS

"We accept responsibility for our past mistakes. We have said we are profoundly sorry for them, and we do so again."[35]
– HSBC Group Chief Executive Stuart Gulliver

To reduce future money-laundering risks, HBUS has embarked on a variety of measures to strengthen its internal controls. These include the implementation of stricter KYC standards,[36] and subjecting non-U.S. group affiliates to similar due diligence as non-affiliates. In addition, to further reduce its exposure to high-risk transactions, HBUS terminated 109 correspondent relationships. New monitoring systems for wire transactions and improved customer risk rating methodology have also been developed.[37]

As a means of internal disciplining, HBUS clawed back bonuses from their AML and Compliance Officers. It also increased spending on AML controls by nine times to address the inadequate staffing and also to reorganise its AML department.[38]

Too Big To Jail

It's a dark day for the rule of law.
– New York Times Editorial, 11 December 2012

Upon the conclusion of the investigation by the U.S. federal and state authorities, it was decided that no charges would be pressed against any of the HSBC officials.[39] Despite the gravity of the matter, HSBC would only have to pay a US$1.92 billion settlement,[40] which was insignificant relative to the US$20.6 billion profit before tax HSBC earned in 2012.[41]

The decision not to prosecute HSBC was driven by the fact that HSBC employs nearly 16,500 workers in the U.S. Should the bank face criminal charges, it would lose its license and cost thousands of Americans their livelihood.[42] Therefore, it was purportedly for society's good that the bank was not prosecuted.[43]

Although Columbian drug traffickers who took advantage of HSBC's lax regulations were charged with time in prison, the HSBC employees who allowed for such poor regulations escaped unscathed.[44] Even with the fine of an unprecedented amount of US$1.92 billion, the passing of a no-jail sentence begs the important question – are global banks really too big to jail? Nobody, not even Senator Carl Levin, has an answer to that, at least not for now.

Shell in Nigeria: "Safe Sex"?

Case Overview

Since 1998, OPL245 – one of Nigeria's massive offshore oil blocks – has been changing hands between the Federal Government of Nigeria ("FGN"), Royal Dutch Shell plc ("Shell") and Malabu Oil and Gas Ltd ("Malabu"), a shell company widely believed to be controlled by the former oil minister from the corrupt Abacha-era regime, as well as convicted money launderer – Chief Dan Etete.

In 2011, Shell and its partner ENI eventually reached an agreement with the FGN to take ownership of the block from Malabu for an inflated price of US$1.3billion. However, this was not the last of the OPL245 controversy. The tripartite arrangement between buyer, seller and FGN sparked international debate about FGN's ambiguous role in the transaction, as well as the legitimacy of the Malabu shell company. Consequently, Shell's willingness to carry on such shady dealings catapulted its ethical stance into the media spotlight, with industry analysts and the relevant authorities questioning if Shell in fact used the government as a "condom" - a protection layer to distance themselves from the secrecy and illegitimacy shrouding this shadowy deal with Malabu. This case can be used to discuss issues such as money laundering; the effect of countries' corruption on multi-national corporations' transparency and reporting; and possible measures to prevent these corporations from taking advantage of weak governments to reap profits.

In a Nut(Shell)

Shell is a holding company that owns, directly or indirectly, investments in the numerous companies constituting Shell.[1] Shell is engaged worldwide in the oil and gas industry and also has interests in chemicals and other energy-related businesses.[2] It is incorporated in the U.K. and headquartered in Netherlands, with its shares traded on London Stock Exchange (primary listing), Euronext Amsterdam and New York Stock Exchange.[3]

Organisation Structure

The structure of Shell may be viewed in terms of a share ownership perspective or a management perspective. The management structure of the Shell Group does not correspond strongly to its formal ownership structure.

In terms of ownership structure, only two companies are directly held by Shell – Shell International Finance B.V. (which provides funding to other members of Shell Group) and Shell Petroleum N.V.[4] Besides these two companies, there are 177 other significant subsidiaries in more than 70 countries, most of which have 100 percent share capital held indirectly by Shell.[5] The exact linkages and percentages of ownership between Shell and its subsidiaries are not known, as many of these subsidiaries are private companies with undisclosed financial information. Hence, looking at its management structure might shed more light on this complex group.

Shell has a unitary board of directors and a Chief Executive Officer (CEO) at the group level.[6] Its businesses are separated into 3 divisions – Upstream (which is further divided into two geographically focused divisions – Upstream Americas and Upstream International), Downstream, and Projects and Technology, while its non-operating businesses go under the Corporate division.[7] These operating and non-operating divisions are each headed by an executive director. The Upstream International and Downstream divisions are split further into the different countries the businesses operate in and each country has a Country Chairman. Shell's subsidiaries are categorised under Upstream, Downstream and Corporate and are subsumed under these divisions. Each subsidiary also has its own management team.

Shell and Ethics

Shell purports to have a set of three core values - "integrity", "honesty" and "respect for people."[8] To demonstrate its commitment to these values, Shell established three sets of employee guidelines, namely Shell General Business Principles,[9] Code of Conduct[10] and Code of Ethics.[11]

Corruption in The Oil Industry

In sharp contrast with Shell's purported strong commitment to ethics and business integrity, the oil industry is often associated with corruption. Transparency International's Corruption Perception Index (CPI) indicates that many oil-rich regions are high in corruption.[12]

However, corruption in these oil-rich countries is not the sole contributor to the alleged widespread corruption in the oil industry. Many oil and gas companies, both big and small, often do not include country-specific financial information in their financial statements, thus allowing secret payments made to corrupt leaders to go undetected.[13]

Nigeria and Corruption

One of the countries where Shell operates in is Nigeria. Nigeria, situated in the resource-rich continent of Africa, accounts for 2.9 percent of the world's oil and gas reserves.[14] The country, like many other oil-rich ones, is no stranger to corruption – since the release of the CPI in 1998, Nigeria has consistently scored way below average.

Did Shell Practise "Safe Sex" in Nigeria?

1998: Award of OPL245 to Malabu

The story of OPL245 began in 1998. Under the Abacha administration, Nigeria's then-Minister of Petroleum, Dan Etete, awarded the OPL245 concession to Malabu.[15] Malabu was a company registered on 24 April 1998, just 5 days before the award,[16] had no employees or assets, and had three shareholders, including one Kweku Amafagha. The price for the oil block was a "signature bonus" of US$20 million, but Malabu only ever paid US$2 million of this required US$20 million.[17] Three months later, Abacha died, ending 16 years of military rule and a new government took power in 1999 under the administration of Olusegun Obasanjo.[18]

2001: "Farm-in" Agreement Between Malabu and Shell

Although Malabu had secured the rights to OPL245, it had problems extracting the oil. OPL245 was an ultra-deepwater block[19] populated with many deeply-submerged oil wells. Only top global oil companies like BP, Chevron and Shell had the specialised deepwater drilling technology to access such oil wells.[20] Malabu, on the other hand, was an empty holding company with no deepwater drilling capabilities. Moreover, Malabu did not want to assume all the development risks involved. Thus, in March 2000, a representative from Malabu approached Shell Nigeria Ultra Deep Limited (SNUD), a subsidiary of the Shell Group, with a proposal for a "farm-in" agreement, under which the owner of a working interest in a natural gas and oil lease assigns the working interest to another party (the "farmee"),[21] in return for a share of the income generated from the farmee's activities.[22] In this case, Malabu proposed to give Shell a 40 percent equity stake in OPL245.[23]

As part of due diligence for the transaction, Shell made enquiries with the Assistant Director of the Department of Petroleum Resources (DPR), Andrew Obaje, on 31 March 2000. Obaje confirmed to Shell that the map of allocated concessions indicated that OPL245 had been owned by Malabu since April 1998 and was currently in good standing.[24] He also explained that the FGN did not intend to revoke the allocation since Malabu had dutifully paid the required "down payment". In addition, Shell received verbal assurances from the then-Vice-President of Nigeria that there was no objection from the FGN to Shell acquiring an interest in OPL245.[25]

Therefore, after extended negotiations, the OPL245 Deed of Agreement between Malabu and Shell was finally effected in early 2001.[26]

2001: Withdrawal of Concession to Malabu

However, on 2 July 2001, the new FGN under President Obasanjo suddenly transferred ownership of the block to Nigerian National Petroleum Corporation (NNPC). Shell and ExxonMobil were informed that they would be formally invited to bid for the role of contractor in a production sharing agreement (PSA) with NNPC.[27]

Although Malabu retaliated by threatening to commence legal proceedings against the FGN to assert its proprietary interest in OPL245, the FGN continued with the bid solicitation process. On 23 May 2002, Shell won with a bid of US$210 million.[28]

2006: Reinstatement of Malabu as Owner

In 2006, the FGN took yet another U-turn and reinstated Malabu as the owner of OPL245. This reversal by the FGN took Shell by surprise. However, with Shell already incurring a significant amount of expenses with respect to the oil block,[29] Shell was unwilling to relinquish their rights to operate in OPL245 and thus instituted legal action against the FGN.[30]

In addition to instituting lawsuits, Shell also tried to deal directly with Malabu's representative, Dan Etete. Both Shell and ENI, an Italian oil giant, had separately tried to broker a deal directly with Etete regarding OPL245. However, both Shell and

ENI admitted that direct dealings with Etete broke down as they felt that Etete was "impossible to deal with."[31]

It is also noteworthy that during Shell's ensuing negotiations with Etete, Etete was convicted for money laundering in the French courts in 2007, and in 2009, his court appeal was rejected.[32] Despite knowing about Etete's conviction, Shell did not break off dealings with him. It was revealed in court that Shell officials had lunch and 'lots of iced champagne' with Etete even subsequent to his money laundering conviction.[33]

2011: Shell and ENI's Joint Partnership

Due to the failure of Etete's direct negotiations with Shell and ENI, Malabu hired Ednan Agaev to act as the middleman. Agaev in turn subcontracted Emeka Obi, a Nigerian from Energy Venture Partners.[34] After a series of discussions facilitated by Obi and Nigeria's attorney general, Mohammed Bello Adoke, Shell and ENI eventually agreed on 29 April 2011 to jointly share ownership of OPL245. In addition, it was decided that Shell and ENI would pay US$1.3 billion to the FGN,[35] which would in turn deduct Malabu's unpaid signature bonus of US$210 million before remitting the remainder – about US$1.1 billion – to Malabu.[36]

2011: Malabu's Legal Troubles

Despite reaching an amicable settlement with Shell and ENI with regard to OPL245, Malabu was once again put under the legal spotlight towards the end of 2011 when it was sued by its middlemen, Obi and Agaev. Although the real beneficial ownership of Malabu was not an issue of contention, the hearings uncovered a lot about the matter. It was revealed that "Kweku Amafagha" was in fact just Etete's alias, and that not only was Etete the company's main negotiator and its representative in the High Court, he was also the sole signatory on its bank accounts. All these evidence pointed to Etete being the real beneficial owner of the company, despite his assertions that he was merely a consultant to the firm.

To exacerbate Malabu's legal troubles, Nigeria's Economic and Financial Crimes Commission (EFCC) launched an inquiry into Malabu in 2012 due to allegations made by Mohammed Abacha that he was a founding shareholder who had been illegally cut off. EFCC's investigations were presented in a report stating, "Investigations conducted so far reveal a cloudy scene associated with fraudulent dealings. A prima facie case of conspiracy, breach of trust, theft and money laundering can be established against some real and artificial persons."[37]

In addition, documents from the EFCC reports showed that out of the US$1.3 billion transacted in the deal, US$800 million was paid in 2 tranches into Malabu accounts, which were then transferred to five anonymous Nigerian shell companies suspected to be owned and controlled by cronies of current FGN officials. In fact, it was discovered that one such person was Abubakar Aliyu, an individual known for shady business deals and close ties with the current President Goodluck Jonathan.[38] This lack of disclosure of the recipients of the payments has raised concerns as to who truly benefitted from the deal.[39] However, EFCC investigations unofficially ceased when President Jonathan got wind that Aliyu was involved.[40]

2012: Shell's Legal Troubles
The EFCC's discovery that monies were routed to Malabu led the British Metropolitan Police's Proceeds of Corruption Unit to question whether Shell is guilty of money laundering which potentially makes Shell liable under the U.K. Bribery Act.

However, Shell insisted that it bought OPL245 legitimately from the FGN, and did not make corrupt payments to Malabu or other parties. Nevertheless, many critics argued that it was a two-part transaction, and an intentional and deliberate scheme by Shell to interpose the FGN as a "protective layer" between the company and Malabu. As Global Witness campaigner Tom Mayne said, "It's obvious…that they agreed that the deal be structured in such a way that it went through the government…a 'safe-sex' transaction, with the government acting as a 'condom' between the buyers and seller." To date, Shell vehemently denies having any knowledge that Etete and Malabu were corrupt, and hence maintains that there was no intention to use the FGN as a conduit to launder money for Malabu.

What is Happening Now?

"From its incorporation and at all material times, Etete had a substantial beneficial interest in Malabu."
– Justice Elizabeth Gloster, U.K. Judge for Malabu court case

There have been important developments in the lawsuits involving Malabu. The case raised by Agaev was recently settled behind closed doors, while the U.K. High Court passed a ruling on 17 July 2013 that Obi should be paid at least US$110.5 million by Malabu. It was also conclusively held by the U.K. judge, Justice Elizabeth Gloster, that Etete was in fact a hidden beneficial owner of Malabu "from its incorporation and at all material times,"[41] thus confirming that Etete had corruptly awarded OPL245 to himself back in 1998. In February 2014, an ad-hoc committee of Nigeria's House of Representatives set up to investigate the sale of OPL245 to Shell and Eni recommended that the government revoke the oil block license granted to Shell.[42]

The Transparency Movement

The movement towards a global standard of transparency in the extractives sector (oil, gas and mining companies) has been gaining momentum in recent years. With the adoption of the European Union (EU) Accounting and Transparency Directive in June 2013,[43] all 28 EU Member States are required to introduce payment disclosure legislation for extractive companies by July 2015.[44] Under these legislation, oil, gas and mining companies listed on EU stock exchanges will be required to report payments they make to governments on a country-by-country and project-by project basis with no allowance for exemptions. Canada, Norway and Switzerland have also recently announced plans to enact similar legislation.[45]

This new global standard of a common, mandatory reporting regime for extractive industries will allow citizens of resource-rich countries and civil society to identify what deals are being made on their behalf for their natural assets, thus helping to combat cases of corruption in which the country's natural resources are misappropriated by the government.[46]

Shell's Commitment to Transparency

Despite Shell's public statements and internal codes indicating their support for transparency, Shell was a key protagonist in efforts to water down the transparency laws under the EU directive.

In addition, Shell (under the auspices of the American Petroleum Institute) also filed a legal challenge in America claiming that laws in countries such as Angola and China ban revenue payments disclosures,[47] and hence payments in these countries should be exempted from disclosure. This is despite the fact that oil companies have failed to prove their claim that payment disclosure is outlawed in any oil-producing country.[48]

Are these actions justified? Or is it just a bid to keep deals with corrupt countries secret? This issue has definitely raised concerns and questions for oil companies like Shell and their commitment towards the global transparency movement. As Brendan O'Donnel from Global Witness advocates, "Shell, BP and others should stop swimming against the tide of transparency and rescind their effort to kill off similar legislation in the U.S."[49]

Leighton Holdings: Building Bribery

Case overview

Allegations relating to a culture of corruption, bribery and cover-ups involving Leighton Holdings (Leighton), the world's 12th largest contractor by revenue, shook the Australian corporate landscape in October 2013.[1] It was reported that company executives of the Australian construction empire had known of various kickbacks paid to secure projects, and that payoffs made to Leighton employees had happened as early as 2009. Early warning signs that executives may be involved in rampant corruption and mismanagement had been observed. Other internal company documents also revealed a corporate culture that accepted and rewarded corruption, leading to a scrutiny of excessive remuneration packages paid out to former senior executives. The Leighton saga placed regulatory bodies in the spotlight, as the media and politicians heavily criticised regulators' lack of prompt and thorough investigations, which allowed the incident to manifest. This case can be used to discuss issues such as corruption and bribery; the response of the board, management and regulators to bribery allegations; tone at the top, remuneration and other corporate governance practices in reducing bribery and corruption risks; and corporate governance in company groups.

Leighton on the Rooftops

Leighton is a project development and contracting group headquartered in St. Leonards, Australia. Its principal subsidiaries comprise of Leighton Contractors Pty Ltd, Thiess Pty Ltd, Leighton Asia Limited, John Holland Pty Limited and Leighton International Limited (Leighton International) and operate in Australia, Asia, the Gulf region and Africa.[2] Leighton provides engineering, building construction, facilities management and contract mining services.

The Bricks of Bribery Laid

"I asked did Wal K approve this? And he said 'yes'." - Memo by David Stewart, then acting Chief Executive[3]

A series of articles by Fairfax Media in Australia that began on 3 October 2013 revealed the existence of a handwritten memo by the acting Chief Executive of Leighton, David Stewart, on 23 November 2010.[4] According to the memo, David Savage, former Managing Director of Leighton International, and Wal King, who was the Leighton CEO for 23 years, were aware of and approved an A$42 million kickback paid to a Monaco-based company, Unaoil. Unaoil was "nominated by Iraqi officials who selected Leighton for a A$750 million oil pipeline contract".[5] The payments were called "project support" fees in the contract. The fees were to be reviewed by the Board of Leighton International, including King, who was also part of the Board. However, these fees had "mysteriously disappeared… when they were revised by top Leighton's staff one month later."[6]

“He [Savage] said less than 50 percent of the payment.” - David Stewart’s memo on questioning the proposed payment and the real value of the work to extend the Iraqi contract.[7]

Court documents also revealed the existence of Memorandum of Agreements in early 2011 between Unaoil and Leighton to guarantee a minimum payment of US$55 million for “construction and marketing fees in the event that the Iraqi government awarded Leighton with a second pipeline contract” that was worth US$500 million.[8] Of this US$55 million, marketing-specific fees were specified to be “no less than US$25 million”, even though no actual marketing services were required.[9]

Man of Steel

A specific incident involving Gavin Hodge, senior project manager for the building of an Indonesian barge, revealed senior executives’ mismanagement of impropriety, which may have enabled the culture of corruption and cover-ups to take root all across Leighton.

