

COUNCIL ON ETHICS

THE GOVERNMENT PENSION FUND GLOBAL

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Recommendation to exclude ZTE Corp. from the
Government Pension Fund Global

Summary

The Council on Ethics recommends the exclusion of ZTE Corporation (ZTE)¹ from the Government Pension Fund Global (GPF) due to an unacceptable risk of gross corruption. In its assessment, the Council has emphasised the company's involvement in corruption allegations in 18 countries, of which 10 cases are alleged to have been investigated. Weight has also been given to the fact that the company has been convicted of corruption in one instance, that a corporate penalty was imposed and that the company has been temporarily barred from public competitive tenders. The Council has concluded that the company has failed to demonstrate satisfactorily that internal anti-corruption procedures are being effectively implemented in its business. In conjunction with previous corruption cases and the fact that the company operates in a sector and in many countries associated with a high risk of corruption, this finding indicates that there is an unacceptable risk that the company may once again become involved in gross corruption.

About the company

ZTE is one of the world's five largest producers of telecommunications equipment and network solutions. The company was listed on the Shenzhen Stock Exchange in 1997 and in Hong Kong in 2004. As of 2014, the company had more than 75,000 employees spread across 100 subsidiaries, and operations in 160 countries. At the end of 2014, the GPF owned shares in ZTE valued at approximately NOK 85 million, corresponding to an ownership interest of 0.15 %.

What the Council has considered

The Council on Ethics has assessed whether there is an unacceptable risk of ZTE being responsible for gross corruption contrary to section 3, d) of the Guidelines for Observation and Exclusion of Companies from the Government Pension Fund Global.

The Council has examined ZTE's response to current corruption allegations against it, including whether the company's anti-corruption measures sufficiently reduce the risk of the company becoming involved in similar practices in future.

The Council's findings

ZTE and its representatives have been linked to corruption allegations in 18 countries, and the Council on Ethics is aware that formal investigations into corruption on the part of the company have been launched in 10 different countries. The incidents in question cover a period of 17 years, from the year after ZTE was listed until 2014.

The Council has commissioned three studies by consultants into the corruption allegations against ZTE referred to in the media. The Council has also contacted, among others, public investigatory and prosecutorial bodies to obtain public information on the particular instances of corruption. The Council has also been in dialogue with ZTE in 2014 and 2015. ZTE has been sent a draft of the recommendation, but has not commented on it.

All corruption allegations against ZTE of which the Council is aware relate to the payment of bribes to public officials to secure the award of contracts. In 2012, ZTE's representative in Algeria was sentenced to 10 years' imprisonment for corruption in connection with a contract won by ZTE in the country. A corporate penalty was imposed on the company, and it was

¹ The company has Issuer ID 304299.

barred from participating in public competitive tenders for two years. In Zambia, the national anti-corruption commission decided in 2014 that corruption had occurred in connection with a contract between ZTE and government ministers. In Kenya, a contract was cancelled by a public body in 2012 due to overpricing, a decision which was upheld by an appellate court in 2014.

Not all of the corruption cases involving ZTE have been concluded. In the spring of 2015, a criminal trial began in Singapore against persons who in police interviews have admitted passing large commission payments to the [REDACTED] and other public officials on Papua New Guinea on behalf of ZTE. The Council on Ethics is also aware that a corruption investigation has recently been opened in Malaysia.

Serious corruption allegations have also been made against the company in the Philippines, Myanmar, Nigeria and Liberia. As far as the Council is aware, ZTE has not responded to any of the allegations made against it. The available information indicates that ZTE, either directly or through its representatives, has paid bribes to public officials with the aim of securing public contracts. The large numbers of allegations in many different countries indicate that the company makes systematic use of corruption in its business. Further, the size of the amounts suggests that ZTE's management knew, or should have known, about the payments. In all of the cases which remain under investigation, the suspected bribes amount to several million US dollars and in some cases many tens of millions of US dollars.

ZTE operates in many countries in which the risk of corruption is high. The telecommunications industry, in which large public contracts are commonplace, also exposes the company to significant risk. In the Council's view, this places a particular requirement on the company to adopt robust systems and measures to prevent corruption. The significant number of corruption allegations against the company strengthens this requirement further.

ZTE has an internal compliance programme. The compliance programme covers not only anti-corruption, but also many other topics related to laws and regulations relevant to the company.

