



ForensicFocus

China's challenging documents

Fighting back on falsifications and forgeries.

March 2016



Today's reality

- China is a strategic market for most organizations doing business globally. Unfortunately, this can lead to higher exposure to corruption.
- Companies may be putting themselves at risk if they are not vigilant in detecting falsified documents, as in-country companies often rely on scanned or electronically submitted information, and original versions of key documents are seldom available.
- Companies with compliance programs in place that implement enhanced procedures to prevent, detect, and respond to falsified documents can save on compliance costs and, moreover, can reduce possible fines and penalties over time.

Overview

The cultural and political impacts of doing business in China entail the combination of high corruption exposure levels, a relationship-oriented business culture (*guanxi*), and the government's anti-corruption initiative. Falsified documents can play a large part in exposing companies to risk. They can implicate violations of the company's code of conduct, laws, and regulations of local and/or foreign jurisdiction laws, such as the U.S. Foreign Corrupt Practices Act and the U.K. Bribery Act. The degree of violation varies, depending on the nature and the benefactor of the scheme.

China's frequently falsified business documents

Among China's three most frequently falsified business documents are 1) *fapiao*, 2) company chops (seals), and 3) vendor-supporting documents via travel agencies.

Fapiaos

A *fapiao* (发票) is an official invoice issued by the Chinese tax bureau and is widely used as the main supporting document for ongoing transactions in China. The details of *fapiaos* usually include a code, number, issuer, expense amount, type and date. There are different types of *fapiaos*, such as fixed-amount, machine-printed, and handwritten. Depending on the expense type, *fapiaos* can be either B2B- or B2C-issued by either a state tax bureau (国税) or a local tax bureau (地税).

Generally, *fapiao* authenticity can be verified by checking the combination of the *fapiao* code, number, and password (if any) via the tax bureau's Web site or hotline. The detailed information available for verification varies among the provinces and cities, and the verification results commonly indicated valid, invalid, record not found, inconsistent amount, inconsistent vendor or inconsistent date. Due to the limited information provided in *fapiao* verification and the various level of detail among the provinces and cities, what is most concerning is that falsifying *fapiaos* is not a difficult task. They are often faked, inflated, "doppelgänger-ed," or substituted.

One of the most common ways of falsifying *fapiaos* is to buy them from vendors or black market *fapiao* dealers. Some vendors may sell valid *fapiaos* in return for commission, while *fapiao* dealers distribute flyers or business cards at major public transportation spots, such as train stations, to seek potential buyers.

Another common way of falsifying fapiao is to make copies of the same one and manipulate the date, amount, or issuer. As the input of fapiao verification may only require the unique combination of the fapiao code and number, these manipulated, false fapiao may actually show as valid during the online or hotline verification with the tax bureau.

Company chops

When conducting business in China, what matters the most on contracts or agreements besides an authorized signer's signature is what is known as the qualified company chop—an official company seal or stamp used to sign all legal documents.

The little red chop, in lieu of signatures, is a symbol of authorization of execution, which plays a critical role on legally binding documents. It is normally round in shape and has the registered name of the company, and/or its related pattern engraved. The production of a company qualified chop needs to be approved by the Ministry of Public Security and local Public Security Bureaus, and engraved at designated institutions. A sample of the qualified company chop is required to be registered in the Public Security system.

The company chop is normally under authorized personnel's custody, and the chopping process usually follows a formal approval protocol as specified in the company's standard operating procedures.

The most common chop forgery is done by engaging illegal chop engraving services, whose contact information could be located by public domain search or on the printed flyers or business cards distributed to people on the streets. They reproduce a similar chop with the company's name and pattern in accordance with the authorized one. Some people may take advantage of the relationship with the custodian of the chop and borrow it as a sample for the forgery. Others may simply obtain a copy of an effective contract that has been properly chopped and provide it to the engraver for reproduction based on the shape, font, and pattern reflected on the contract.

As revealed in past police investigations, the buyers and the engravers normally complete the transaction without directly contacting each other in person. The cost of chop forgery, in most cases, could be very minimal.