In early 2009, a whistleblower informed the top executives that Hodge had allegedly diverted A$500,000 of steel from Leighton to build a barge for an Indian company, Adani, in a black-market project.[10] A company legal report indicated that Russell Waugh, a Leighton executive who was also Savage’s right-hand man, had approved this transaction. Waugh later ordered internal investigations, which concluded that Hodge’s actions “had no material benefit to Leighton” and put the company “in a position of potential compromise of integrity.”[11] Despite these findings, Waugh merely gave Hodge a stern warning. A second inquiry by the company’s accountants then failed to find further evidence of these illicit payments and the matter was put to rest. Despite this, Waugh rewarded Hodge in appreciation of his “efforts over the last year”, giving him an A$40,000 bonus and salary increments upon closure of the incident.[12]

“If you go quietly, you’ll be back in three months.” - Phone conversation between Waugh and the whistleblower who shed light on the Hodge incident[13]

The persistence of the whistleblower eventually led to a launch of a third inquiry, this time independent of Waugh and carried out by a newly appointed Leighton executive. It was revealed that the investigations carried out previously were sorely inadequate. Reference was made to Waugh paying out a bonus to Hodge and also directing the investigations when he himself was in a potential conflict of interest, since Waugh himself signed off and approved the steel transaction.[14]

In response to criticisms, Leighton eventually dismissed Hodge and initiated legal proceedings against him to recover the money he allegedly stole. In Leighton’s media release to shareholders in response to the allegations by Fairfax Media, it was mentioned that this incident also led Leighton to “strengthen and improve its corporate governance and risk management processes”, such as the revision of its comprehensive Code of Business Conduct as well as a “5 gate tender review and approval process.”[15]

Building a Stonehouse

"Savage and Leighton International had extraordinary autonomy compared to the rest of the operating companies ... One of our major concerns here was that there was very little corporate governance within Leighton International." – Leighton witness to the Australian Federal Police (AFP)[16]

A lack of corporate governance and excessive autonomy within Leighton International also created the opportunity for Savage and fellow executives to use confidential information to establish a private business venture. All these were carried out via the company's internal email system,[17] at a time when Leighton International was facing probes on corrupt practices.

A review of Savage's confidential emails revealed that he had covertly launched "Project T", which sought to lure Leighton senior officers to a private firm in order to compete directly against Leighton so as to win projects.[18] This was evident as Savage's new venture "emphasised resource projects and offshore shallow-water projects", which was very much similar to work he had been helping to win for Leighton.[19]

Towering Remuneration Packages

Amidst the corruption scandals and heightened media attention, the excessive compensation packages of executives that came to light enraged the public further.

During King's tenure, he was criticised for receiving excessive executive pay, collecting at least A$100 million in remuneration since 2004, including a A$14.7 million compensation package in 2010, which was the year of his departure.[20] Moreover, King's remuneration package was not strongly linked to shareholder returns and was mainly in the form of cash rather than equity. His short-term incentive was also substantially above his counterparts at similar-sized companies – in a year that Leighton suffered a fall in profits.[21]

A closer scrutiny of Leighton's remuneration structure revealed its heavy emphasis on financial measures in its Key Performance Indicators (KPIs). More specifically, the company's profitability played a crucial role in determining the amount of remuneration. Executives' short-term incentives, such as cash bonuses, were directly linked to achievement and outperformance of profit targets, while medium-term deferred incentives hinged on profitability over a three-year period. Likewise, 50 percent of the long-term incentives were only achievable with substantial growth in earnings per share, which in turn depended on earnings and profitability.[22] In 2009, King's and Savage's short-term variable bonuses constituted 65.6 percent and 62.9 percent of their respective total remuneration.[23] This was noticeably higher than all other executives. Moreover, in 2009, performance against financial KPIs was also significantly weaker compared to previous years. On average, key executives only obtained 58 percent of the maximum remuneration payable to all eligible employees.[24]

The Board's Defence

Throughout Fairfax Media's numerous allegations, the Board had maintained the directors had "at all times executed their duties with the appropriate care and diligence, and in the best interest of each company [within Leighton]."[25]

Yet, the signature of former Leighton senior executive David Savage appeared on a preliminary tender document that includes an alleged A$42 million kickback to win a lucrative project in Iraq.[26] In defence of the Board's approval of the Iraq Project in October 2010 despite the alleged A$42 million bribe, a former director claimed that the bribe was deliberately disguised by Leighton's management as an "onshore and security payment" to avoid raising the suspicions of the Board. He also added that there were no discussions of potential "agency" payments of bribes. Instead, the A$42 million payment was portrayed as necessary by the management due to security concerns in Iraq. The evidence suggests that the Board approved the project without further inquiry despite knowing that the deal was carried out in a corruption-prone country.[27] It was also revealed that a six-month audit in early 2011 had prompted Board members to "examine bribery-prone practices with necessary details", but this did not appear to have resulted in any action.[28]

In a leaked Australian Federal Police (AFP) interview transcript, a former top executive said that he "never got the sense that the Board was excited by this stuff [due diligence, upholding corporate governance standards etc.]. The way Leighton International had been managed was an absolute disaster from a commercial perspective."[29]

Silent Fire Alarms

Despite uncovering appalling evidence of serious misconduct and corruption, the media reported that Leighton had withheld the memos and files detailing corruption and failed to notify authorities. The company had waited a year before it called the Federal Police in 2011.[30] It also took a further three months of delay till February 2012 to notify shareholders that an investigation was underway about the work in Iraq, and that the company had voluntarily notified the AFP of the alleged breach of its Code of Ethics.[31]

In response to these accusations, the Board maintained that once they knew of the matter, they had immediately reported it to the AFP. The reason that the market and shareholders were only notified in February 2012 was due to the confidential nature of the investigation.[32]

A Board Facing Constant Shake-Up

In the midst of the alleged corrupt deals in 2010, Leighton's controlling shareholder, the Hochtief Group, faced a takeover bid by Spanish Group ACS,[33] and the hostile takeover was eventually successful.[34] The stage was set for a new wave of power struggles within Leighton, with Hochtief engaged in a takeover bid to increase its stake in Leighton from 58.8 percent to 74 percent.[35]

With five out of 10 seats on Leighton's Board already controlled by either Hochtief or ACS, the threat of a potential overhaul arising from the takeover was very real.[36]

According to former Chief Financial Officer Scott Charlton, the Board's preoccupation with its internal struggles could have hurt governance and placed issues of potential corruption low on the agenda.[37]

In addition, the Board had been facing a flurry of changes in its composition. An examination of the composition of the Board indicates that the Chairman of the Audit Committee changed every year between 2009 and 2011.[38] Further, in financial year 2011, David Stewart held the post of CEO for a mere nine months, and then left along with six other directors. Clearly, the Board had pressing changes to deal with.[39]

In 2014, Hochteif ousted CEO Hamish Tyrwhitt and CFO Peter Gregg and replaced them with M Fernandez Verdes, CEO of Hochtief and former ACS executive, further cementing ACS' control over Leighton and its Board.[40]

Regulatory Bodies

"I would be surprised if the federal police or ASIC have the expertise or technical knowledge to undertake investigations of this nature." - Former top executive Stephen Sasse, in an interview with Fairfax Media[41]

The AFP and the Australian corporate watchdog, the Australian Securities and Investments Commission (ASIC), were also in the spotlight, with numerous reports published by Fairfax Media alluding that the AFP and ASIC had been slow to conduct thorough investigations. It was highlighted that "almost two years have passed since the AFP agents were first called in and they have still not spoken to key witnesses and suspects."[42] Similarly, ASIC had also been reported to not have reached out "to even a single witness."[43]

The AFP was overwhelmed by the case, due to reasons such as a lack of experience, technical knowledge, funding and manpower, and their "lack of urgency" was said to "stem from resourcing issues",[44] as revealed by former Leighton officials during interactions with the federal police.

ASIC was also under fire for not proactively fulfilling its duties as the corporate watchdog. In a bid to defend themselves, Greg Medcraft, Chairman of ASIC, told Federal Parliament's economics legislation committee that the agency was working to improve the handling of foreign bribery cases.[45] They also asserted that ASIC's enforcement record had always been "solid".[46] However, media reports referred to past instances of ASIC's tardiness in handling whistleblower information, including a poor handling of serious misconduct within Commonwealth Bank's financial planning division.[47]

ASIC also defended that they had to wait until the Police referred the case to them, and that the Police faced constraints as well, since there were laws in place to prevent the Police from sharing information with ASIC.[48] It was only on 2 April 2014 that ASIC confirmed its launch of a formal investigation allowing them to exercise the powers of the Star Chamber to question the witnesses and also demand for documents. Upon hearing this, the Australian Senate criticised ASIC for the delay in their investigation, claiming that formal investigation came two years late from the time ASIC had first known about the allegations in November 2011.[49] Consequently, questions have been raised if Leighton corruption could have been mitigated if ASIC had stepped up to investigate earlier.

Under pressure from the media and politicians, ASIC and AFP have since begun to find better ways of working together, starting with the signing of a memorandum of understanding[50] between both parties in October 2013. Furthermore, a proposal to the Senate has also been drafted to allow parallel inquiries to be conducted and there has also been a call for legislative reform to allow the AFP to share information with ASIC for such offences.[51]

Investors Scramble for the Emergency Exit

Leighton's share price dipped when shareholders caught wind of its work in Iraq; this was the first piece of public information received by investor community regarding the possibility of a breach of ethics and law.[52]

The share price fell a further 10.4 percent the day the reports were published by Fairfax Media, wiping A$688 million from its market capitalisation.[53] Hochtief Group's share price fell 7.9 percent, its largest single-day share price loss in more than two years. The following day, Leighton's share price fell another 4.6 percent, resulting in a cumulative total loss in market capitalisation of almost A$1 billion. Further, it was estimated that the legal and reputational damage resulting from this scandal could amount to as much as A$562 million,[54] as Leighton faces possible fines under the Commonwealth Criminal Code and losses of future contracts or cancellations of existing ones.

In an unusual turn of events, on 20 February 2014, Leighton declared profits for the year 2013, up 13 percent from the previous year. Investors reacted positively to this earnings announcement, with the share price going up by 6.5 percent – or by A$1.0755 – as Leighton was profitable even against the gloomy backdrop of a mining sector downturn. However, the share price of A$17.48 was still slightly shy of the almost A$20 pre-scandal share price. Leighton's former CEO Hamish Tyrwhitt remarked that "to get investor confidence back Leighton really needs to resolve those [corruption] issues."[56]

Epilogue

In an attempt to distant themselves from the corruption allegations, the construction group's new Spanish owners, ACS, decided to change Leighton's name[57] to Construction, Infrastructure, Mining and Concessions (CIMIC). Even so, the stock price has only risen to around A$20, still far from its former glory.[58]

Something Fishy: The ST Marine Corruption Scandal

Case overview

On 11 December, 2014, as Singaporeans prepared for the upcoming holiday season, the Corrupt Practices Investigation Bureau (CPIB) announced that it had charged three former employees of Singapore Technologies Marine Ltd ("ST Marine"), a subsidiary of Singapore Technologies Engineering Ltd ("ST Engineering"), for alleged bribery and corruption. The alleged bribes occurred between 2004 and 2010, amounting to hundreds of thousands of dollars.[1] The news was particularly shocking given that it involved a Singapore blue-chip engineering giant – one that had won several awards for best corporate governance from 1999 to 2004.[2] As shareholders of ST Engineering saw the stock price fall following the announcement, they were left wondering in disbelief. How could this have possibly happened? This case can be used to discuss issues such as factors that could lead to bribery and corruption in organisations; the role of the Board, senior management and external auditors in monitoring and detecting corruption risk; and policies that could be put in place to minimise corruption risk.

Background

ST Marine is the wholly-owned subsidiary of ST Engineering, which is a subsidiary of Temasek Holdings,[3] an investment company wholly-owned by the Government of Singapore.[4] ST Engineering, incorporated in 1997, is an integrated engineering group that provides "innovative solutions and services in the aerospace, electronics, land systems and marine sectors".[5] It is listed on the Singapore Exchange.

ST Marine is a leading shipyard that engages in the turnkey shipbuilding, ship conversion and ship repair business.[6] It provides services to naval and commercial customers in the global market, including the Republic of Singapore Navy and the Royal Navy of Oman, as well as customers from the Netherlands and the United States. It operates out of its shipyards located in Singapore and the United States. ST Marine has main facilities and offices in USA, Brunei and Shanghai. In the financial year ending 31 December, 2014, ST Marine accounted for 21 percent of ST Engineering's revenue, and 20 percent of net profits.[7]

Directors on Board

ST Engineering had a 15-member Board of Directors. Its Non-Executive Chairman, Kwa Chong Seng, was appointed on 25 April 2013. Kwa was previously the Chairman and Managing Director of ExxonMobil Asia Pacific Pte Ltd. He was also the Chairman of Neptune Orient Lines and Olam International, and also served on the boards of other companies such as the Singapore Exchange Ltd.[8]

ST Engineering had increased the size of its Board of Directors gradually over the years, from 11 directors in 2004 to 15 in 2015. Its directors were mostly non-executive – in 2015, there was only one executive director, the President and CEO of ST Engineering – and they came from a wide range of industries. For instance, the Chief of Defence Force in Singapore's Ministry of Defence sat on the Board, alongside senior management from law firms, financial advisory firms, and the civil service. The number of independent directors had also gradually increased over the years, from five independent directors in 2004, to 11 in 2015.[9]

There are various committees within the Board of Directors. Besides the Audit, Remuneration and Nominating Committees found in many public companies, the ST Engineering Board also has committees related to business investment and divestment; budget and finance; research development and technology; senior human resource; risk review; and tenders.[10]

Murky Waters

On 8 September 2011, CPIB arrested Patrick Lee Swee Ching, then Chief Financial Officer of Vision Technologies Systems, Inc. ("VT Systems"), an ST Engineering holding company based in the United States. Lee was previously ST Marine's group financial controller from 2001 to 2006. He was arrested for an offence under section 477A of the Penal Code, Chapter 224.[11]

Lee was subsequently released on bail and given permission to leave Singapore by CPIB. He returned to the United States on 10 September, 2011 to resume his responsibilities in VT Systems. The statement from ST Engineering, released on 12 September 2011, revealed that two current and one former employees were also arrested by CPIB, none of whom held management positions in ST Marine. ST Engineering also announced that an internal inquiry had been set up with respect to this matter.[12]

On 16 September 2011, Lee took a leave of absence pending the CPIB investigation and the abovementioned internal inquiry.[13] He retired in October 2012, without giving any reason.[14]

The years 2012, 2013 and most of 2014 went by without any updates from CPIB and ST Engineering regarding the investigation. However, the calm was broken on 11 December 2014 when CPIB charged three senior executives from ST Marine under the Prevention of Corruption Act and the Penal Code. The three senior executives were Chang Cheow Teck, president from March 2008 to April 2010; Ong Teck Liam, group financial controller and senior vice-president (Finance) from April 2007 to December 2012; and Mok Kim Whang, senior vice-president (Tuas Yard) from June 2000 to July 2004.[15]

On 30 December 2014, a fourth person, See Leong Teck, was also charged. See had been president of ST Marine for more than 10 years, from December 1997 to February 2008.[16]

Chang was charged with three counts of corruption and accused of conspiring with his subordinates, Teh Yew Shyan and Ong. From 2004 to 2010, they had allegedly paid bribes in exchange for ship repair contracts, amounting to a total of S$273,778.[17] These included a bribe of more than S$234,000 to an employee from Hyundai Engineering and Construction Co., Ltd (HDEC) in March 2009, and two bribes to staff of Myanma Five Star Line (MFSL) worth more than S$39,000 between February to April 2010.[18]

In addition to allegedly conspiring with Chang, Ong was slapped with 118 charges under section 477A of the Penal Code. She was accused of making false petty cash claims for bogus, non-existent entertainment expenses exceeding S$521,000.[19]

Mok was accused of conspiring with See and Lee to bribe a HDEC employee S$43,700 in May 2004, for the purpose of winning shipbuilding contracts.[20]

Lastly, See faced seven counts of conspiring with Ong, Mok, Teh, and Lee to bribe agents of ST Marine's customers in return for ship repair contracts between 2004 and 2010. The alleged bribes involving HDEC and MFSL amounted to more than S$556,000.[21]

In a press release dated 11 December 2014,[22] ST Engineering stated that the charges were "not expected to have any material impact on the consolidated net tangible assets or consolidated earnings per share of the ST Engineering Group for the financial year ending 31 December 2014." Despite ST Engineering's reassurance that the incident had no material impact on the company's financials, its stock fell three cents, closing at S$3.39. This drop continued to a one-year intra-day low of S$3.14 on 17 December, 2014.[23]

Professor Mak Yuen Teen from the National University of Singapore commented on the announcement: "While ST Engineering has won awards for best corporate governance, good compliance processes are no guarantee that people will keep in line. Three factors come into play — the nature of the industry, interaction with overseas governments, and the remuneration system."[24]