According to the company's ethical guidelines, which are enshrined in its Code of Conduct, no-one may pay or accept bribes in China or abroad. This applies throughout the ZTE group, and to both private and public contracts. The company has procedures for reporting and approving gifts, as well as due diligence procedures for the use of third parties. The company also has training and whistleblowing systems in place, such as an internal hotline and an email address to which all staff can report breaches. A compliance team also carries out regular inspections to uncover violations of the Code of Conduct.

Despite of this, based on information available, the Council cannot see that ZTE's anti-corruption systems include the elements that can reasonably be expected. The systems appear deficient especially because it is unclear what risk identification and assessment the company has carried out when establishing and improving them. It is also unclear what risk assessments the company performs with regard to partners, sales consultants and third parties, among others. Such risk identification is an essential prerequisite for the introduction of robust, targeted measures. It lays the foundation for, and facilitates continual adjustment and improvement of, the entire company's anti-corruption systems.

It is also unclear what consequences employees face if they breach laws and internal guidelines. Moreover, it is unclear how the company ensures the independence of its compliance staff, and how anti-corruption procedures are monitored and improved.

As recently as 2013, the company has stated that new measures were implemented to prevent corruption. However, it is unclear which measures are new and how effective they will be in

reducing the future risk of corruption. The Council notes that the investigation into the company concerning corruption in Malaysia was launched after this date, and that the contract in Kenya which may have involved corruption was concluded the same year as the new measures apparently were implemented.

The Council has also concluded that the extensive anti-corruption measures implemented in China recently have the potential to play an important role in preventing corruption in Chinese companies. The Council's conclusion that ZTE should nonetheless be excluded from the GPFG rests on the Council's decision to give greater weight to the known instances of corruption and the company's response to these. The Council has also placed particular emphasis on the company's efforts to prevent corruption, given the corruption risk in the telecommunications industry and in many of the countries in which the company operates.

Based on the available information, the Council on Ethics considers that there is an unacceptable risk that ZTE has been involved in gross corruption and that the company may again become involved in similar practices in future. The Council therefore recommends the exclusion of ZTE from the GPFG.

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1 Introduction

ZTE is one of the world's five largest producers of telecommunications equipment and network solutions.² The company, which was established in 1985, was originally named Zhongxing Semiconductor Co., Ltd. ZTE's headquarters are located in Shenzhen, and it was listed on the Shenzhen Stock Exchange in 1997 and in Hong Kong in 2004.

In 2014, the company had more than 75,000 employees³, more than 100 subsidiaries and operations in 160 countries.⁴ In 2013, the company had the following sales breakdown: China 47%, Europe/USA/Oceania 26%, Asia 18% and Africa 7%.⁵ The company has production sites in the USA, Europe and several locations in Asia. The company also operates 18 research centres in countries including China, the USA and Germany⁶, as well as 14 training centres in locations such as Turkey, Germany, Brazil, Ethiopia, Russia and Indonesia.⁷

1.1 What the Council on Ethics has considered

The corruption allegations against ZTE concern the payment of bribes to public officials in several countries to secure the award of contracts. The Council on Ethics has evaluated whether there is an unacceptable risk that ZTE may be responsible for gross corruption contrary to section 3, d) of the Guidelines for Observation and Exclusion of Companies from the Government Pension Fund Global.⁸

The Council has previously applied the following definition when assessing the term gross corruption:⁹

Gross corruption exists if a company, through its representatives,

a) gives or offers an advantage – or attempts to do so – in order to unduly influence:

- i) a public official in the performance of public duties or in decisions that may confer an advantage on the company; or*
- ii) a person in the private sector who makes decisions or exerts influence over decisions that may confer an advantage on the company,*

and

² See <http://www.reuters.com/article/2013/09/16/zte-cloud-idUSL3N0HC1IE20130916> (28 May 2015).

³ ZTE Annual Report 2014:

http://www.zte.com.cn/en/about/investor_relations/corporate_report/annual_report/201504/P020150408612617327250.pdf (28 May 2015).

⁴ See <http://www.zte.com.cn/en/about/> (28 May 2015).

⁵ See http://www.zte.com.cn/en/about/corporate_citizenship/report/201407/P020140715391031798502.pdf, page 6 (28 May 2015).

⁶ See http://www.zte.com.cn/en/about/corporate_citizenship/report/201407/P020140715391031798502.pdf, page 19 (28 May 2015).

⁷ See http://enterprise.zte.com.cn/us/support/training/zte_university/201308/t20130827_404838.html (28 May 2015).

⁸ Section 3 of the guidelines states: "Companies may be put under observation or be excluded if there is an unacceptable risk that the company contributes to or is responsible for: d) gross corruption..." The Guidelines for Observation and Exclusion of Companies from the Government Pension Fund Global can be found here: <http://etikkradet.no/en/guidelines/>.

