

Should Hong Kong businesses be resetting their integrity agenda?

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COVID-19 disrupted businesses globally and impacted the way they operate, with knock on effects on employees, counterparties and customers. Amid the turmoil, new opportunities and challenges emerged, some posing difficult ethical dilemmas affecting future viability and success of businesses. These factors created a perfect storm for misconduct. Two plus years on, we are starting to see its impact on businesses and their personnel.

In our "Integrity Is Key" publication¹ which surveyed enforcement actions for corruption related offences in Hong Kong the second half of 2021, we reported on a number of such actions, noting that they involved diverse industries, functional areas, and both senior and junior personnel in organizations as well as "gatekeepers" such as directors, senior management and professionals from underwriting and accounting firms. The EY Global Integrity Report 2022 ("GIR")² published earlier this year reported that more organizations experienced incidents of significant fraud in Hong Kong (19%) than globally (13%). Further, nearly two fifths of the Hong Kong respondents (40%) stated that they would be prepared to engage in misconduct to improve their career progression or remuneration package. Are the enforcement actions and survey results a mere coincidence or a harbinger of more deep seated integrity issues that need to be addressed?

In this publication, we highlight some key observations from the GIR, focusing on the Hong Kong data, consider possible reasons that standards may be slipping and ways in which businesses can foster a culture of integrity to ensure a sustainable future.

Hong Kong's integrity scorecard

Most Hong Kong respondents (96%) believe integrity is important to sustain their business, with more than two out of five (43%) saying that behaving with ethical standards or complying with laws, rules and regulations are important aspects of integrity. A fairly high number of respondents (70%) also indicate that they tend to / strongly agree that impact on reputation is always considered when important decisions are made in organizations.

Overall, they consider integrity standards have stayed the same or improved - only 6% respondents indicated that they felt that standards have dropped. A high percentage of Hong Kong respondents are fairly / very confident that employees in their organizations demonstrate integrity in the work they do (81%), and that management (85%) and employees (86%) abide by relevant laws, codes of conduct and industry regulations. Only 27% consider that management would misconduct themselves for short term gain and 23% consider that misconduct by senior or high performers would be tolerated, which are much lower than the global averages of 43% and 33% respectively.

¹ Integrity is key: Hong Kong's new Corporate Governance Code mandates that issuers establish anti-corruption and whistleblowing policies: https://www.eylaw.com.hk/en_hk/publications/our-latest-thinking/2022/jan/integrity-is-key

² EY Global Integrity Report 2022: https://www.ey.com/en_gl/forensic-integrity-services/how-a-focus-on-governance-can-help-reimagine-corporate-integrity, which canvassed the views of more than 4,700 employees, managers and board directors from 54 countries and territories, including Hong Kong.

However, as highlighted in our introduction, organizations seem to have experienced more incidents of significant fraud in Hong Kong than globally, and two fifths of the Hong Kong respondents stated that they would be prepared to engage in misconduct to improve their career progression or remuneration package, including by ignoring unethical conduct in their teams (19%), ignoring unethical conduct by suppliers, distributors and other third parties (19%), offering and/or accepting bribes (16%), falsifying financial records (12%), providing false information to management (10%), misleading external parties such as auditors or regulators (10%) and falsifying customer records (10%). Moreover, two thirds of respondents in Hong Kong (67%) stated they would be very / fairly concerned if information about their decisions taken as part of their work are subject to public scrutiny, which is much higher than the global average (42%).

There is clearly a disconnect between what Hong Kong respondents have said about their organization's standards of integrity, and what they have said management and they would be prepared to do to get ahead, as well as the standards themselves manifested in the incidents of fraud and corruption enforcement actions. We consider below various factors that may have led to this incongruity and potential deterioration of standards.

Reasons integrity standards may be deteriorating

External factors

Undoubtedly, the ongoing COVID-19 pandemic has contributed to the potential deterioration in standards. The upheaval that it has caused to business operations and relationships, including the introduction of remote working arrangements and the engagement of new supply chain partners, bypassing usual policies, procedures and controls, has created opportunities for unethical behaviour. Many organizations and individuals are under tremendous economic pressure and looking for ways to *"turn things around"*, which may have led some to rationalize unethical behaviour. In Hong Kong, organizations have also had an additional year of depressed economic performance due to the social unrest in 2019. Unsurprisingly, between 42 - 54% Hong Kong respondents believe external factors, including COVID-19 pandemic, politics, changing rules and societal expectations are making it more difficult to carry out business with integrity. In fact, a higher percentage of Hong Kong respondents compared to respondents globally believe it is more challenging to work given market condition and rapid change in environment (63% for Hong Kong cf. 57% for global).

Lack of tone from the top and focus on integrity

A much lower percentage of Hong Kong respondents (31%) recalled hearing management communicate about importance of behaving with integrity in the last 18 months as compared to global average (43%). Additionally, while almost all Hong Kong respondents said they have some form of internal policies and measures in place in their organizations, only 37% said they had a code of conduct on how they should behave in business, only 30% said they had a statement of organization values to inspire people's conduct, only 27% said they had training on ethics and integrity in business or professional life, only 26% said they had a whistleblowing hotline to report wrongdoing confidentially, only 26% said they had incentives to encourage behaviors that demonstrate integrity, and only 26% said they had sanctions applied to address behaviors which do not demonstrate integrity.