Naval Mines

ST Engineering's main business is in the defence industry. In addition to the Republic of Singapore Navy and the Royal Navy of Oman, it has other military customers such as the Brazilian Navy and US Navy.[25] According to Professor Mak, "when you have a company with businesses in defence, they tend to deal with a lot of government procurement and subsequently get exposed to public-sector corruption."[26]

Overseas government procurement contracts tend to be of a "winner-takes-all" nature. These contracts often include renewal and escalation clauses, decreasing the likelihood that they will be re-offered in the near future. According to Richard Bistrong, who used to be involved in military sales in the United States, it is common for such contracts to have "renewal clauses over the course of three or four years". As such, the contracts are significant in value and failure to win the contract would imply that there would be no business opportunities in the years to come. Hence, there are high stakes involved for sales teams to clinch the contract and seal the deal.[27]

Transparency International views the defence sector as having 'unique' corruption risks: "… at least US$20 billion is lost to corruption in the sector every year. And that is only a modest estimation of the costs incurred when national security concerns become a veil to hide corrupt activity. Single source contracts, unaccountable and overpaid agents, obscure defence budgets, unfair appointments and promotions… waste taxpayer funds and put citizens' and soldiers' lives at risk."[28]

Moreover, the nature of the procurement process may be unstable. Factors affecting international procurement in this industry, such as regime change, personnel turnover and logistics, all culminate to give rise to increased international procurement instability. Regime change may result in "a cancellation and re-bidding of all outstanding tenders in state ministries". Replacement of existing procurement staff can lead to an indefinite delay of tenders. Delays may also arise from licensing requirements, especially if regulatory authorities are involved, and the necessary arrangements and costs of logistics such as warehousing, shipping and forwarding.[29]

The shipbuilding industry also appears to be prone to corruption. For example,, the level of corruption in the Russian national shipbuilding industry has significantly risen in recent years, leading the government to focus more attention on the problem.[30] Similarly, the anti-corruption team in China's central government also recently began investigating the operations of China Shipbuilding Industry Corporation following allegations of corruption activities in the procurement department.[31]

There was also a previous incident of corruption in ST Marine, in which Senior Assistant Engineer Norrudin Bin Jalaluddin had exploited his position as the person in-charge of procurement to receive bribes in the form of loans from a supplier, totalling S$650. Norrudin was subsequently fined S$3,500 and ordered to pay a penalty of S$650.[32]

Foreign Waters

As Professor Mak commented on the case, "When you have a company with businesses in defence, they tend to deal with a lot of government procurement and subsequently get exposed to public-sector corruption. A lot of civil servants overseas are not well paid, so the risk of bribery and corruption in some countries is high."[33]

Indeed, several of the corrupted transactions involved foreign entities such as HDEC, a large Korean conglomerate, and MFSL, the national flag carrier of Myanmar.[34] This could be worsened by the fact that the discussions might have taken place overseas, leading to a lack of witnesses to any corrupt acts. As mentioned by Bistrong, "for the most part, front-line sales, marketing and business development personnel travel alone to their overseas territories. Agent meetings (maybe including a public official) also usually occur without anyone else present."[35]

While Singapore is known to have the lowest corruption levels in Asia,[36] there is very little control when it comes to the bribery and corruption that occurs in a foreign jurisdiction. The CPIB and the Attorney-General Chambers deal with acts of misconduct in Singapore seriously, but when the acts take place overseas, they are challenging to handle. Given that ST Marine deals with many foreign clients, the exposure and inherent risks of engaging in bribery and acts of corruption could potentially be higher.

Furthermore, bribery may pose an "illusion" of a "win-win" situation with no victims, as the sales person wins the deal and the client wins the bribe.[37] Hence, they require effective compliance measures for preventing and detecting bribery.

Professor Mak concluded: "Singapore is one of the major exporting economies in the world and is well regarded for having low public sector corruption by Transparency International and other organisations. However, as our companies increasingly venture overseas into emerging markets, there is considerable risk that we will also become a major exporter of corruption."[38]

Risky Pay

A large variable compensation component may place an emphasis on winning sales and contracts. This may tempt employees to use aggressive and unethical strategies especially when their compensation plan is tied to individual performance in a high-risk environment.[39]

Professor Mak commented that "if staff are set aggressive targets or paid in a way where they aim for profits, then they may not pay heed to compliance as much."[40]

During his stint as president of ST Marine, Chang received high remuneration, a considerable proportion being variable compensation. Variable compensation made up 59 percent and 65 percent of his total compensation in 2009 and 2010 respectively. Variable compensation includes "annual wage supplement, performance target bonus paid and economic value-added (EVA) earned" for the year. The EVA earned each year is added to the balance carried forward in an executive's EVA Bank, and one-third of the total is paid out. The remaining two-thirds is carried over to the following year.[41] According to its 2010 Annual Report, ST Engineering has been earning a positive EVA since its formation in 1997. Similarly, contingent shares granted are subject to key performance indicators being met over a specified period of three years.[42]

In another article, Professor Mak commented, "…[Employees] are expected to comply with a business conduct code which says all the right things about zero tolerance for bribery, corruption and other forms of unethical behaviour on the one hand, while being incentivised to pursue aggressive growth through pay for performance plans."[43]

Could the compensation plan at ST Engineering, comprising a considerable proportion of variable pay, have sent mixed signals to the employees, creating ethical dilemmas for them?

Calm After the Storm?

Following the initiation of investigations by CPIB in 2011, and the subsequent arrest of former ST Marine employees suspected of bribery and corruption, ST Engineering made a statement that they "take a zero tolerance approach to all forms of corruption including fraud and bribery"[44] and had taken steps to remedy the situation.

In its 2014 Annual Report, ST Engineering identified corruption as an inherent top risk when operating in a global market. ST Engineering also introduced an e-learning course on anti-corruption for employees identified to be exposed to corruption risks; 1,885 employees finished the course in 2014, and the course was subsequently rolled out to all identified employees in Singapore and other countries.[45]

The company also completed fraud risk assessments and will review existing policy and procedures against significant corruption or fraud risks, with the objective of ensuring adequate preventive and detective anti-fraud controls. Between 2012 and 2014, it completed briefings relating to anti-corruption policies and procedures for 42 percent of its employees.[46]

With the exception of Lee, who was fined S$210,000 in July 2015, the remaining cases are still pending before the courts.[47]

Viva La FIFA

Case Overview

Following a slew of bribery and corruption allegations over the past decade, the Fédération Internationale de Football Association (FIFA) was caught in what appeared to be its biggest scandal yet in May 2015. The New York Justice Department announced a 47-count indictment which pointed towards allegations of bribery, vote-buying, and questionable contracts over World Cup broadcasting rights, and arrested FIFA's top executives. Amidst it all, FIFA President Sepp Blatter's abrupt decision to resign after 17 years in office generated further interest over FIFA's "culture of corruption". This case can be used to discuss issues such as corruption stemming from poor tone at the top; conflicts of interest; whistleblowing; transparency and disclosures pertaining to executive remuneration; and applicability of corporate governance principles and practices for listed companies to sports bodies.

Kick-Off

27 May, 2015, 6.39 a.m.: Swiss plainclothes policemen streamed through the Baur au Lac – a five-star hotel, the site of FIFA's annual committee meeting. The officers retrieved room numbers from the front desk and headed upstairs, where they arrested seven FIFA executives.[1]

Hours later, the Justice Department in New York issued a 47-count indictment against 14 defendants, comprising FIFA officials, and sports marketing and broadcasting personnel. The indictment included charges of racketeering, wire fraud, and money laundering dating back to 1991, with bribes and kickbacks adding up to a tune exceeding US$150 million.[2]

"It spans at least two generations of soccer officials who, as alleged, have abused their positions of trust to acquire millions of dollars in
bribes and kickbacks." – Attorney General Loretta Lynch[3]

Historically, FIFA had deflected widespread allegations instead of addressing problems at an institutional level.[4]

Blatter's Reign

Sepp Blatter won the 1998 FIFA presidential elections only by a close margin over Swedish rival Lennart Johansson. This came after 17 years as the right-hand man to then President Joao Havelange. Despite his victory, Blatter's win was plagued with rumours of bribery.[5] Subsequent presidential elections were also shrouded in suspicion regarding the legitimacy and transparency of results.

"I am the president of everybody, I am the president of the whole FIFA." – Sepp Blatter[6]

Amidst the unraveling of FIFA's biggest scandal yet, Blatter was re-elected as its president for the fifth consecutive term, his 17th year running. However, just a week into his re-election, Blatter abruptly announced his resignation. This came in the wake of the FBI confirming that Blatter was now the focus of their corruption investigations.

FIFA Vows Reform

On 2 December 2010, Russia and Qatar were announced as hosts of the 2018 and 2022 FIFA World Cup respectively.[7] Upon the announcement, Qatar's Stock Exchange responded strongly, and neighbouring countries like Iran also showed excitement and enthusiasm for the opportunity to promote and develop football in the Middle East.

However, allegations of corruption dogged FIFA throughout the bidding and voting process for the 2018 and 2022 World Cup. There was significant pressure on FIFA to conduct reforms on an institutional level. Blatter launched a governance reform process at the 61st FIFA Congress held in June 2011 in Zurich, Switzerland.[8]

Blatter announced at the launch:
"This committee will strengthen our credibility and give us a new image in terms of transparency. I will take care of it personally, to ensure there is no corruption at FIFA." – Sepp Blatter[9]

The aim of the proposals was to improve governance, transparency, and to eradicate misconduct on and off the pitch. This resulted in a two-year road map for the subsequent establishment of the Independent Governance Committee (IGC).[10]

This was initiated shortly after Blatter was re-elected into his fourth consecutive mandate, which was also his 13th year of service as president. During that election, Blatter was the incumbent candidate again, with the only other candidate, Mohammed Bin Hammam of Qatar, withdrawing from the presidential race just three days before the vote.[11]

Whistle-Blowing Woes

Phaedra al-Majid was one of two whistleblowers who spoke up on Qatar 2022. al-Majid was a former media officer on the Qatar bid team.[12] If her corruption allegations surrounding the Qatar World Cup were true, Qatar could be stripped of its right to host the World Cup. After keeping mum for two whole years, she mustered up the courage to speak to Michael Garcia, then head of the investigatory arm of FIFA's ethics committee. al-Majid's allegations revolved around top FIFA executives receiving bribes in exchange of votes for Qatar. In return for Garcia's word that her identity would be kept confidential, al-Majid agreed to cooperate in the investigations of the 2018 and 2022 World Cup bidding process.

Unfortunately, in a 42-page summary of the investigations issued by Hans-Joachim Eckert, chief judge of FIFA's ethics committee, the identity of the two whistleblowers was revealed.[13] Although the summary did not explicitly expose the whistleblowers by name, it was not difficult to connect the dots based on the evidence cited, and al-Majid's cover of anonymity was blown just hours after the summary was published.[14]

"I kept my promise. Herr (Mr.) Eckert breached that confidentiality. I did not. The disciplinary committee's avoidance of this undisputable violation is emblematic of its culture of self-protection." – Phaedra al-Majid[15]

Not long after she came forward in 2011, al-Majid retracted her claims, and later added that she was coerced into it, citing fear for the safety of her family as the reason.[16] Despite the withdrawal of the allegations, it sparked off investigations into the Qatar 2022 World Cup.

Sidelined

Garcia also alleged that Eckert's summary misinterpreted the findings and presented a materially fragmented and fallacious view of the facts. This ultimately resulted in Garcia "losing confidence in the independence" of Eckert.[17] On 17 December 2014, Garcia's appeal to the FIFA committee to have his original report published in its entirety was rejected.[18] Garcia tendered his resignation, criticising the "lack of leadership" in the global football arena.[19]

The Heated Decision on Qatar

"Yes, it was a mistake of course, but one makes lots of mistakes in life, the technical report into Qatar said clearly it was too hot but the executive committee – with a large majority – decided all the same to play it in Qatar." – Sepp Blatter[20]

Since the announcement that Qatar would be hosting the 2022 World Cup, there had been much speculation over the landslide victory.[21] The outcry over Qatar's win arose over reasons such as its searing summers, strict alcohol restrictions and the lack of a developed football culture.

The 2022 World Cup bid attracted interest from Australia, Japan, Qatar, South Korea and the United States, and the final decision was voted on by FIFA's executive committee, where 22 members had one vote each.

During the bidding process, Qatar promised an advanced air-conditioning technology that would cool down the stadiums, training pitches and fan zones to a cool 23°C. This was in response to Doha's stifling summer heat, where average daily temperatures could range from low to mid 40°C in June.[22] Skepticism towards this ambitious technology was assuaged by Qatar's World Cup organising committee's confidence that the event would proceed as planned in summer under cooled conditions.

However, in March 2015, FIFA's Task Force decided that moving the tournament to end-November or December would be best. Furthermore, amidst the heavy media coverage on the bidding process over the 2022 World Cup, allegations against Qatari Mohammed bin Hammam quoted involvement in bribes to secure votes for Qatar. Following this, FIFA commissioned a report over the allegations and cleared Qatar of all suspicions. However, this report was never published.[23]

Waka Waka (This Time It's Africa)

Investigations into FIFA uncovered other skeletons in the closet, this time pertaining to the 2010 World Cup hosted by South Africa. Jack Warner, then vice-president of FIFA, became the centre of allegations involving a US$10 million bribe paid by South African officials in return for securing the rights to host the 2010 World Cup. The monies were traced to accounts controlled by Warner. However, South Africa denied payment of any bribe in relation to the securing of the 2010 World Cup. Instead, sports minister Fikili Mbalula "categorically denied" the allegations, citing that the monetary payment went towards "an approved program to help the development of football in the Caribbean."[24] However, in another inquiry, Mbalula harped on the fact that the money did not constitute a bribe, but rather "a donation to support the African diaspora."[25]

Secret Profits

It was not long before Blatter was also dragged into the scandal. Further investigations uncovered evidence pointing to Blatter's approval of a suspiciously small contract in relation to the 2010 and 2014 World Cup television rights. This allegation pointed to Blatter awarding the rights to the Caribbean Football Union (CFU), which was under the control of Warner – who had his own fair share of corruption allegations.

The contract dating back to 2005 was uncovered by Swiss broadcaster Schweizer Radio und Fernsehen (SRF), which documented the sale of the 2010 and 2014 World Cup broadcasting rights to the CFU for US$600,000.[26] This was a mere 5 percent of its true value. Warner subsequently sub-licensed the rights to his own company J & D International (JDI), whereby his subsequent profit was estimated to be about US$16.5 million.[27]

Blatter Gets a Yellow

The initial investigations unraveled one suspicious transaction after another. The Swiss police chased down a lead regarding a US$2 million payment made by Blatter to Michel Platini, then vice-president of FIFA and president of UEFA (Union of European Football Associations), just three months before he won his fourth term of office in 2011. Blatter asserted that the money was related to an overdue payment owed for work done by Platini in 1999. Similarly, Platini responded by insisting that the money was for work which he had previously performed. However, he did not address the issue of the near decade-long delay in receiving it.[28]

A Very Profitable Non-Profit

Contrary to FIFA's establishment as an "association of associations with a non-commercial, not-for-profit purpose", its commercial dealings rake in billions of dollars in revenues every year.[29] FIFA's expenditures, particularly the remuneration of top executives, are also ambiguous and poorly defined. In its 2014 financial report, FIFA showed a total of US$88.630 million in wages and salaries, of which US$39.731 million was paid to its top 13 executives. Despite immense pressure for greater disclosures in all aspects of FIFA operations, the organisation had yet to publicly disclose the exact amounts earned by FIFA's top echelon.[32]

Extra Time

FIFA's proposed reforms first saw the light of day on 11 August 2015, when the new 2016 FIFA reform committee was established with the appointment of a fresh face[33] as the Independent Chairman. This was meant to build upon the reform work undertaken since 2011. There had also been unprecedented stress on FIFA to enhance and improve its corporate governance in order to restore its reputation as the governing body for world football.

"We need reforms now, we cannot wait. FIFA works very well operationally and has not come to a halt. But this is a watershed in terms of role going forward" – Domenico Scala[34]

As at 2016, the ball had been set in motion. However, it would take a long while before any conclusive evidence can establish that the reforms have been effective in addressing the governance issues plaguing FIFA. Only time will tell if the reforms would truly score.

Substitution: Blatter Out, Hayatou In

8 October, 2015: After years of deflecting corruption allegations and side-stepping his way out of the most convoluted scandals, Blatter faced a 90-day ban from all football activities, an order enforced by FIFA's Ethics Committee,[35] following which he was relieved of all presidential duties with immediate effect. Issa Hayatou, the longest serving vice-president on the FIFA Executive Committee, filled the gap and took over as acting president of FIFA for the interim period prior to the following presidential elections in 2016.[36]

Petrobras: Not Your Typical Carwash

Case Overview

On 20 March, 2014, the former refinery chief of Petroleo Brasileiro SA Petrobras ("Petrobras") was arrested during "Operation Carwash", under allegations of money-laundering during his term at Brazil's largest company. In a bid to obtain concession from the prosecutor, Paulo Roberto Costa agreed to a plea bargain. This led to a divulgence of insider information that included many alleged elaborate kickback schemes between Petrobras, its corporate partners and some members of Brazil's top political leadership echelons. Since then, Brazil has been embroiled in the largest corruption scandal the country has ever faced. This case can be used to discuss issues such as bribery and corruption; the role of public governance in companies; corruption risk in countries with poor public governance; and the effectiveness of anti-corruption programs in business environments where corruption is rampant.

Petrobras - Powering Brazil's Future, Once Upon A Time

"The economics are just so poor at Petrobras, that we really have called it a scheme, not a stock." – Jim Chanos, founder of Kynikos Associates LP[1]

At its peak, Petrobras had been the symbol of Brazilian pride and envy of the world. Today, its tainted reputation has become a source of public ridicule and mockery. What had once been heralded as the gold standard of global energy producers has since plunged into the doldrums.