⁹ See the Council on Ethics' recommendation to exclude the French company Alstom SA, 1 October 2010: <http://etikkradet.no/en/tilradninger-og-dokumenter/recommendations/gross-corruption/recommendation-of-december-1-2010-on-exclusion-of-the-company-alstom-sa/>

- b) the corrupt practices as mentioned under paragraph (a) are carried out in a systematic or extensive way.*

The Council has considered whether there is an unacceptable risk of ZTE's present and future involvement in gross corruption.

In its assessment of whether the corruption is gross, the Council has placed particular emphasis on the large number of corruption cases. In its assessment of the risk of corruption, the Council has given weight to corruption allegations made against the company to date and the company's response to these, the countries and industries in which ZTE operates, and the company's efforts to prevent corruption.

1.2 Sources

The primary source of information on the corruption allegations is the international press. Such press coverage often provides only general details of the corrupt practices. With the exception of the corruption cases in Papua New Guinea, the Philippines, Kenya and Liberia, it has proven impossible to obtain copies of court documents and documents from ongoing investigations. This is because the corrupt practices are being investigated and prosecuted in countries where such documents are not published. However, the Council on Ethics has commissioned two comprehensive reports by consultants on the allegations reported by the media. The Council has also contacted relevant bodies directly, including public bodies responsible for the investigation and prosecution of corruption cases, to obtain public information on the corrupt practices in which ZTE is allegedly involved.

The evaluation of the company's compliance systems is based on information published on ZTE's own website and written and oral communications between the Council and the company. The Council has also consulted experts in China to obtain general information on the anti-corruption systems of Chinese companies, including anti-corruption standards relevant for listed Chinese companies.

2 The Council's findings

The Council's findings have shown that ZTE is involved in corruption allegations in 18 countries dating from 1998 to the present day. In the following, only the most recent and most serious incidents are described. Other instances of corruption are described in brief.¹⁰

2.1 Algeria

During an investigation in Luxembourg into the circumstances surrounding the construction of a highway in Algeria, it was discovered that an Algerian businessman, [REDACTED], had opened an offshore bank account through which, among others, ZTE channelled bribes to

¹⁰ In addition to the cases discussed below relating to Algeria, Kenya, Papua New Guinea, Zambia, the Philippines, Malaysia, Burma, Nigeria and Liberia, ZTE has apparently also been involved in corruption in Ethiopia, DR Congo, Tajikistan, Kazakhstan, Kirgizstan, Mongolia, Thailand, Pakistan and India. According to the information obtained by the Council on Ethics, ZTE has also been under formal investigation for corruption in several of these countries.

██████████ a senior public official at Algérie Télécom. ZTE's subsidiary, ZTE Algérie, and another company were suspected of transferring around USD 10 million to ██████████ via a shell company registered in the British Virgin Islands.¹¹

On 6 June 2012, two ZTE executives and one executive from another company were convicted of corruption in connection with contracts awarded in Algeria between 2003 and 2006. ZTE's representatives were sentenced *in absentia* to 10 years' imprisonment and a fine of USD 65,000. Together with another company, ZTE Algérie were fined and banned from participation in public tenders in Algeria for a period of two years. ZTE was notified of the ruling in 2012, and did not wish to comment on the outcome at that time.¹² To the Council's knowledge, the ruling has not been appealed.

2.2 Kenya

ZTE is the subject of corruption allegations in Kenya connected to public contracts awarded to the company in 2009 and 2013.

In 2009, ZTE was awarded a contract from Telkom Kenya. Under the agreement, ZTE was to deliver landline-telephone surveillance equipment to Kenya's National Security Intelligence Services (NSIS). According to a report from the US Embassy in Nairobi, ZTE allegedly paid kickbacks to persons including ██████████, in connection with the contract.¹³ According to the report, ██████████ received kickbacks from the company during a visit to China.¹⁴

In 2013, ZTE was awarded a contract by the Kenyan Civil Service for the delivery of communications equipment to the Kenyan police. The contract was valued at USD 17 million. The contract was later cancelled by Francis Kimemia, head of the Kenyan Civil Service.¹⁵ The reason for the cancellation was that the contract sum represented considerable overpricing, and that the real contract value lay between USD 9 million and USD 12 million.¹⁶ In a letter to the Internal Security Ministry, Kimemia also stated that several public officials had received kickbacks to influence the award of the contract. ZTE appealed the decision to the Kenyan Public Procurement Administrative Review Board, which in November 2013 ruled that the contract was significantly overpriced.¹⁷ Although ZTE appealed against both decisions, they were upheld by the High Court of Kenya in 2014.¹⁸

¹¹ See *Trace Compendium*, ZTE Corporation, <https://www.traceinternational2.org/compendium/view.asp?id=250> (28 May 2015).