In addition to the prevalence of illegal chop engraving services and the low forgery cost, the lack of a publicly available chop authentication process has also increased the tendency of forgery. Although today's company chops are produced with a unique guilloche pattern, a fingerprint technique, or antiforgery ink—the authenticity can still only be confirmed through official forensic expertise procedures, which is usually too difficult to verify with the naked eye during the regular business contracting process.

Vendor-supporting documents via travel agencies

In China's business operating model, travel agencies are widely used to facilitate event organization and for the vendor payment process. Due to its heavy involvement with a company's business and marketing activities, vendors colluding with travel agencies to fabricate various supporting documents becomes a common practice.

Most companies' nonstock procurement and finance policies require travel agencies to submit an overall service fapiao with the total amount (including the service charge) as well as detailed breakdown of the expense items (if required by the company policy). Some company policies may require underlying vendor fapiao and other supporting documents to be provided, while others may not. Common issues include invalid or substituted fapiao, inflated expenses, mismatched credit card receipts, falsified or manipulated hotel folios, and itemized receipts.

As travel agencies maintain close business relationships with the frequently used vendors, they may take advantage of such relationships and, easily get access to the vendors' official template, and create a set of supporting documents to cover up the falsification. It is important to note that itemized receipt printers can be easily purchased online very inexpensively.

Some of the issues can be uncovered by performing authority database verification, a desktop search, vendor outreach, or a surprise site visit. But some of the issues could be undetected, due to uncooperativeness of vendors, limited retained historical transaction details, or further needs to verify credibility if collusion exist between the travel agency and its vendors.

Companies can take preventive and reactive measures

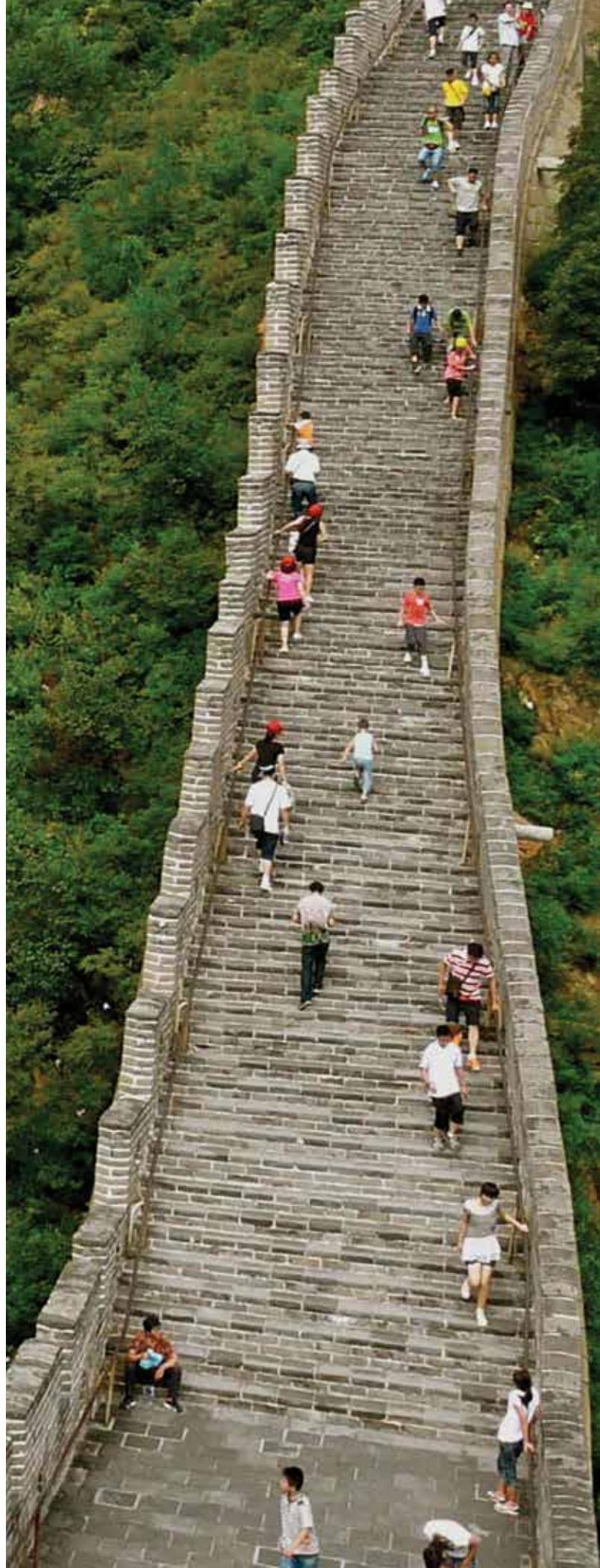
To help combat the risk of encountering falsified and forged documents in China, companies can take various measures.