Petroleo Brasileiro SA Petrobras, Que Saudade!

Petrobras was founded in October 1953 by Brazil's former president, Getúlio Vargas. Headquartered in Rio de Janeiro, Petrobras was a major player in the oil and gas industry. It sought a public listing on the Sao Paulo Stock Exchange in 1997 and listed as a depository receipt on the New York Stock Exchange thereafter. In 2011, Petrobras was ranked the fourth largest energy company worldwide and the largest company in South America.[2]

Petrobras' operations can be segmented into five divisions: exploration and production; refining, transportation and marketing of oil and natural gas; petrochemicals; distribution of derivatives, electrical energy, biofuels; and other renewable energy sources.[3] Through these segments, Petrobras aims to deliver a variety of quality products processed from the energy it produces.

Board of Directors

Chairing its Board of Directors between 2003 and 2010 was Dilma Rousseff, before her win at the 2011 Presidential Elections. It was a historic moment for Brazil as the Office of the President was held by a woman for the first time. In January 2012, Maria das Graças Foster was appointed Chief Executive Officer (CEO) by the controlling shareholder (i.e. the Brazilian Government).[4] She also sat on the Board of Directors.

The Board at Petrobras comprised 10 directors, each elected for a one-year term, with re-election allowed. Seven of these directors had been appointed by the controlling shareholder, one by the minority common shareholders, one by the preferred shareholders and one by the employees.[5] Four out of the 10 directors were considered independent.

Shareholdings

Petrobras issued two classes of shares – Common and Preferred, with the latter class having no voting rights and being offered primarily to investors. As at February 2015, the Brazilian government had control of more than 50 percent of the voting rights. A further 11 percent was controlled by entities over which the government had effective control. Additionally, the government also retained veto power over major decisions concerning the company.[6]

New Money, Suit and Tie

"To end corruption is the supreme goal for one who has not reached power." – Paulo Roberto Costa[7]

Costa had it all, or so he thought. He led an upscale lifestyle, owned luxurious cars, and loaded bank accounts.[8] As he rose through the ranks at the energy giant, he frequently indulged in the company of high society and their world of merry-making. It was a world where individual profit-making was encouraged and self-interests were advocated.

Eventually, blinded by greed, Costa turned a deaf ear to his conscience and eventually went down the wrong path. In his 35 years with Petrobras, he channelled a significant amount of wealth from the company into his pockets through an elaborate corruption and bribery scheme. Little did he know that the cheating would soon come to an end, as would the extravagant living.

From Handshakes to Handcuffs

The 20th of March 2014 seemed like any ordinary day, except that it was not. On that fateful day, Costa was apprehended by the federal authorities from the comfort of his luxurious gated community to assist in investigations concerning money laundering malpractices. The arrest had been unexpected, and had sent Costa's daughters and sons-in-law into a packing flurry, as they filled suitcases and bags with cash, incriminating documents and a laptop in a bid to hide them from the prosecutor. Unfortunately for the Costa family, however, a security camera had taped the entire episode, and the footage was handed over to the judge presiding over the case.[9] The investigation was nicknamed *Operção Lava Jato*, or Operation Carwash, because Youssef had allegedly used carwashes to launder money.

Spilling the Beans

Between 2004 and 2012, Costa held the appointment of Chief of Refining and Supply at Petrobras. Evidence show that at the peak of his career he had acted as an intermediary for money launderers and the state. The notorious Alberto Youssef formed the other half of the criminal duo. He had acted as the black-market currency dealer for the scheme and had been caught earlier on 17 March 2014. Previously, Youssef had been arrested nine times for laundering more than R$10 billion.[10]

On 27 August 2014, Costa appeared in the Parana federal court and pleaded for leniency. As part of the plea bargain, he spilled the beans on Petrobras' illegal activities which had been going on for almost a decade, dishing out the names, bank accounts, political connections and contacts of all those involved. Youssef did likewise, unravelling the details of the biggest corruption scandal to date in Brazil.[11] Over a period of at least seven years, Costa and several others had embezzled kickbacks amounting to millions from companies to whom Petrobras had awarded inflated construction contracts. In addition, they had given bribes to politicians through intermediaries to ensure they voted in line with the ruling party.[12] During a recorded court hearing, Costa described the kickbacks he received from the companies as a "three percent political adjustment" which equated to tens of millions of dollars.[13]

Greasy Palms, Troubled Nation

According to Brazilian law, the commencement of investigations against congressmen and top figures of the executive branch was subject to the approval of the Supreme Court. Subsequent criminal charges or trials against these persons must also be approved and judged by the highest court. As a result, legal proceedings concerning such persons implicated in the Petrobras scandal were expected to span at least a few years.[14]

Upon investigation, the Federal Police found 750 construction and public works implicated in the scandal.[15] Costa divulged a total of 54 names to the Attorney General, many of whom were members of Rousseff's Workers Party (PT) and its coalition allies in the Congress.[16] Although Rousseff chaired the board of Petrobras when the kickback scheme was still in operation, she vehemently denied any knowledge of it. Eventually, her name was cleared by the prosecutors.[17] However, opinion polls revealed that most Brazilians believed she knew of the scheme.[18]

As investigations continued, more dirty secrets and dishonourable acts were uncovered. A further probe revealed that nine of the biggest Brazilian infrastructure and construction companies had been involved in the scheme.[19] Prominent corporations such as Rolls Royce, and Singaporean companies such as Keppel Corporation, were also accused of paying bribes to Petrobras in exchange for favourable treatment.[20] Three political parties made the headlines for allegedly receiving benefits from the state-owned enterprise – PT, Brazilian Democratic Movement (PMDB) and the Progressive Party (PP). On 6 March 2015, 12 senators and 22 congressmen were formally held under investigation.[21]

On 14 October 2014, Petrobras took another blow as PricewaterhouseCoopers (PwC), the company's external auditor since 2012, refused to sign off the third-quarter earnings and threatened to bring the case to the United States authorities.[22] Petrobras admitted that it was "impracticable to measure in a correct, complete and definite manner" its losses from the corruption scandal.[23] The accounting firm refused to comment and demanded further investigation.

On 24 November 2014, Petrobras received a subpoena from the US Securities and Exchange Commission requesting for access to documents which were needed in an ongoing investigation. Petrobras duly obliged. Petrobras was also separately investigated by US Department of Justice for potential violations of the US Foreign Corrupt Practice Act. Probes by the United States authorities were said to be ongoing since start of 2014.[24]

Mired in Financial Turmoil

On 21 October 2014, in light of the corruption scandal and its huge amount of debt, Moody's Investors Service (Moody's) downgraded Petrobras' global foreign currency and local currency debt ratings from Baa1 to Baa2.[25] Coupled with falling oil prices and a weakening local currency, the future of Petrobras seemed bleak. Despite the negative outlook, Rousseff managed to emerge victorious at the Brazilian presidential elections by a narrow margin, securing 51.6 percent of the votes. However, the news was not well-received by investors – Petrobras stock fell 16.4 percent on 27 October, 2014.[26]

After being left in the lurch by PwC, Petrobras released its unaudited 2014 third-quarter results on 27 January 2015. The company's shares fell 11.6 percent to US$6.59 the following trading day in reaction to the news.[27] On 29 January 2015, Moody's downgraded all ratings for Petrobras. This included a downgrade of the company's senior unsecured debt from Baa2 to Baa3 and Baseline Credit Assessment from ba1 to ba2.[28]

To aggravate matters, the company was simultaneously facing a dozen class-action lawsuits in the US including a lawsuit from Ohio's pension fund on the basis that it had violated US federal securities laws.[29]

As if things were not bad enough, on 25 February 2015, shares of Petrobras fell more than eight percent to US$6.29 following Moody's further downgrade of the company's long term debt rating from Baa3 to Ba2 (junk status).[30] The firm offered a probable explanation of the downgrade to its stakeholders – concerns over the corruption investigations and potential liquidity pressures, as well as Moody's negative outlook on Petrobras' ability to reduce its significant debt levels in the following years.[31]

The scandal took a huge toll on Brazil's economy and few have managed to emerge unscathed. With the cancelled contracts and delayed payments, many construction companies were facing credit downgrades and bankruptcies. The oil industry bore the brunt of the fallout with thousands of workers dismissed, worsening the unemployment situation in the country.[32]

Easy Come, Easy Go

Back in 2012, Foster's appointment as the CEO of Petrobras had been met with some resistance. As Foster and Rousseff maintained a close relationship, many questioned if Foster would have a potential conflict of interest maximising firm value and catering to Rousseff's political agenda. Although not accused of direct involvement in the scheme, Foster was reported to have ignored internal whistleblowers about the corruption scandal. Venina Velosa da Fonseca, a former Petrobras manager, said that she had warned several directors about inflated contracts in 2008, including Foster who was then the head of the gas and energy division. However, Foster vehemently denied all knowledge of the scheme.[33]

On 4 February 2015, Foster tendered her resignation. This move was generally accepted by the markets but investors were concerned about the government's failure to name her replacement immediately. Together with Foster, five other Petrobras top executives also resigned from their positions.[34]

A Leadership Vacuum

"We have seen today an episode of disrespect for the board of directors of Petrobras. Once again the controlling shareholder (the government) has imposed its will over the interests of Petrobras, ignoring the appeals of long-term investors." – Mauro Cunha, Petrobras' Representative Director for Minority Shareholders[35]

Following the mass resignations, Rousseff used her personal connections to search for replacements for the key management positions at Petrobras. The five executive positions were filled two days later on 6 February 2015, all of them by employees of the company who had considerable experience in engineering and the oil and gas industry.[36]

Additionally, Rousseff nominated Aldemir Bendine, head of state-owned Banco do Brazil, as Petrobras CEO. However, the independent directors were not consulted and the appointment was not supported by the full Board, which was unsurprising given that he possessed neither experience nor expertise in the oil industry.[37] Furthermore, Bendine's appointment was met with disappointment given his close relationship with Rousseff, and Banco do Brazil's status as a major lender to Petrobras and its contractors. As expected, the stock market reacted negatively – Petrobras' shares fell by nine percent.[38]

A Change in Board Leadership, Again

Guido Mantega, Brazil's former finance minister, had been chairing the Board since March 2010 before the baton was passed to Murilo Ferreira, CEO of Vale SA, a Brazilian multinational corporation engaged in metals and mining. It was hoped that Ferreira would be able to "replicate this story in Petrobras", referring to how he had "corrected a very serious problem of capital allocation" at Vale SA.[39] Moreover, Ferreira's appointment, along with two other executives from Vale, were seen as a departure from the tradition of appointing cabinet ministers and allies of the Brazilian government.[40]

However, less than eight months into his appointment, Ferreira vacated his position on 30 November 2015. Neither Petrobras nor Vale's press department provided any reason for Ferreira's departure, but it was believed that Ferreira had clashes with Bendine, and that fundamentally, they had "disagreed on how to conduct business".[41] Taking his place was acting Chairman Luiz Nelson Guedes de Carvalho, who was subsequently re-elected on 28 April 2016.[42]

In a surprising turn of events, Rousseff was forced to step down as Brazil's president amid impeachment trials, for allegations that she had "illegally manipulated fiscal accounts".[43] Michel Temer, who assumed the role of acting president, proceeded to appoint new heads for state-run banks such as BNDES and Banco do Brasil, as well as Petrobras, "as part of a broad shuffle of top government jobs."[44]

Pedro Parente, Chairman of BM&Fbovespa SA, the operator of Latin America's biggest securities exchange, succeeded Bendine and became Petrobras' third CEO in less than two years. Even though Parente had never managed an oil company, his experience in business and government garnered praises from investors, as he had led Brazil out of a national crisis when he oversaw energy rationing during his term as an energy minister in a 2002 drought.[45]

Blessing in Disguise?

Industry experts predicted that as Petrobras and other implicated companies were blacklisted from further work, opportunities may arise for medium-sized and global construction and engineering companies that had previously been unable to contract for large projects in Brazil as the "political shield often blocks public bids".[46]

On 20 March 2015, Petrobras' Executive Board approved a project to be led by Bendine to revise its corporate governance and management rules. This project aimed to "adapt the company's governance to a new business environment and a revised investment plan."[47]

Amidst the troubles plaguing Petrobras, some investors remained hopeful. For instance, Skagen AS, a Scandinavian employee-owned investment manager,[48] continued investing in Petrobras' shares, as it anticipated that Petrobras would be in a stronger position after the corruption probe. In the short term, cash flows were seen to be improving due to decreasing oil prices and fixed retail product prices in Brazil.[49]

Tougher Rules, Greater Enforcement

Prosecutors who had uncovered the scandal appealed for tougher prison sentences and greater legal authority to clamp down on "rampant graft that costs taxpayers more than the annual budget for education and health."[50] As the scandal unravelled, more executives and directors of Petrobras, even politicians from the Workers' Party, were arrested and prosecuted.[51]

Evidently, some believe that the corruption scandal will lead to better governance in Petrobras and even in the country in the long run. However, much remains to be seen and the world watches on with interest as the saga unfolds.

Keppel Corporation: Offshore and Off-Course

Case Overview

On 23 December 2017, corporate Singapore was shocked when Keppel Corporation (Keppel) announced that its wholly-owned subsidiary, Keppel Offshore and Marine (KOM) had reached a global resolution with criminal authorities in the United States, Brazil and Singapore relating to corrupt payments made by a former KOM agent in Brazil. Under this global resolution, KOM was to pay fines totaling US$422 million to authorities in the three jurisdictions. This was the first time that any Singapore company, let alone a government-linked one, has been caught in a global bribery scandal. It emerged that the corrupt payments started in 2001 and totaled US$55 million, and helped KOM obtain 13 contracts over 13 years. What was equally shocking was the corrupt payments were made with the knowledge or approval for former KOM executives. Court proceedings involving the agent revealed that some of the most senior executives were involved, including a former chairman and CEO of KOM, who was also CEO of Keppel. This case can be used to discuss issues such as corporate culture; board composition; remuneration; whistleblowing policies; governance of company groups; and governance of governance-linked companies.

Keppel Corporation

"To become a truly global company, we would have to forge a unified team. And it was clear what we had to do. There would be no more in-fighting and competing against each other within the group. We would always focus on the outside - focus on our customers and on the marketplace." – Choo Chiau Beng, Former CEO of Keppel Corporation and Chairman of KOM[1]

Keppel Corporation (Keppel) had come a long way since its establishment in 1968 as Keppel Shipyard in the ship repair, ship building and offshore business. The 1970s was a period of tremendous growth for Keppel as it acquired Keppel FELS and Singmarine yard and ventured overseas.[2] Keppel Shipyard listed on the Singapore Stock Exchange in 1980 but the years ahead proved to be rough due to the gloomy outlook for the offshore and marine industry, coupled with the major recession hitting Singapore.[3] However, Keppel sailed through the rough storms and clinched several ground-breaking projects before Keppel Shipyard became Keppel Corporation, while Keppel Shipyard remained as a major operating division.[4] Today, Temasek Holdings, the investment company which is wholly owned by the Singapore government, holds 20 percent of the shares of Keppel.[5] As of 18 May 2018, Keppel has a total market capitalisation of $14.88 billion.[6]

"The gold standard for corporate governance"

"Keppel is focused on upholding high standards of corporate governance with a strong and independent board, demonstrating its strong commitment to good business ethics and maintaining clear, consistent and regular communication with shareholders." - Keppel Corporation[7]

Since its inception, Keppel has bagged many corporate governance awards and has been often been ranked amongst the top three for the Best Annual Report award and/or Best Managed Board Award for the Singapore Corporate Awards (SCA). During the 2015 SCA, it won the most prestigious award for the Best Managed Board for companies with a market capitalisation of a billion or more[8].

Keppel has also constantly been ranked amongst the top five in the Singapore Governance & Transparency Index (GTI) throughout the years and in 2017 it were ranked fifth[9]. In 2014, it were named the best governed and most transparent listed company[10]. Keppel was said to have performed well in several corporate governance measures used for the GTI, including disclosures in its annual report on the details of the process by which it appointed its new CEO, Loh Chin Hua and criteria considered for CEO succession[11].

Keppel O&M

Riding on the wave of globalisation, Keppel entered many strategic partnerships and 2002 marked a significant milestone as it established Keppel Offshore and Marine (KOM).[12] KOM is one of the four key businesses that make up Keppel. It is headquartered in Singapore and was formed by combining three different operating businesses of Keppel - Keppel FELS, the rig designer and builder; Keppel Shipyard, the ship repair and conversions specialist; and Keppel Singmarine, the shipbuilding specialist. This was done to exploit the potential synergies and collective competitive advantage that each of the businesses possess.[13]

KOM soon established itself as one of the leading players in the marine and offshore industry.[14] It was undoubtedly the crown jewel of Keppel. Between 2005 and 2015, it contributed from 56.6 percent to 75.5 percent of total group revenues, with the percentage contribution peaking in 2006, while contribution to pre-tax group profit from 35 percent to 65.1 percent during that same period, with its peak in 2011.[15]

However, the global offshore and marine sector has been suffering from sluggish growth in recent years. In addition, volatile and depressed oil prices which fell to a 13-year low of below US$30 at the start of 2016 led to the lack of new projects for KOM.[16] KOM achieved revenues of S$2.9 billion in 2016, which was 54 percent lower than the previous year.[17] Its revenue contribution to the group fell from 60.6 percent in 2015 to 42.2 percent in 2016, while pre-tax profit contribution fell from 35 percent to just 8.5 percent.[18] However, in 2016, it delivered 21 major projects and secured new contracts worth about S$500 million.[19]

Early 2017 saw the start of the recovery of oil prices which rebounded to above US$50 but there were low expectations for a quick turnaround for the offshore and marine sector, especially since production increases from shale oil producers in the United States have impaired the recovery of oil prices.[20] Contributions to the group continued to tumble, with revenue falling to 30.2 percent of total group revenues. In 2017, it secured new contracts of about S$1.2 billion.[21]

Sailing into Brazilian Waters

KOM's long standing relationship with Brazil began in the 1980s when it took on multiple vessel repair and conversion jobs from Petrobras.[22] In 2000, BrasFELS shipyard and FELS Setal were established in Brazil. BrasFELS shipyard was located in the city of Angra dos Reis to provide upgrading and repair services for the rigs working in the region whilst FELS Setal was a joint venture in Rio de Janeiro between Keppel FELS and Brazil's PEM Setal Group. This joint venture was set up to operate BrasFELS while providing for the booming market of oil and gas exploration and production activities in Brazil and in the west coast of Africa.[23]

After the first year of inception, FELS Setal acquired repair and conversion contracts exceeding US$120 million.[24] FELS Setal was also successful in leading foreign companies in Brazil and allowed local rig owners to increase turnover by sending the jobs to the yard.