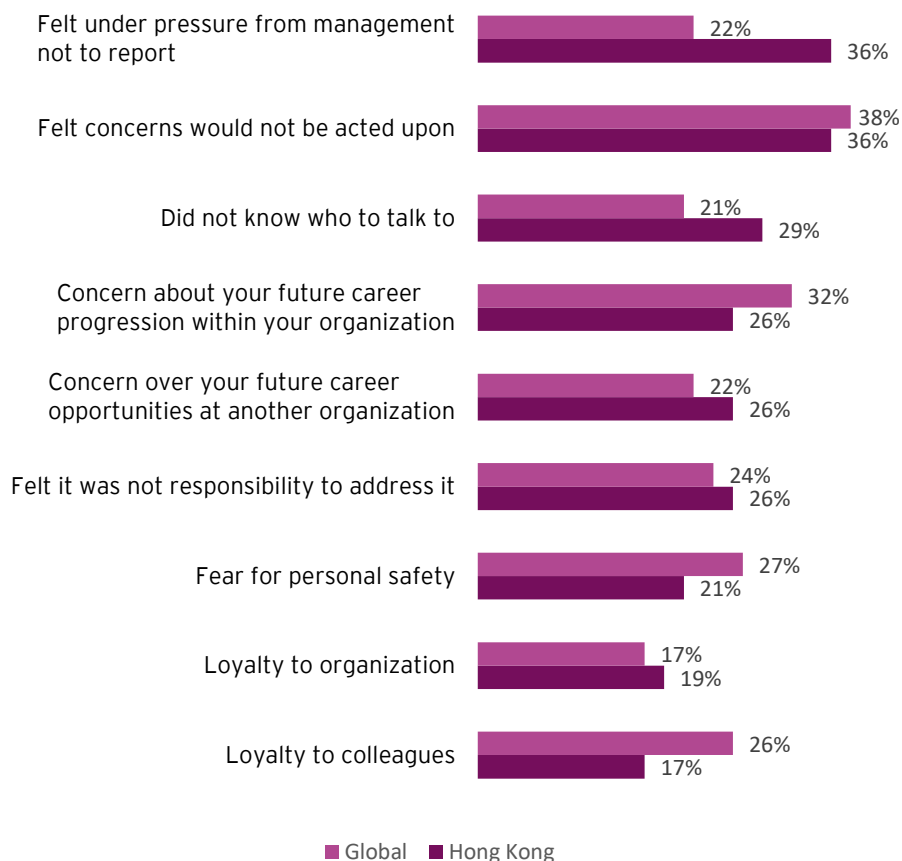
Unsurprisingly the lack of *"tone from the top"* and consistent messaging on the critical importance of integrity in businesses, appears to have resulted in Hong Kong respondents having differing views on what having *"integrity"* means and what standard of behavior is expected. While close to half of Hong Kong respondents (43%) consider *"compliance with laws and regulations"* is a very / fairly important characteristic of integrity, only 32% believe that *"acting responsibly to colleagues, customers, suppliers and others"* and 31% believe that *"doing the right thing even when no one is watching"* are very / fairly important characteristics of integrity. These percentages are lower than global average.

It is also alarming that one in four Hong Kong respondents said that it is easy to bypass the standard business rules and processes in their organizations.

Lack of a speak up culture

Another potential cause may be the low percentage of people willing to speak out when there are integrity concerns. Hong Kong respondents say the dominant reason for not reporting misconduct in their organization is pressure from management not to report and concern that no action would be taken. A higher number of Hong Kong respondents as compared to global average also do not know who to report to, feel it is not their responsibility to address the concerns and have concerns about their future career opportunities.

Figure 1: GIR: Reasons for not reporting concerns



Resetting the integrity agenda

The GIR results indicate that integrity standards are slipping and businesses need to reset their integrity agenda.

As a starting point, boards and senior management need to take stock of what is happening in their organizations. Technology can and should be leveraged to perform robust gap analysis to identify risk areas for mitigation.

Secondly, boards and senior management need to invest in building a culture of integrity which is focused on doing the right thing - not just complying with laws and regulations. Some key steps to consider include (i) providing clear and consistent messaging from the top down on the importance of having a culture of integrity; (ii) having an organization statement on values to inspire ethical behavior; (iii) having a code of conduct defining acceptable and unacceptable behaviors with corresponding incentives and sanctions; (iv) providing coaching on the importance of business integrity; (v) encouraging a speak up culture backed up by a properly implemented and resourced confidential whistleblowing hotline; and (vi) demonstrating commitment to a culture of integrity by incentivizing ethical behaviors and sanctioning unethical ones.

Thirdly, boards and senior management should ensure that they have a comprehensive compliance framework and program which leverages technology, in particular to detect unethical behavior and guide responses in investigating, remediating and preventing its recurrence.

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