Prevent

1. Ensure the tone set at the local level is aligned with the parent company. Global policies need to be converted to a more customized and comprehensive language in local subset policies, and the consequences of noncompliance should be specified.
2. Constantly raise employees' and third parties' compliance awareness by setting up systematic training trackers, and closely link the participation and completion of such trainings to a key performance indicator assessment.
3. Enhance the preapproval control matrix for expenses related to business events and activities, revisit the exceptional approval protocol, incorporate an expedited approval process into a system rather than allowing informal consent sent via e-mails, and reassess the expedited approval process under special circumstances to reduce risks of control override.

Detect and Respond

1. Utilize advanced document management and data analytics tools to perform multidimensional review for ongoing risk monitoring purposes, and understand the correlations and key factors reflected from the underlying data for further management actions.
2. Enforce reaction plans for violations of policies more rigorously and timely, perform gap analysis between policies and common practice, and increase individual employees' and supervisors' accountability.



Case studies

Fapiao falsifications discovered in employee time and expense claims

During an employee misconduct investigation, KPMG noticed that some of the subordinates of the company's regional sales manager frequently used fixed-amount fapiao from the same restaurants when claiming expenses.

- We performed fapiao verifications with the local tax bureau hotlines by referring to the preassigned numbers on these fixed amount fapiaos, and concluded they were fake. Furthermore, we cross-referenced expenses submitted by the team members and noted that fapiaos from different team members were sequentially numbered.
- During the interview, several employees admitted their supervisor instructed them to buy the fake fapiaos from the black market near the local train station. They then claimed falsified expense reports with these fapiaos for reimbursement, and the supervisor would decide how to use the money received. Further investigation discovered some of the money was used as a sales incentive, while some was used for bribery.

False and inflated expenses submitted by a travel agency

In an investigation of questionable event-related expenses submitted by a travel agency, although the event did occur, we noted falsified taxi expenses and inflated airfares.

- Taxi fapiaos include details such as the taxi company name, license plate number, the time, duration and the miles of the trip. Based on the reasonableness analysis performed, we attempted to verify the taxi fapiaos and found a majority of the taxi fapiaos showed the same license plate number, which indicated that it was issued by the same taxi for two consecutive days. Some of the transportation time appeared to be unreasonable (e.g., 30 minutes for 100 miles) and some of the taxi fapiaos shared overlapping travel times. Our further investigation revealed the taxi fapiaos were bought from the local black market, and the "transportation expense" was actually payments to physicians to influence their purchases.
- We reviewed flight itinerary details and noted one of the attendees had trips from two different cities to the same destination on the same day around the same time. We further verified the ticket details on the airline Web site and found out this ticket was invalid, and the prices of those valid airfares were marked up in addition to the agreed-upon travel agency service charge.

Contact us

Phillip D. Ostwalt

Partner

T: 404-222-3327

E: postwalt@kpmg.com

Samantha Hsu

Director

T: 214-840-2384

E: sjhsu@kpmg.com

kpmg.com/socialmedia



The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

© 2016 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. The KPMG name and logo are registered trademarks or trademarks of KPMG International. NDPPS 544110