Following PEM Setal Group's divestment of its entire interest in the joint venture in 2005, FELS Setal was renamed as Keppel FELS Brasil.[25] In addition, BrasFELS subsequently managed to expand its services to include construction and conversion services. It attracted customers locally and internationally and established itself as one of the most prominent offshore and marine facility in the Latin American region.[26]

Unfortunately, it was later discovered that 13 contracts of KOM from Petrobras and Sete Brasil were obtained through illicit payments from 2001 to 2014. KOM earned approximately US$351.8 million through this bribery scheme, with illicit payments for these contracts amounting to US$55 million.[27]

KOM's Brazil Breakthrough: P-48 Project

"The conversion of P-48 was undertaken at Keppel FELS Brasil's BrasFELS yard between 2003 and 2004 and was the largest conversion project ever carried out in Brazil." - 2005 Annual Report

In 2001, BrasFEL was given the subcontract for Brazil's first floating production storage and offloading (FPSO) conversion and integration project, the P-48 project.[28] The project, reportedly worth US$75 million, was to convert an aging tanker into a floating offshore production centre platform for Petrobras.[29] This FPSO was to be deployed for oil and gas production at Caratinga. Former CEO and Chairman Choo Chiau Beng also mentioned in a stakeholder report that its completion in 2004 was a "milestone" for KOM's operations in Brazil. Furthermore, this project was touted by KOM as the "largest and most complex offshore conversion project undertaken to date in Brazil" and was completed by BrasFELS in five million work hours without a loss time incident.[30]

Unfortunately, it emerged that the P-48 project was secured through corrupt means. According to the US District Court, a KOM executive and sub-executive "authorised the payment of bribe amounting to approximately US$300,000 to government officials in Brazil in connection with securing the subcontract for Petrobras' P-48 project".[31]

In one of the emails that was sent to its subsidiary's financial controller from KOM's executive director, it stated that "[T]here is a commitment to pay US$300k for some governmental guy(s) to help us put pressure for the [P-48 project] to be carried out in Brazil. [KOM Sub Executive] and myself have discussed this and decided to keep to the commitment. [Please] make arrangement for the first US$50k to be paid accordingly…".[32]

On top of this first payment, several more payments were also made for the P-48 project, with the last payment of US$50,000 made on 4th April, 2002.[33] This marked the beginning of KOM's bribery practices.

Mechanism of bribery

Companies (including KOM) that were suppliers to Petrobras formed a cartel in collusion with senior Petrobras officials.[34] The "winner" of the bid would already be predetermined by the cartel, but there was a fake bidding process to keep up the illusion of a competition. Petrobras officials would help in the process by adding unnecessary jobs to inflate contract values and leak confidential information to the cartel to give a clear advantage to their members, while ensuring that non-cartel bidders were disadvantaged.[35]

In accordance with this arrangement, Jeffrey Chow, the then General Manager (Legal), drafted agreements containing inflated agency fees on behalf of KOM with consulting companies controlled by Zwi Skornicki (the Consultant).[36] These agreements were co-signed by other KOM executives.[37]

Under the guise of consulting agreements, KOM made payments to bank accounts in the United States and elsewhere in the names of shell companies controlled by the Consultant.[38] An example of this scheme was when a KOM subsidiary based in Singapore made seven payments totaling approximately S$17.6 million to a bank account which was controlled by the Consultant.[39] Following this, the Consultant transferred these funds to a bank account outside of the United States, supposedly to the Brazilian officials.

Companies often disguise bribes to avoid detection. For example, in the ST Marine case, S$24.9 million in bribes were falsely classified as entertainment expenses made to employees of ST Marine's customers in return for ship repair contracts.[40] Reclassifying the expenses and collusion helped hide the existence of the bribes for an extended period of time.[41]

The Calm Before the Storm

Following the bribery for the P-48 project, the P-51 and P-52 Projects were secured in 2003 through similar underhanded means. The consultant received explicit authorisation from KOM's executives and the firm's joint venture partner to pay bribes equivalent to a percentage of the contracts' value which amounted to a whopping US$13.3 million.[42] The illegal funds went through an intermediary who would transfer the money from the consultant to a Brazilian official at Petrobras who would subsequently split the money amongst himself and the rest of the officials at Petrobras and the Workers' Party.[43]

The pursuit for more contracts through underhanded means did not stop and more payments were made in 2005, 2007 and 2009. In 2007, the P-56 Project was secured through a bribe of US$14.2 million.[44] This amount was similarly determined as a percentage of the project's contract value and paid to a Brazilian official and the Workers' Party. The cost of this bribery payment was shared with KOM's joint venture partner. Payments of approximately US$4.4 million were made for the P-53 and P-58 Projects in 2005 and 2009 to secure portions of two floating platform hull conversion projects.[45] The P-61 Project obtained in 2009 involved payments of about US$8.8 million and were likewise made to the same beneficiaries on the same terms as their previous contracts.[46]

Before KOM ran out of luck with its dirty schemes, it clinched a big project between 2011 and 2012 when its subsidiary was one of the five selected companies for the Sete Brasil Projects to construct the Petrobras's rigs.[47] Court documents revealed negotiations between contracted companies, including KOM, and a Brazilian official where bribes were matched to 0.9 percent to 1 percent of the value of their respective contracts.[48] Two-thirds of the payments were made to the Workers' Party while one-third was to be shared equally between the relevant Petrobras and Sete Brasil executives. Throughout the negotiation period, telephone calls were made by a KOM executive to authorise the consultant to pay bribes equivalent to 1 percent of the contract value. Consequently, the consultant received a substantial amount of about US$14.4 million in bribes for the Brazilian officials and the Workers' Party.[49]

Facing the Storm

In March 2014, the Brazilian police detained Alberto Youseff, a black-market money dealer during what was seen a routine money-laundering investigation in Brazil, where petrol stations were often used as a shell.[50] However, he was no ordinary criminal; further examination of data on his computer revealed a number of substantial money transfers involving hundreds of senior executives and several companies, one of which was Petrobras and its director Paulo Roberto Costa.[51]

Arrested and pressured by investigators, Costa revealed that for more than a decade, Petrobras managers had colluded with ruling politicians and other local companies in illegally accepting hundreds of millions of dollars in exchange for Petrobras contracts.[52]

In 2013, Brazil's Organised Crime Law was introduced and passed, which paved the way for the rising adoption of plea bargain in court and provided a "detailed road map for collaboration by witnesses".[53] As long as what was revealed is true and can be verified thereafter, the witness involved can face a lesser sentence or even receive a judicial pardon. This was what prompted certain Petrobras executives, such as Pedro Jose Barusco Filho, a former executive at Petrobras to divulge extra information to facilitate the investigation.[54] It was through these disclosures that the name of Skornicki was flagged to the investigators. Skornicki was Keppel's former agent in Brazil from 2000 to 2006 and was finally arrested in 2016 under Brazil's massive graft crackdown called "Operation Car Wash".[55]

Keppel ran out of luck as further digging by investigators revealed that KOM and many other global corporations were involved in bribing Petrobras.

The central figures

Although those involved in the bribery scandal were not specifically disclosed by KOM, the court testimonies of Skornicki revealed that some executives of KOM and Keppel Fels Brasil were involved in authorising and directing the illicit payments.[56] The executives named by Skornicki include Choo Chiau Beng, Tong Chong Heong, Chow Yew Yuen, Tay Kim Hock and Kwok Kai Choong. In addition, Jeffrey Chow, a senior member at KOM's legal team from 2009 to 2017, was also found guilty of drafting contracts for the bribery payment.[57]

The executives that authorised these payments are mainly from the top management as Choo Chiau Beng, Tong Chong Heong and Chow Yew Yuen were CEOs of KOM during the period of the scandal. Tong was also Senior Advisor to the Board after handing his CEO position to Chow, who was the CEO when the scandal was discovered. The other two executives identified, Tay Kim Hock and Kwok Kai Choong, were previously CEOs of Keppel Fels Brasil.

Skornicki also revealed that KOM approached him with the intention of engaging him as a dealer whereby he could sign contracts with Petrobras on behalf of Keppel. This was evidenced by a contract with Keppel that Skornicki presented in court which stated that he would be rewarded with a percentage of any deals he cut in Brazil.[58] Using the same account which Keppel paid his agency fees to, he then used it to bribe Petrobras officials. Petrobras, a state-owned company, was then controlled by the ruling political party at that time, the Workers' Party. Thus, most Petrobras officials who were bribed were the politicians from the Party, including Joao Vaccari, who was the treasurer of the Workers' Party.[59] Over the years, the ruling Workers' Party had pocketed up to almost US$200 million from bribery[60].

We Did Not Do It….Or Maybe We Did

Keppel had initially denied all allegations of involvement in making bribe payments.[61] In February 2015, there were media reports in Brazil about the involvement of Keppel FELS in the Petrobras scandal. Pedro Jose Barusco Filho had alleged that illegal payments were made by Skornicki. Keppel made the following statement:[62]

> *We refute allegations made in media reports on Keppel FELS' involvement in the scandal surrounding Petrobras.*
>
> *We would like to emphasize that Keppel Group has a Code of Conduct which prohibits, among others, bribery and corruption. Our employees are required to conduct themselves with integrity, in an ethical and proper*

manner, and in compliance with the applicable laws and regulations of the countries in which we operate, including anti-bribery laws.

We wish to point out that Zwi Skornicki is an employee of Eagle do Brasil, which is the agent of Keppel FELS in Brazil. Keppel FELS had conducted due diligence review of Eagle do Brasil and Zwi Skornicki. Further, the Agency Agreement with Eagle do Brasil categorically states that Eagle do Brasil and Zwi Skornicki 'shall not make, either directly or indirectly, any improper payment of money or anything of value to an Official in connection with the Contract.' In addition, Eagle do Brasil's services are not exclusive to Keppel FELS, and it is also an agent to other reputable multi-national companies.

We would also like to clarify that as part of initiatives to contribute to the communities around the world in which we operate, we make various contributions in Brazil, which include social welfare programs, community activities and political donations. All of our various contributions are made according to and within local laws and regulations, which are documented in the respective companies' records and audits.

In October 2015, Keppel issued another announcement that the Parliamentary Commission of Inquiry had voted to deepen its investigations into 10 companies involved in transactions with Petrobras and Sete Brasil, including Keppel FELS Brasil. It said it would extend full cooperation to the authorities if approached. It again reiterated its zero-tolerance stance against any form of illegal activity, including bribery and corruption.[63]

Further announcements followed In February, April and May 2016 announcing that the agency relationship with Skornicki had been put on hold, his arrest and charging, with Keppel continuing to reiterate its zero-tolerance stance. In August 2016, Keppel issued the following announcement after Skornicki in his testimony alleged that bribe payments were done with prior approval and endorsement by the senior management in Keppel:[64]

Keppel refers to the Bloomberg article dated 3 August 2016 reporting allegations made by Mr Zwi Skornicki in criminal proceedings brought against him in Brazil. Keppel strongly denies the allegations reportedly made that Keppel executives authorized Mr Skornicki to pay bribes on its behalf. None of the individuals named in the article, including the current CEO of Keppel Offshore and Marine Mr Chow Yew Yuen, have ever authorized Mr Skornicki to make any payments as bribes.

Finally, on 3 October 2016, Keppel announced that its internal investigation into the allegations involving Skornicki revealed that certain transactions may be suspicious.[65] Keppel also announced at the same time that it had notified the relevant authorities of its intention to cooperate and work towards a resolution of the underlying issues. It again reiterated its zero-tolerance stance.

For its cooperation and remediation efforts, Keppel received a 25 percent discount off the bottom of the applicable fine range, which is the maximum discount allowed.[66]

Paying the Price

KOM was given a conditional warning by the Corrupt Practices Investigation Bureau (CPIB) in Singapore which took into consideration the cooperation KOM had given for the investigations.[67]

KOM paid a penalty of US$422 million (S$567 million) as part of the global resolution reached in 2017 with criminal authorities in the United States, Brazil and Singapore.[68] The financial penalty and related costs eventually amounted to a whopping S$619 million and had a significant impact on Keppel's bottom line.[69] Keppel recorded a net profit of S$217 million during the financial year ended 31 December, 2017 and this was 72 percent lower than the net profit of S$784 million recorded in the previous financial year.[70] and KOM reporting a $862 million loss in 2017, including a $570 million financial penalty from the global resolution with criminal authorities in the United States, Brazil and Singapore for bribery in Brazil and $49 million of related legal, accounting and forensic costs.[71]

Where was the Board?

This massive bribery went on undetected for years. In response to queries about board accountability, the current boards of directors of Keppel Corporation and its unit KOM said that they were unaware of the illegal payments made to secure the contracts with Petrobras in Brazil as they were disguised as agency fees.[72] These agency fees were said to be "built into the contract values of the respective projects, and bidding for projects is in the ordinary course of KOM's business".[73]

In response, corporate governance experts have highlighted the board's responsibility for overseeing a business in a foreign environment where there is high risk of corruption. They mentioned that although it may be challenging for the board to know everything, the board should not have just relied on information given by the management.[74] According to them, in countries and sectors where there is high risk of corruption, the board should have questioned how the contracts were obtained, rather than adopting the usual approach of only questioning the management when financial targets are not achieved.[75] They also pointed out that the fact that bribery has occurred multiple times over a decade highlights a deeper culture issue in the organisation. Some also mentioned that early warning signs and whistleblowing may have been ignored as employees may feel that if the wrongdoers are from the senior management, then it is pointless for them to report the matter.[76]

Doubts were also raised regarding the effectiveness of KOM's and Keppel's checks and balances. These include questions as to whether the independent directors were fulfilling their duties to help ensure corporate integrity and good governance.[77]

Keppel Board of Directors

Between 2000 and 2007, Lim Chee Onn was the Chairman and CEO of Keppel, holding the title of Executive Chairman.[78] This was highly unusual among government-linked companies in Singapore as Temasek Holdings, its largest shareholder, advocates the separation of the positions of chairman and CEO and the appointment of a on-executive chairman for its portfolio companies.

Lim started his career in the civil service. He was deputy secretary in the Ministry of Communications before he was elected as a Member of Parliament (MP), and held positions of Political Secretary in the Ministry of Science and Technology, Secretary-General of the National Trades Union Congress and Minister without Portfolio in the Prime Minister's Office, before retiring as an MP in 1992.[79]

On 1 January 2009, Lim relinquished his CEO role at Keppel and became Non-Executive Chairman. He was replaced as CEO by Choo Chiau Beng.[80] On 1 July 2009, Lee Boon Yang was appointed as independent Non-Executive Chairman of Keppel replacing Lim. Lee had joined the board as an independent non-executive director on 1 May 2009.

Lee worked as a veterinarian after graduation and became an MP in 1984. He held appointments as parliamentary secretary, minister of state, senior minister of state, and various full minister positions, including Minister of Defence and Minister of Labour. He retired from political office on 31 March 2009.[81]

Between 2006 and 2010, Keppel's Board had increased from eight to 12 members, before declining from 2012 to its current board size of nine members. Throughout those years, it had a lead independent director. In 2006, half of its eight-member Board were independent directors, with one non-independent non-executive director and three executive directors, including the Chairman. The non-independent non-executive director, Tow Heng Tan, was appointed to the Keppel Board in 2004, having joined Temasek Holdings in 2002 as Chief Investment Officer. He has remained on the Keppel Board after this retirement from Temasek Holdings. Except for part of 2009 when Lim was a non-executive non-independent director, Tow was the only non-independent non-executive director on the Board up till today.[82]

Over the years, the percentage of independent directors has increased to about 80 percent. Before 2013, the Board generally had three executive directors, but that declined to two in 2013 and from 2014, the CEO has been the only executive director on the Board.[83]

Keppel has the following Board committees: Audit Committee, Nominating Committee, Remuneration Committee, Risk Committee and Safety Committee. Except for the Safety Committee which includes executive directors as members, all other committees have only non-executive directors as members, with a majority including the chairman being independent directors. Prior to 1 January 2010, the Board also had an Executive Committee chaired by the Board Chairman, but this was dissolved.[84]

KOM Board of Directors

KOM's Board was established in 2002 with 12 members, with half of them being independent.[85] There were four executive directors – the Chairman and CEO, Choo Chiau Beng; the CFO, Sit Peng Sang; the COO, Tong Chong Heong; and the Managing Director of Special Projects, Charles Foo Chee Lee.

The Board also had a non-independent, non-executive director, Teo Soon Hoe, who was a Senior Director and Group Finance Director at Keppel Corporation. The independent non-executive directors were Neo Boon Siong, Minoo Homi Patel, Malcolm Sharples, Tan Kim Siew, John Rossman Huff, Stephen Pan Yue Kuo and Bjarne Hansen.

Currently, there are eight independent, non-executive directors out of the total of 11 board members.[86] Loh Chin Hua, the group CEO, is the Non-Executive Chairman and Chris Ong Leng Yeow, the CEO, is the sole executive director. Another non-independent, non-executive director, Chan Hon Chew, is the group CFO of Keppel Corporation. Most of the independent non-executive directors who were on the board at the time of KOM's establishment has left, with the exception of Minoo Homi Patel, Malcolm Sharples and Stephan Pan Yue Kuo. New independent, non-executive directors who joined over the years include Po'ad Bin Shaik Abu Bakar Mattar, Tan Ek Kia, Lim Chin Leong, Robert D. Somerville and Kelvin Kwok Khien. Tan Ek Kia is also an independent director on the Keppel Corporation board.[87]

Paying for What Performance?

Keppel has a strong pay-for-performance culture for senior management. This is reflected in both the relative weightage of fixed and variable remuneration components for senior management and the types of remuneration schemes used. In 2009, which was its best year based on revenues, profits and economic-value added, the total remuneration of its CEO, Choo Chiau Beng, was in the range of $11.5 to $11.75 million, with base salary accounting for only nine percent, while variable remuneration components in the form of performance-related bonuses earned and options granted amounted to 91 percent. Teo Soon Hoe, executive director and group finance director received total remuneration of $7.5 to $7.75 million that year, with variable components comprising 90 percent, while executive director Tong Chong Heong received total remuneration of $6.75 to $7 million, with 88 percent being variable. All three executive directors were on the KOM board at that time, holding positions of Chairman, non-executive director and CEO respectively.[88]

From 2006 to 2017, the variable components of the CEO remuneration made up between 81 percent and 91 percent of his total remuneration, and for FY2017, it was 84 percent. The CFO or equivalent over that same period received variable remuneration ranging from 74 percent to 90 percent over the same period, and for FY2017, it was 80 percent.

Prior to 2010, Keppel's share incentive scheme was in the form of a share options scheme. Executive directors and employees were eligible to participate. All options that were granted could be exercised after two years and before the expiry date.

Choo, Teo and Tong all received share options ranging from between 5 and 15 percent of their total remuneration. Some key management personnel just below the executive directors received more than 40 percent of their total remuneration in the form of share option grants in some years.[89]

In 2010, Keppel replaced its share options scheme with two new share incentive plans – a performance share plan and a restricted share plan. Shares awarded under the two plans are based on pre-determined performance targets set over a three-year period and one-year period respectively. For the performance share plans, performance targets include those based on total shareholder return. Changes to these performance and restricted share plans were introduced in recent years.[90]

Performance-related cash bonuses for executive directors and key management included an economic-value added (EVA) and non-EVA component. Prior to FY2012, Keppel disclosed that the annual performance bonuses are linked to company's, business unit's and individual's performance, including a portion which is tied to EVA performance. More recently, performance bonuses are awarded based on the achievement of key performance indicators in four areas: financial and business drivers, process, stakeholders and people.

Under the "EVA bank" system used by Keppel, one-third of the current year EVA-bonus and the one-third of the accrued EVA bank is paid out as long as EVA is positive. The remaining two-thirds of the EVA bank is deferred and is at risk, and can become negative if EVA performance is negatively affected. In FY2007 and FY2008, however, this was changed to one-half of the current EVA bonus and one-third of the accrued EVA bonus being paid out. However, from FY2009, after Choo was appointed as CEO, the operation of the EVA bank system reverted to the pre-FY2007 formula. In FY2017, the company appears to have ceased the deferral of performance-related cash bonuses earned, although the CEO, Loh Chin Hua, received less total performance-related cash bonuses earned, and more restricted shares and performance shares.[91]

Since FY2006, Keppel has paid its non-executive directors a combination of cash fees and remuneration shares. The remuneration shares were intended to align the interests of non-executive directors with shareholders and the long-term interests of the company. Today, non-executive directors receive 70 percent of their fees in cash and 30 percent in remuneration shares.[92]

Risk Management

"Our proactive risk management system enables us to conduct our business in a sustainable manner and navigate through challenging market conditions." – KOM Annual Report 2016

According to KOM, it currently adopts a well-rounded and proactive Enterprise Risk Management (ERM) framework which provides for identification, analysis and management of risks.[93] The Board of Directors, together with the Audit and Risk Committee (ARC), has the oversight of the ERM implementation. Every quarter, the

Management team holds discussions with the ARC regarding KOM's key risks, significant project issues and risk response.

Keppel Corporation's three risk tolerance guiding principles underlie KOM's ERM framework. Firstly, there should be meticulous evaluation of risk taken. Rewards should be commensurate with the risk taken and risk taken has to be aligned with the company's core strengths and strategic objectives. Secondly, risk that arises from a single area of operation, investment or undertaking should not be taken if it is so large that it would endanger the company. Lastly, the Group has zero tolerance for "safety breaches or lapses, non-compliance with laws and regulations as well as illegal acts such as fraud, bribery and corruption."[94]

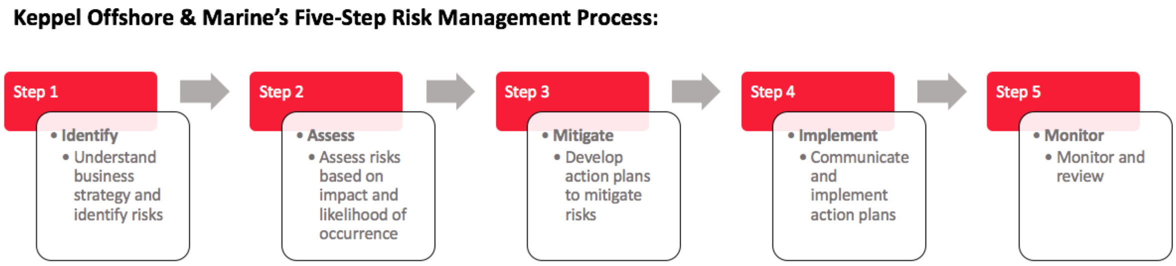

Diagram 1: KOM's five-step process (Source: KOM's Annual Report 2016)
KOM's five-step process from risk identification, assessment, mitigation, implementation and communication to risk monitoring and review in their day-to-day operations and discussions.

Regular reviews of risks across the company are integrated into KOM's strategy discussions to ensure that key risks and mitigating actions are considered. Additionally, projects are only accepted after careful consideration of potential risks in all areas. Project teams also use risk and performance indicators as red flags for project execution risks to help ensure that "projects are delivered on time, within budget, safely and in accordance with the quality standards and specifications defined in the contracts with our customers"[95]. Moreover, for projects that are conducted overseas, there are constant reviews for changes in operating environment, political and regulatory developments. If required, precautionary measures are implemented to mitigate their exposure in different circumstances. KOM's Risk and Compliance team evaluate the emerging risks with project teams and present the potential issues to the Management and ARC. Sharing sessions are conducted across different KOM business units for exposure purposes.

Furthermore, KOM's commitment to fostering a risk-centric culture which emphasises prudent risk-taking in decision-making and business processes is regularly broadcast on multiple platforms and events.

While Keppel's risk tolerance principles now emphasise a zero-tolerance stance towards fraud, bribery and corruption, this was only mentioned in KOM's and Keppel's annual reports starting from FY2013.

Regulatory Compliance

Based on Keppel's and KOM's annual reports, there has been a heightened emphasis on regulatory compliance in recent years.

Keppel adopts a stringent code of conduct with regards to compliance to laws and regulations. It is mandatory for all employees to comply with the relevant laws and regulations and act in line with Keppel's core values and principles. According to KOM, it emphasises ethical actions and has a strong zero-tolerance stance towards any form of illegal activity including fraud, bribery and corruption.[96] KOM has a defined regulatory compliance framework which aids in ensuring an effective compliance culture among employees[97].

The KOM Audit and Risk Committee (ARC) supports the Board in its oversight role of compliance controls. The Risk and Compliance team reports to the ARC on key compliance risks as well as mitigating actions as required. The Regulatory Compliance Governance Structure comprises the Regulatory Compliance Management Committee (RCMC) and the Regulatory Compliance Working Team (RCWT). The RCMC consists of the senior management of all key business divisions while the RCWT consists of key representatives from the Legal, Risk and Compliance, Human Resources, Corporate Development and Finance team of all key business divisions.

The RCMC directs and supports the development of overarching compliance policies, guidelines and procedures for the Group whereas the RCWT drives the implementation of the Group's code of conduct and compliance programmes and ensure adequate assessments for regulatory compliance risks are conducted. They also ensure suitable control measures are implemented to manage all risks.

Keppel has a code of conduct which covers issues regarding anti-corruption and conflict of interest, among others.[98] Business partners and associates that provide services or engage in business activities with Keppel are also required to observe comparable standards.

Across the Keppel Group, compliance messages have been relayed through various initiatives and awareness in regulatory compliance is actively raised during forums and meetings held at the Group level[99]. Training is also a key component of Keppel's regulatory compliance framework and training programmes are consistently refined. Mandatory annual online training along with assessments and declarations relating to the understanding of the company's policies on code of conduct, personal data protection, competition, insider trading, whistle-blowing and conflict of interest is enforced on all employees.

Whistleblowing Policy

Following the release of the revised Singapore Code of Corporate Governance in 2005, which included a guideline recommending that companies have arrangements in place for employees to raise concerns, Keppel introduced the "Keppel: Whistle-Blower Protection Policy".[100] This provides for mechanisms by which employees and other persons may, in confidence, raise concerns about possible improprieties in financial reporting or other matters. This policy is reviewed by the Audit Committee.

The current reporting mechanism under Keppel's whistleblower policy can be found on its website and is shown below.[101]

Home ▸ Whistleblower statement

Whistleblower statement

Whistleblower Policy

Integrity is one of Keppel's core values. Keppel expects its employees to carry out their duties and responsibilities in an ethical manner and in compliance with applicable laws and regulations at all times in the countries where Keppel carries on business.

Keppel has a Whistleblower reporting channel for its customers, suppliers, employees and other stakeholders to report, in good faith, details of any instances of illegal and/or unethical conduct.

Making a Report

Incidents of actual or suspected illegal and/or unethical conduct and violation of laws & regulations should be promptly reported to the Receiving Officer via Keppel's independent reporting channels as follows:

Email	Report@kepcorp.com	
Hotline	Country	Toll Free Number
	Singapore	64136500
	Brazil	08008923174
	China	4001206106
	USA	18338217058
	Vietnam	12065300
Online Form	*Please click here to submit a Report online*	

NOTE: *The Whistleblower reporting channel is not intended for reporting issues that are (i) not factual; or (ii) trivial, frivolous and vexatious in nature; or (iii) where the reported matter or subject has no relevance to Keppel Group.*

Refueling and Overhaul

"The global resolution reached by KOM over past misdeeds in Brazil brings an end to what has been a painful chapter for Keppel - one that we have recognised and dealt firmly with. This is not Keppel. We care not just about results, but also how they are obtained" – Mr. Loh Chin Hua, CEO of Keppel Corporation[102]

In light of this series of incidents, Keppel has taken disciplinary actions against 17 former and/or current employees, while seven of these individuals have left the company.[103] Keppel chose not to disclose the identity of these individuals, citing confidentiality issues. It was disclosed that demotions and/or written warnings were given to seven employees while financial sanctions of US$8.9 million were imposed on 12 former and/or current employees.[104] Lastly, six employees were ordered to undergo anti-corruption and compliance training.[105]

Moving forward, effective compliance controls were said have been implemented to ensure a corrupt-free and sustainable KOM.[106]

Despite the bribery scandal, KOM said it did not expect any negative impact on its ability to bid for contracts and that it would continue its operations in the United States, Brazil and Singapore.[107] KOM managed to secure new orders worth over S$1.2 billion in 2017, which was more than double of the S$500 million secured in 2016.[108]

Overall, the Group has also fared well despite the calamity. Excluding the one-off financial penalty and related costs, the Group would have attained a net profit of S$836 million for FY 2017, which is 7 percent higher compared to S$784 million a year ago.[109] The Group also recorded free cash inflows of S$1,802 million in FY 2017 which was a huge improvement over the inflow of S$540 million in FY 2016.[110]

The Mexican Wal

Case Overview

U.S.-based Wal-Mart Stores Inc. ("Walmart"), the world's largest retailer, is listed on the New York Stock Exchange. In 2005, it was alleged that its Mexican unit, Wal-Mart De Mexico ("WalMex"), was involved in bribery, and that there was a subsequent cover-up. A former executive from WalMex had informed Wal-Mart International's general counsel of the dealings. It was claimed that the then WalMex CEO had been the "driving force" behind the bribery payments. A preliminary investigation unearthed evidence of bribes amounting to US$24 million. However, the investigation was allegedly quietly halted in 2006 with "no evidence of bribery". The issue resurfaced in December 2011 when Walmart disclosed in its SEC filings that it was performing internal investigations into possible infringements of the FCPA. In April 2012, New York Times published a Pulitzer Prize-winning investigative story revealing the allegations of bribery in Mexico. The news caused Walmart shares to plunge. A series of lawsuits by shareholders followed. Regulators then intervened to investigate the alleged bribery. This case can be used to discuss issues such as the risks associated with bribery and corruption; accountability of holding companies for the actions of subsidiaries; the adequacy of the board's reactions; whistleblowing; and corporate governance failures that facilitate bribery and corruption.

Crossing the Borders

WalMex was established in 1991 and was Walmart's first venture outside of the United States. Eduardo Castro-Wright ("Castro-Wright") was a high-flyer who had joined WalMex as Chief Operating Officer (COO) in 2001.[1] He shortly became the President and CEO of WalMex. Under his leadership, the division's net profit grew by 36 percent in a single year.[2] Within a decade, the division had become the largest private employer in Mexico. It controlled 30 percent of all supermarket food sales, and had even more business than Mexico's entire tourism industry. Castro-Wright was praised for his stellar performance, and it was not too long before he became the President and CEO of Walmart.[3]

The Rattlesnake Shakes His Tail

In September 2005, Sergio Cicero Zapata ("Cicero"), an in-house lawyer at WalMex, notified Walmart International senior general counsel Martiza Munich ("Maritza") of prevalent bribery within WalMex.[4] Cicero claimed that he had information regarding corrupt practices by senior WalMex officials, and accused them of bribery and false accounting practices.[5] Cicero also alleged that Castro-Wright was the driving force behind the deals. Castro-Wright set "very aggressive growth goals" which put pressure on WalMex executives to do "whatever was necessary" to open new stores in record time.[6] The bribes were "purified" in accounting records as simple legal fees, and Walmart's management across the border were kept out of the loop.[7]

Maritza brought the accusations to several senior executives in Walmart. Soon after, Walmart hired Willkie Farr & Gallagher, a law firm with considerable experience in Foreign Corrupt Practices Act (FCPA) cases, to investigate the issue.[8]

The law firm planned to conduct an extensive investigation that would span a period of four months. However, Walmart's senior executives opted to conduct a shorter and limited "preliminary inquiry", and tasked Walmart's Corporate Investigations Unit to undertake it instead.[9]

Corporate Investigations Unit (CIU), I See You

The CIU had fewer than 70 employees and only four people were specifically assigned to corporate investigations. Walmart's director of corporate investigations described in a confidential memo that the number was "wholly inadequate for an organisation the size of Walmart". The unit, however, managed to obtain approval to hire four "special investigators" who, according to their job descriptions, would be assigned the "most significant and complex fraud matters".[10]

The role and independence of the CIU had been questioned before. In one of the previous internal investigations, the CIU had been in charge of investigating an allegation concerning one of Walmart's senior vice presidents. However, John Menzer, Walmart's then vice Chairman, intervened and removed CIU from their role as investigator. He then passed the investigator role to a subordinate of the executive being investigated. Eventually, the senior vice president was cleared by the subordinate.[11]

Small "Gestores" Go a Long Way

The CIU began work in November 2005, and uncovered 441 instances of gestores payments dating back to 2003.[12,13] Cicero singled out two prominent gestores who had received payments amounting to US$8.5 million and the CIU noted that payments to these two gestores had halted when Castro-Wright left WalMex to join Walmart in 2005.[14]

An internal WalMex audit in March 2004 had highlighted the gestore payments and recommended notifying Walmart of the issue.[15] However, WalMex's chief auditor, who was implicated by Cicero, altered the recommendations and sacked the internal auditor shortly after.[16]

In December 2005, the CIU proposed ramping up investigations on grounds that there was "reasonable suspicion to believe that Mexican and USA laws have been violated."[17] An anonymous tip was also sent to three senior officials in Walmart – Lee Scott, Mike Duke and Rob Walton – alleging that WalMex executives were receiving kickbacks.[18]

Following the preliminary investigations, Walmart leaders rewrote the protocol for internal investigations to allow them to hand control of the investigation over to José Luis Rodríguezmacedo Rivera ("Rivera").[19] Rivera was WalMex's general counsel, and had been implicated in the scandal. After four weeks, Rivera exonerated the implicated executives and closed the case. He stated that there had been “no evidence of bribery” and accused Cicero of trying to defraud WalMex.[20]

The issue would not come to light again until December 2011 when Walmart made a disclosure with the SEC.[21]

Bad Times for Walmart

In December 2011, Walmart disclosed in its SEC 10-Q filing that, during the year, they had begun a voluntary internal review into possible contravention of the FCPA.[22]

Five months after the disclosure, The New York Times (NYT) published an investigative report alleging widespread corruption in WalMex, and implicating several key executives in both Walmart and WalMex, including then-CEO Lee Scott, former head of Walmart International Mike Duke, and Chairman of the board Rob Walton.[23] Castro-Wright was identified as the driving force in Mexico, while the top brass in Walmart were accused of burying the matter.

Concerned with violations of the FCPA and the cover-up by top officials in the company, two US Congressmen, representatives Elijah Cummings and Henry Waxman, began a congressional investigation into the allegations.[24]

In response to the report, David Tolvar, a company spokesman, issued a statement highlighting Walmart’s non-tolerance towards non-compliance with the FCPA, and stated that it was working closely with the SEC and the US Department of Justice (DOJ) in its investigations.[25]

Chipping Away at the Wal of Silence

It was later discovered that Walmart had been involved in a lobbying campaign against the FCPA.[26] The lobbying group had been pushing to weaken anti-bribery laws. The congressional investigations then expanded to include Walmart’s involvement in the campaign.[27]

Shareholders from CtW Investment Group revealed an internal Walmart memo showing that in 2005, Walmart’s long-serving auditor, Ernst & Young LLP (EY), had known about the possibility of bribery in Mexico.[28] The group accused EY of violating Public Company Accounting Oversight Board (PCAOB) rules and auditing standards, as well as US securities laws.[29]

It was also revealed that there were concerns about Walmart’s internal control system back in 2005. A letter from four major shareholders was sent to Roland Hernandez, the then-Chairman of the Walmart’s audit committee.[30] It urged the company to appoint a special committee of independent directors to review the company’s internal controls. Hernandez rejected the idea.

A second exposé by the NYT was published in December 2012, detailing the extent of Walmex’s reach in Mexico.[31] The report focused on a store that was opened near Elda Pineda’s ancient pyramids despite zoning restrictions and public protests. It further alleged that bribes were used in connection with the opening of 19 different stores, and that WalMex had even influenced public policy to further their agenda.[32]

The report was followed by backlash from Walmart's shareholders. Several major shareholders sued Walmart over a range of issues.[33] Some claimed that Walmart executives had failed to respond to the red flags of unethical conduct in Mexico; others mentioned that Walmart executives had suppressed internal investigations.[34]

One shareholder group, the Indiana Electrical Workers Pension Trust Fund (IBEW) sued Walmart demanding that they release documents related to the bribery probe.[35] The Delaware Chancery Court later held that the shareholders were only entitled to the documents related to the initial investigation in 2006, and that they were not privy to those linked to the subsequent investigations in 2011.[36]

In November 2014, law firm Robbins Geller sued the SEC for improperly withholding documents related to the investigation. They also claimed that the SEC had yet to translate and review many of the documents despite having possessed them for over 40 months.[37]

Confidence Low, Votes Show

Two influential proxy advisory firms, International Shareholder Services and Glass Lewis & Co, recommended that shareholders vote against several of Walmart's key executives and directors including Scott, current CEO Duke, and Christopher Williams.[38] Williams had been a member of the audit committee at the time of the scandal, and was the current audit committee Chairman.[39] At the same time, some prominent institutional shareholders said that they would be voting against several Walmart's directors.[40]

At the general meeting in June 2012, Walmart's shareholders still voted largely in favour of re-electing Walmart's existing directors. However, unlike the 2011 re-elections where re-elected directors received 98 percent or more of votes, most received approximately 10 percent fewer total votes.[41]

Shareholders continued to fight for greater transparency about whether Walmart clawed back remuneration from its executives for violating laws and tarnishing the company's reputation.[42] An investor coalition with a cumulative shareholding of US$3.1 billion filed a proposal titled 'Request for Annual Report on Recoupment of Executive Pay.[43]

At Walmart's annual meeting held in 2014, there was an increase in the percentage of votes on this issue from 32 percent in 2013 to 38 percent.[44]

Rebuilding the Great Wal

Since the publication of the NYT report, Walmart has taken steps to enhance its global compliance program. These include the institution of compliance officers in each division, the implementation of a common compliance system, regular risk assessments, and increased training.[45]

Walmart has also extended its Anti-Corruption Policy to associates and third parties that engage government officials on the company's behalf.[46] The company reiterated disciplinary measures for non-compliance. Senior executives' compensation has also been tied to the achievement of compliance objectives, and their annual cash incentives could be slashed if they fail to meet the Audit Committee's expectations.[47]

During Walmart's annual international employee pep rally in 2012, executives addressed several thousand employees and emphasised that employees and managers must comply with the law even "when no one is watching".[48] The use of the whistleblower hotline was also encouraged.[49]

The Wright Response

On 24 April 2012, Castro-Wright resigned from the Board of MetLife, where he was previously a member of the Governance and Corporate Responsibility Centre.[50] Subsequently, in July 2012, Castro-Wright resigned as vice Chairman of Walmart.[51]

A series of other leadership changes occurred after the NYT exposé. In 2013, Rivera voluntarily resigned from Walmex.[52] Duke stepped down from his role as CEO but continued to sit on the Board. The Board also lost three independent directors in the same year, causing the percentage of independent directors to fall from 71 percent to 64 percent. In 2014, Williams and Scott stepped down from the Board.[53] In 2015, Rob stepped down from his long-standing post as Chairman of the Board, and his son-in-law Greg Penner, took over the post. Shareholders had been pushing for an independent director to chair the board.[54]

Currying Favour In India

In October 2015, the Wall Street Journal ("Journal") reported that the DOJ's investigation was largely complete,[55] and that the extent of the scandal in Mexico was not as serious as it had initially been perceived to be. The investigation also uncovered a vast number of small bribes linked to Walmart India that collectively amounted to a few million dollars. According to insiders interviewed by the Journal, Walmart was likely to receive a fine, and its executives were unlikely to face criminal charges.

Mega Bank, Mega Failure?

Case Overview

Taiwan's third largest bank, Mega International Commercial Bank Co., Ltd. (Mega Bank), was fined US$180 million by US regulators on 19 August 2016. The New York branch of the bank was penalised for its compliance failure and for violating the US anti-money laundering regulations. This was not the first time that the bank was involved in money laundering scandals. The bank's branches in Australia were previously involved in similar cases as well. This case can be used to discuss issues such as board structure; the impact of government influence on corporate institutions; internal control and risk management; and money laundering in the banking industry.

History of Mega Bank

Mega Bank was formed on 21 August 2006 from the merger of The International Commercial Bank of China Co., Ltd. (ICBC) and Chiao Tung Bank Co., Ltd. (CTB), both of which were privatised in the 1900s. In 2014, it had 107 domestic branches, and a total of 39 overseas outposts.[1] It was the third largest bank in Taiwan in terms of size of assets in 2016.[2]

Board Structure

Mega Financial Holding Company (MFHC), formed in 2002, was the holding company of Mega Bank.[3] The Board of MFHC consisted of 15 directors, of which three were independent directors.[4] The independent directors sat on both the Audit Committee and Remuneration Committee. The holding company did not have a separate Nomination Committee.[5]

Mega Bank did not have separate Audit, Remuneration or Nomination Committees. Instead, MFHC's Remuneration Committee approved Mega Bank's remuneration policies, and its Audit Committee assigned supervisors onto Mega Bank's Board. Of the five supervisors sitting on the Board, three held executive positions in MFHC.[6]

There were a total of 15 directors on the Board of Mega Bank in early 2016. The Chairman of the Board, Tsai Yeou-Tsair, was also the Chairman of MFHC. Wu Hann-Ching was the President and Managing Director of both Mega Bank and MFHC. In addition, there were two other managing directors, eight other non-independent directors, two independent directors, and an "independent managing director" on the board. Three of the 10 non-independent directors also held executive positions in MFHC.[7]

In September 2016, both Mega Bank and MFHC reshuffled their boards, re-appointing the majority of the board members.[8] Tsai resigned from his post as Chairman of MFHC and Mega Bank, while Shiu Kuang-si was appointed as his replacement by Taiwan Premier Lin Chuan.[9] Tsai had reportedly offered to resign more than 10 times since May 2015, but his offer was repeatedly rejected by

Minister of Finance Chang Sheng-ford on the grounds that the January 2016 presidential election was approaching.[10] Mega Bank also carried out an organisational restructuring, which included separating the Risk Management Committee from the Asset Liability and Risk Management Committee as a standalone independent committee, and establishing new departments such as the Anti-Money Laundering Centre.[11]

Privatisation or a Facade?

"Some of the largest state-owned enterprises are becoming almost like private corporations… They are traded in stock exchanges and have boards of directors, maybe even with external managers. We haven't always understood these changes."
– Associate Professor Aldo Musacchio, Harvard Business School[12]

To improve the performance of Taiwan's banking industry, the Taiwan government focused on privatising many state-owned banks in the 1990s.[13] Although Mega Bank became a privatised bank, it still maintained some inextricable links to the Taiwan government.[14] As of September 2016, the Ministry of Finance was the largest single investor of Mega Bank, with an 8.4 percent share ownership, and was able to appoint seven directors to the MFHC board to represent its interests.[15]

The track records of the two ex-chairmen of MFHC were indicative of their connections with the government. Tsai, who served as Chairman of MFHC from 1 July 2010 to 1 April 2016, had also served in various governmental organisations.[16] In fact, he was appointed to the Board by former Taiwan President Ma Ying-jeou.[17] Shiu, who succeeded Tsai as Chairman of MFHC on 16 August 2016, had served as the Chairman of partially state-owned Hua Nan Financial Holdings and held high-level positions at state-owned banks. Shiu had also previously served as the president of MFHC and Mega Bank.[18] Amid criticism over possible conflicts of interests in the Mega Bank scandal, Shiu resigned from his position as Chairman within two weeks of his appointment, on 31 August 2016.[19]

The Beginning of a Mega Failure

In June 2009, Mega Bank admitted to breaches of the Australian Financial Transaction Reports Act and the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF). Following this, Mega Bank agreed to enter into an enforceable undertaking with the Australian Transaction Reports and Analysis Centre (AUSTRAC), and its processes and procedures would be reviewed by the Australian Prudential and Regulatory Authority (APRA).[20] An enforceable undertaking was an alternative to criminal or civil enforcement action in ensuring compliance with the AML/CTF Act.[21]

Two months later, Mega Bank entered into another enforceable undertaking with APRA for suspicious transactions identified within the bank. APRA had concerns that Mega Bank's risk management system and internal audit were ineffective. In addition, some of the bank's staff had structured transactions to bypass the anti-money laundering laws. Some staff also knew about the non-compliant practices but did not act upon them.[22]

Despite prior warnings, concerns regarding Mega Bank's compliance with financial services laws were raised for the third time in August 2010, this time by the Australian Securities and Investments Commission. No penalties were imposed, but the bank had to undergo an independent review by PricewaterhouseCoopers.[23]

The Mega Fine

"DFS will not tolerate the flagrant disregard of anti-money laundering laws and will take decisive and tough action against any institution that fails to have compliance programs in place to prevent illicit transactions." – Maria T. Vullo, Financial Services Superintendent[24]

On 19 August 2016, The New York State Department of Financial Services (DFS) announced that Mega Bank's New York branch (Mega-New York) was fined US$180 million for money laundering activities. During the investigation, DFS discovered "numerous deficiencies in Mega-New York's compliance function". These deficiencies were of great concern as Mega Bank also operated branches in Panama, a country often associated with money laundering.[25] A significant number of the bank's "customer entities" were found to be shell companies formed by Mossack Fonseca, the law firm involved in the Panama Papers scandal.[26]

Failed Risk Management and Internal Controls

DFS highlighted several internal control problems present in Mega-New York. Firstly, there was a lack of proper segregation of duties between the compliance and business functions, due to conflicting responsibilities of certain compliance personnel. For instance, Mega-New York's BSA/AML officer was also operations manager of the Business Division.[27]

DFS further found fault in Mega-New York's transaction monitoring systems and policies. Compliance staff failed to regularly review "surveillance monitoring filter criteria designed to detect suspicious transactions".[28] Various documents were also not translated from Chinese to English, impeding effective checks and investigations by regulators.[29]

In addition to these structural deficiencies, the staff at Mega-New York lacked proper knowledge and training with regards to US regulatory requirements. These included executive staff such as the BSA/AML Officer and the Chief Compliance Officer.[30]

Suspicious Activity Involving Panama Branches

The compliance failure identified at Mega-New York further raised concerns over suspicious activity involving the Panama branches. Due to the high risk of money laundering in Panama, the bank was supposed to deal with transactions between Mega-New York and the Panama branches with high-level surveillance and diligence. However, the compliance failures in the bank's New York branch raised doubt on whether checks had been carried out properly. This was aggravated by the large sums of financial transactions between the two locations. On top of this, Mega-New York failed to give adequate explanations regarding suspicious "payment reversals" received from its Panama branches.[31]

Negotiating the Fine

DFS reportedly intended to impose a larger penalty on Mega-New York, but the penalty amount was negotiated down by Perng Fai-nan, the governor of the Central Bank of the Republic of China. Perng was the brother-in-law of Shiu, the Chairman of MFHC at that time.[32]

Huang Kuo-chang, the New Power Party Executive Chairman, expressed his concerns about "the administrative negligence and the question of who will foot the bill for the US$180 million fine". He also raised concerns about the inappropriateness of having Shiu participate in the administrative investigation conducted by the Financial Supervisory Commission (FSC), and the inaction of the Ministry of Finance against former MFHC Chairman Tsai. By not holding the bank's officers responsible, Huang believed that it was unfair to the shareholders and taxpayers who might end up bearing the burden for the fine.[33]

MFHC Denial

After his meeting with US regulators, Shiu, then-Chairman of MFHC, claimed that his US trip was not meant to investigate misconduct at the bank, but to meet with US regulators and clear up any misunderstanding.[34] Moreover, the Vice-President of MFHC also denied that the bank had any involvement in money laundering activities, claiming that the fine was due to the bank's failure in adapting to the new and more stringent anti-money laundering regulations in the US.[35]

Government Involvement in Mega Bank

As the money laundering saga continued to snowball, Taiwan lawmakers alleged former President Ma Ying-jeou's involvement in the illegal transactions. Ma was also the Chairman of Kuomintang (KMT), the second largest political party in Taiwan and the ruling party at that time, which was accused to have used Mega Bank to conduct money laundering activities.[36] In its defence, KMT released the results of an investigation by the Legislative Yuan, showing that none of the 174 suspicious transactions flagged by DFS had passed through Taiwan.[37] However, political activists still found it difficult to ignore the possibility that Mega Bank had assisted KMT in cleaning up illicitly gained assets. Democratic Progressive Party (DPP) legislator Luo Chih-cheng alleged that Mega Bank had been used to empty out KMT's assets, while Mega-New York was used to launder them.[38] Another DPP legislator, Su Chen-ching, also highlighted the fact that the bank had increased its loan to KMT-backed businesses, from NT$3.68 billion in 2010 to NT$11.19 billion in 2015.[39]

Cleaning Up the Mess

"The amended law shows our country's resolve to fight economic crimes and money laundering." – Premier Lin Chuan[40]

The entire Mega Bank scandal had cast doubt on the integrity of the anti-money laundering protocols in Taiwan.[41] Given the severity of the situation, the Taiwan government undertook several corrective actions. In one notable move, the government passed a bill to amend the country's anti-money laundering law, which included, inter alia, increasing the ceiling for the amount of fine from NT$1 million to NT$5 million.[42]

The Ministry of Finance also planned to make several improvements by strengthening mechanisms, requiring government-controlled banks to report serious incidents, assessing the qualifications of board members who represent government-controlled shares, reviewing the responsibilities of the board of the banks, as well as enhancing on-the-job training for staff assigned to overseas branches.[43]

Conflict of Interests: Self-Investigation is No Investigation

The Executive Yuan was first informed of the fine on 1 August 2016. Before breaking the news of the Mega-New York scandal to the public on 19 August 2016, it appointed Shiu as the new Chairman of MFHC on 11 August 2016.[44] Premier Lin justified the appointment by asserting that Shiu bore little responsibility in the scandal, and that he had prior experience from dealing with a similar crisis.[45]

Thereafter, in response to the money laundering scandal, the Taiwanese government appointed the FSC to lead an administrative investigation on 21 August 2016.[46] Tsai, who held office as MFHC's Chairman when the lapses in compliance occurred, was summoned to the FSC headquarters for questioning on 28 August 2016. FSC officials claimed to have obtained greater insight into the case after the questioning, but refused to release any details.[47]

As investigations continued, Huang expressed his concern over the fact that the FSC was "an agency that is likely to be found guilty of administrative negligence over past violations". Furthermore, the fact that Shiu was involved in the investigations was questionable given his alleged involvement in the scandal.[48] Some political activists also pointed out the potential conflict of interests embroiling the FSC-appointed task force since they were reporting to the Ministry of Finance, which had substantial shareholdings in Mega Bank.[49] Furthermore, the Deputy Minister of Finance also stated that there were no plans to level any charges against Tsai.[50]

The Investigator Becomes the Investigated

Amid mounting pressure and criticism on the Executive Yuan, Premier Lin appointed a new cabinet task force, which consisted of legal and finance experts, on 30 August 2016 to investigate Mega-New York and oversee the ongoing efforts under the FSC and the Ministry of Justice.[51]

On 18 September 2016, Premier Lin issued a directive to investigate possible negligence of FSC officials in detecting compliance issues in Mega Bank. The political responsibility of FSC and the Ministry of Finance would be reviewed as well. FSC's claim of ignorance of Mega Bank's non-compliance could not be overlooked, given its responsibility in overseeing financial institutions. This sent a message to the top financial watchdog that it would be held accountable if it failed to detect serious breaches of regulations made by banks.[52] Indeed, as pointed out by Huang, in addition to the misconduct within the bank itself, the Mega Bank incident had also revealed the shortcomings of Taiwan's regulatory bodies.[53]

Fat Leonard: The Elephant in the U.S. Navy's Room

Case Overview

In January 2015, Leonard Glenn Francis, President and Chief Executive Officer (CEO) of Glenn Defense Marine Asia Pte. Ltd. pleaded guilty to charges of bribery, conspiracy to commit bribery and conspiracy to defraud the United States, admitting that he had defrauded the U.S. Navy of US$35 million. It was reported that over 200 naval officers were under investigation in connection with the corruption scandal that involved some of the highest-ranking officers of the U.S. Navy.[1] This case can be used to discuss issues such as the impact of organisational culture on corruption; bribery risks in certain sectors and countries; cross-border bribery risks; internal control measures to combat bribery and corruption; and the effectiveness of legislation in addressing bribery risks.

Glenn Defense Marine Asia

Glenn Defense Marine Asia Pte. Ltd. (GDMA) is a subsidiary and the flagship company of the Glenn Marine Group, a premier maritime service provider.[2] GDMA was a commercial and government contractor whose main business involved the husbanding of marine vessels.[3] Based in Singapore, GDMA was founded in 1946[4] with operations mainly in the Asia-Pacific, including Japan, Singapore, Thailand, Malaysia and the Philippines. GDMA was a reputable company with strong business ties with the U.S. Navy for 25 years.[5]

Between 2006 and 2013, GDMA was awarded multiple high-value contracts to provide husbanding services to U.S. Navy ships and submarines at ports throughout Singapore, Japan, Philippines, Malaysia, Pacific Islands, South Asia and Islands in the Indian Ocean.[6] In addition to the provision of husbanding services, GDMA also engaged in other services such as naval support, maritime security, and force protection.[7]

Fat Leonard

Leonard Glenn Francis was a Singapore-based defence contractor who was president and CEO of GDMA.[8] Born in Penang, Malaysia, he was nicknamed Fat Leonard, Lion King and Big Bro due to his large size.[9] Francis took over the family business – Glenn Marine Enterprise – from his father at the age of 24 and later renamed the company as Glenn Defence Marine Asia. As GDMA became a renowned name in the husbanding services industry, Francis amassed wealth which he unabashedly flaunted. Francis was known to be a remarkably sociable individual who had a way with people. His penchant for throwing lavish parties for his clients and business partners earned him a reputation as a high-flying businessman in the maritime and defence circles.[10]

However, on 16 September, 2013, the party ended for Francis when he was arrested in a hotel room in San Diego on charges of bribing U.S. Navy officers to obtain contracts and defrauding the United States.[11]

The U.S. Navy

The U.S. Navy, and the military in general, has a very hierarchical structure "characterised by strong chains of command and obeying orders", which may enable high-ranking officers to get away with corrupt acts without being reported by their subordinates.[12] As the high-ranking officers provided Francis with classified information in exchange for bribes, subordinates would rarely question their actions.[13]

The Navy is always on the move, constantly negotiating access to foreign ports for resupply and replenishing, and is therefore particularly reliant on foreign contractors at these ports. These contractors are known in the maritime world as husbands, a position that GDMA served for the U.S. Navy. GDMA would arrange everything that the Navy ships in the Pacific Rim required, from tugboats for docking to people who emptied the bilges. At the end of the stay in port, the bill for various subcontractor services would be presented by the husbanding agent to the ship.[14]

However, the system was not particularly well run, as it was difficult for ship captains to keep up to date with changing costs, fees, and tariffs. "The Navy's ability to track and analyse port-visit cost changes remains rudimentary," says a 2009 Naval Postgraduate School paper.[15]

Throughout the process of contracting, there was little oversight and insufficient internal controls to deter abuse and fraud, thereby creating opportunities for bribery to occur.[16] Adding to this, there is a greater risk when dealing in foreign countries and ports where bribery and corruption are pervasive, such as Indonesia, Philippines and Thailand, which rank poorly in the Corruption Perceptions Index.[17] In such countries, giving and accepting bribes are commonplace.

Modus Operandi

Between 2006 to 2013, in order to win exclusive high-value husbanding services contracts from the U.S. Navy, Francis offered bribes to Navy officers in the form of cash, gifts, prostitutes, airfare, luxury hotel stays, alcohol and much more. He cultivated favour with high-level commanders through his lavish spending and hospitality, reeling the U.S. officials into his sphere of influence. During a court hearing in 2015, Robert Huie, an assistant U.S. attorney in San Diego, referring to Francis' acts of bribery, commented that "Mr. Francis' conduct has passed from being merely exceptional to being the stuff of history and legend."[18]

Steering ships his way

For Francis and GDMA, the bribes often had their intended effect. In exchange for the bribes, the Navy officers provided Francis with information about the scheduling and selection of U.S. Navy port visits, competitors' pricing and performance, competitors' bids and other information.[19]

Armed with this information, Francis was able to influence the 7th Fleet's port visits. In one instance, Francis requested Captain David Newland, the Chief of Staff to the 7th Fleet Commander, to convince Navy officials to ensure that the U.S.S. Abraham Lincoln's escort ships docked at Laem Chabang, Thailand. Newland, having been a recipient of Francis' gifts, duly complied and exerted pressure on Navy officials to ensure the docking of three escort ships at Laem Chabang. In April 2006, GDMA was awarded nearly US$2 million in contracts to service the escort ships of USS Abraham Lincoln. Similar incidence of diverting U.S. Navy ships to ports in Laem Chabang, Port Klang and Phuket occurred multiple times, earning GDMA millions of dollars in profits.[20]

Francis and other GDMA employees also undermined the bidding process for Navy contracts by getting his Navy co-conspirators to brush aside competition and put pressure on Navy officials who were contemplating awarding contracts to GDMA's competitors.[21]

Bogus companies and fraudulent quotes

The contracts that the Navy awarded GDMA were often of significant value. In 2011, the Navy Supply Systems Command awarded GDMA three contracts in three different regions. The contract in the Southeast Asia region had a first-year base value of US$25 million, comprising of fixed price items where prices of services were agreed upon beforehand, fuel and port tariff items which were billed at the actual cost without markup, as well as incidentals.

The process of sub-contracting for incidentals required GDMA to provide at least two competitive quotes, after which the Navy would decide which vendor to use. GDMA was allowed to submit its own quote among the two required, but it was required to disclose any profit or mark-up.[22] GDMA's management team created bogus companies and port authorities, representing them to be bona fide organisations to the U.S. Navy and subsequently submitted fraudulent quotes for incidentals and inflated port tariff items under these bogus companies. Fraudulent bids that were fictitious or falsified were submitted to ensure that GDMA's quotes would be chosen. These quotes were inflated, allowing GDMA to illicitly overcharge the U.S. Navy for the provision of the aforementioned items over a span of eight years. It was reported that GDMA and Francis defrauded the U.S Navy for close to US$35 million through this scheme.[23]

Covering their tracks

As Francis and the corrupt Navy officials became wary that their lavish parties and extravagant dinners were gaining unwanted attention, they attempted to cover their tracks by fabricating receipts that represented only a small fraction of the actual value of things that Francis had provided, or reimbursing Francis to comply with ethics rules.[24,25]

The mole investigator

Francis was not afraid to continue his exploits and managed to evade the authorities as he had control over an agent within the Naval Criminal Investigative Service (NCIS), Supervisory Special Agent John Bertrand Beliveau, Jr., who fed

Francis sensitive information and gave advice on the agency's investigations against him and GDMA.[26] Beliveau proved extremely reliable and Francis' intelligence system became so successful that Francis began to feel absolutely untouchable by authorities.[27]

Establishing an elaborate network

Over the years, Francis formed a strategic network of informants throughout the ranks of the Navy, including its contracting office in Singapore, the hub for maritime operations in Asia, the wardroom of the flagship of the Navy's 7th Fleet and the U.S. Embassy in Manila. While allegations against GDMA came up frequently in law enforcement case files, informants and agents whom Francis had bribed were quick to shoot down accusations, hampering or dismissing investigations.[28]

All in all, NCIS opened a total of 27 investigations into GDMA but failed to gather sufficient evidence to take action against it. All 27 cases were eventually closed. With turncoat admirals within the Navy, investigative efforts were blocked for more than two years. It was only in 2013 that they were able to gather sufficient evidence to charge and arrest Francis.[29]

Breeding corruption

Francis manipulated the naval officers by feeding their insatiable lust. One official on the receiving end of such bribes was Commander Jose L. Sanchez, a logistics officer at the headquarters of the 7th Fleet, who regularly sought out Francis to arrange for the services of prostitutes for him and his friends in Singapore, Kuala Lumpur, and Manila. This was in exchange for classified ship and submarine schedules, as well as tip-offs each time GDMA went under the radar for defrauding the Navy. In total, Sanchez was estimated to have accepted tens of thousands of dollars' worth of cash and prostitution services, in addition to other bribes.[30]

Francis was also adept at capitalising on the greed of several other Navy officers. One example was Dan Layug, a petty officer in the Japanese headquarters of the 7th Fleet. Francis and his team initially bribed Layug with a free mobile phone, but over the next three years, the bribery escalated to a monthly allowance of up to US$1000 and free hotel stays.[31]

Once Navy officials got a taste of Francis' lavishness, their lust and greed always seemed to make them seek him out again. The Navy officials who most frequently participated in these revelries at Francis' expense and provided him with confidential information became known as the "cool kids' or the "wolf pack", making them more devoted accomplices in Francis' grand corruption scheme.[32]

Silent Whistleblowing

There were occasions when individuals lodged complaints about Francis, but the Navy's whistleblowing process proved futile against other forces. The culture of corruption had become deeply entrenched in the 7th fleet. Despite Francis' scheme becoming known to many, few took any action, preferring instead to fiercely protect the status quo. Lower-ranking officials who challenged GDMA and attempted to blow the whistle were intimidated by Francis and other Navy officials.[33]

The involvement of high-level officials proved to be a further impediment to junior officers who wanted to expose Francis' scheme. This was because promotions in the U.S. Navy were heavily dependent on a superior's endorsement, and the Navy had an "up or out" promotion policy; that is, junior officers either get promoted or are forced to leave the service. Junior officers seeking to stay in the Navy long enough to earn their pensions were thus incentivised to keep their bosses satisfied, even if it meant feigning ignorance about their corrupt activities.[34]

Failure of Ethics Rules and Policies

There were several instances in the scandal when the ethics rules and policies put in place in the U.S. Navy clearly failed. On 16 February 2006, the 7th Fleet Judge Advocate General circulated an ethics message to all senior officers of the 7th Fleet advising them about ethics regulations on acceptance of gifts in foreign ports, which clearly prohibited receiving gifts, particularly from defence contractors such as GDMA. The Navy officers forwarded the ethics message to Francis, informing him that their corrupt relationships would have to be kept a secret. The very next day, Francis lavished Navy officers with a dinner at the Petrus Restaurant in Hong Kong that cost US$20,435.[35]

In January, 2010, a senior civilian lawyer drafted an ethics message for Navy personnel, reminding them of federal ethics rules that restricted the value of gifts from defence contractors, as well as introducing a regulation that required the submission of receipts and a written justification for accepting gifts in kind. Although it did not specifically target Francis or GDMA, it applied solely to contractors that provided port services, an area that GDMA dominated in Asia. The proposal was rejected and revised multiple times due to admirals who were on good terms with Francis, such that the final approved message two and a half years later had much fewer restrictions than when it was first drafted.[36]

Catching the Whale

When the United States Federal Agents eventually discovered that there was a mole within NCIS, they decided to set a trap for Francis, which eventually led to his arrest. They were able to gain access to Francis's emails, which revealed incriminating evidence that pointed to corruption and bribery involving GDMA and U.S. Navy officials.

Francis was charged under three separate counts of the United States Code - Conspiracy to Defraud the United States, Bribery, and Conspiracy to Commit Bribery. Based on the plea agreement signed by the attorneys for the United States and Francis, Francis faces a total prison sentence of 25 years.[37] His sentence is still pending.[38]

In November 2015, a total of 440 active-duty Navy personnel and Navy veterans, including 60 current and former admirals, were under investigation for suspected violations of military law or federal ethics rules in connection with Francis and GDMA.[39] The number has since grown to a total of 480, excluding those who have already been charged. It has been reported that more than half of these individuals have been cleared of wrongdoing. However, the Navy has substantiated misconduct by approximately 50 of them thus far.[40] Five sailors have been subject to court-martial proceedings and have been charged under military law, four of whom have either contested the charges or declared that they are innocent of wrongdoing. Additionally, six admirals have been admonished and disciplined by the Navy, with punishments such as censure, reduction of rank, forced retirement, fines and administrative action.[41]

To date, the U.S. Department of Justice has indicted 28 people,[42] including two admirals.[43] The indicted include Francis and four other GDMA executives who have pleaded guilty; 14 Navy officials who have pleaded guilty, including Sanchez, Layug and Beliveau; as well as nine named Navy officials, including Newland; and one unnamed GDMA employee awaiting trial. Those sentenced face prison terms ranging from 18 months to 12 years, with some facing fines and restitution.[44]

However, these cases represent but a small fraction of a longer list of present and retired Navy officials who remain under investigation but who have not yet been publicly named.[45]

Additionally, the former lead contract specialist of the U.S. Navy, Gursharan Kaur Sharon Rachael, was charged under the Prevention of Corruption Act (PCA) of Singapore for corruption and money-laundering offences punishable under the PCA and the Corruption, Drug Trafficking and Other Serious Crimes (Confiscation of Benefits) Act (CDSA), relating to accepting bribes from Francis.[46]

GDMA in Tatters

Under the Plea Agreement between GDMA and the U.S. Navy, GDMA was charged with a maximum penalty of a 5-year probation and a minimum of a one-year probation.[47] In the forfeiture addendum, GDMA consented to forfeit to the United States US$35 million, which represents a portion of the gross proceeds of the conspiracy to commit bribery and defraud the United States.[48]

Besides Francis, four other executives of GDMA, Neil Peterson, Linda Raja, Edmond Aruffo and Alex Wisidagama, pleaded guilty for conspiring to defraud the U.S. Navy.[49] Wisidagama was sentenced on 18 March 2016 to 63 months,[50] while Peterson and Raja were sentenced on 11 August 2017, to 70 months and 46 months respectively.[51]

Sweeping Reforms Across the U.S. Navy

In an audit report dated 30 September 2014 concerning Navy husbanding and port services contracts, the Auditor General of the Navy outlined opportunities to improve internal controls in areas such as the acquisition of port services, awarding of task orders or contracts, surveillance responsibilities, and invoice review and payment process supporting the delivery of goods and services relating to husbanding and port services contracts.[52]

The recommendations include the designation of an organisation within the Navy to take primary responsibility for the oversight of assessments and improvements in internal controls; the detailing of specific responsibilities, in writing, of each command in the appointed office of primary responsibility and circulating it Navy-wide to ensure necessary oversight and accountability over husbanding and port service processes; improving the system controlling approvals and authorisation of the purchase of goods and services overseas; and conducting routine assessments of individual commanders to ensure compliance with Navy regulations.[53] Improvements were also made to the whistleblowing channels and ethics training programs based on best practices that were being employed around the world.[54]

With the implementation of new measures and revamps of processes still in progress, one question is whether these changes can truly address deficiencies and change the organisational culture to prevent a similar scandal in the future.

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JLJ Holdings Limited: Poisoned by Its Rotten Apple
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Sun Hung Kai: Brothers (Up) in Arms

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GlaxoSmithKline: The Etiquette of Bribery

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Petrobras: Not Your Typical Carwash

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Keppel Corporation: Offshore and Off-Course

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Mega Bank, Mega Failure?

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Fat Leonard: The Elephant in the U.S. Navy's Room

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Mak Yuen Teen is an associate professor of accounting and former Vice Dean of the NUS Business School, National University of Singapore, where he teaches corporate governance. He holds first class honours, master and PhD degrees in accounting and finance and is a fellow of CPA Australia. He was the founder and director of the first corporate governance centre in Singapore at the National University of Singapore. Over the past 10 years, Prof Mak has also held positions of Asia-Pacific or Singapore head of research in major consulting firms.

Prof Mak has served on key corporate governance committees in Singapore developing and revising codes of corporate governance for listed companies and not-for-profit organisations. He has also been involved in developing several corporate governance ratings and scorecards and has chaired judging panels for corporate governance-related awards in Singapore and the region.

Prof Mak is an active researcher, commentator, speaker and advocate on corporate governance. He has published reports on topics such as corporate governance of banks and insurance companies, board diversity, governance of company groups, annual general meetings, and executive and director remuneration. Each year, he edits a collection of corporate governance case studies published by CPA Australia, and a selection of these cases have also been translated to Chinese and Vietnamese. He has also co-produced two volumes of corporate governance cartoons, with all proceeds from these donated to charities.

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Prof Mak has served on boards of several large not-for-profit organisations in Singapore, including as board chairman, and on audit committees of large not-for-profit organisations in Singapore and in UN funds based in New York. He also served as a member of the Governing Council of the Singapore Institute of Directors from 2000 to 2005.

In 2014, he received the Corporate Governance Excellence Award from the Securities Investors Association (Singapore) for his contributions to corporate governance in Singapore, becoming only the second individual to receive this award. In 2015, he received the Excellence in Corporate Governance Award from the Minority Shareholders Watchdog Group in Malaysia for his contributions to corporate governance in the region. That same year, he was recognised by the Singapore Institute of Directors as a Corporate Governance Pioneer in Singapore.

For more on Prof Mak’s work, visit: www.governanceforstakeholders.com.

Endnotes

JLJ Holdings Limited: Poisoned by Its Rotten Apple

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