¹² See *Information Age*, 12 June 2012, <http://www.information-age.com/technology/mobile-and-networking/2107858/huawei-and-zte-execs-convicted-of-bribery-in-algeria>, *Channel News*, 8 June 2012, <http://www.zdnet.fr/actualites/huawei-et-zte-condamnes-pour-corruption-en-algerie-39772672.htm>, *Trace Compendium*, ZTE Corporation, <https://www.traceinternational2.org/compendium/view.asp?id=250> (28 May 2015).

¹³ See <http://cablegatesearch.net/cable.php?id=10NAIROBI181&q=zte> (28 May 2015).

¹⁴ <http://cablegatesearch.net/cable.php?id=10NAIROBI181&q=zte> (28 May 2015).

¹⁵ See the following ruling by the appeal court in Nairobi dated 2 July 2014: *High Court of Kenya at Nairobi, Judicial Review Case No. 441 of 2013*.

¹⁶ *Business Daily*, 19 February 2013, available at <http://www.businessdailyafrica.com/Kimemia-cancels-exaggerated-police-equipment-tender/-/539546/1699146/-/qt0qcf/-/index.html> (28 May 2015).

¹⁷ Parts of the ruling have been reproduced in an article in *Business Daily Africa*: "The board has already stated why the applicant's bid was not successful and adds that it was against the promotion of the principles of integrity, fairness, transparency and accountability to award a tender where the tender price was increased by 106 per cent due to the overpricing of items", and further that "It does not require rocket science in view of the evidence before the Board to establish that (ZTE's) financial proposal was highly exaggerated"; see <http://www.businessdailyafrica.com/How-Chinese-bidder-inflated-police-radio-tender-to-Sh18bn/->

2.3 Papua New Guinea

In 2010, ZTE was awarded a contract worth USD 35 million as the main contractor on an ambitious schools project on Papua New Guinea (PNG). The purpose was to establish a virtual university network encompassing 13 schools. These schools would become part of an online educational programme connected to 89 community colleges across the country.¹⁹ [REDACTED] was the company's representative.²⁰

Singapore's Corrupt Practices Investigation Bureau has investigated circumstances surrounding the contract. It has been admitted in police statements that the parties had agreed in advance to set aside USD 3.6 million of the contract value for "commissions".

According to bank transfers, on 31 July 2010, ZTE transferred USD 3.6 million to the company Questzone Offshore Pte. Ltd. ("Questzone") via ZTE's subsidiary in Hong Kong. Questzone was established in 2010, and is registered in the British Virgin Islands.²¹ ZTE's representative had asked that the company be registered in the British Virgin Islands because such companies were "less troublesome". According to police interviews conducted in connection with the investigation into the transactions, the company was established for the purpose of receiving and distributing the commission payments to the parties. Several transfers were registered from Questzone to persons including the [REDACTED] of PNG and to a bank account in Hong Kong belonging to [REDACTED].

On 13 September 2012, the prosecuting authority in Singapore issued indictments against [REDACTED] and two persons who acted as facilitators of the agreement and the transfers.²² [REDACTED] left Singapore after An Wei, Chief Technology Officer and the person responsible for ZTE Singapore's Asia Pacific Marketing Centre, posted bail of USD 600,000 for him in July 2013.²³ The legal proceedings against [REDACTED] are ongoing.²⁴

[/539546/2096258/-/9x4ypx/-/index.html](http://539546/2096258/-/9x4ypx/-/index.html) (28 May 2015), see also *Wall Street Journal* 6 January 2014, <http://online.wsj.com/news/articles/SB10001424052702303653004579212092223818288> (28 May 2015).

¹⁸ *High Court of Kenya at Nairobi, Judicial Review Case No. 441 of 2013*. It should be noted that the high court ruling did not examine whether or not bribes were paid in connection with the contract.

¹⁹ See, for example, [REDACTED] and other matters v Public Prosecutor (2013) SGHC 69 and *Statement of Thomas Philip Doherman, recorded 16 March 2011*, a witness statement given to the investigating authorities in Singapore and now forming part of the court documents in an ongoing criminal prosecution in Singapore.

²⁰ [REDACTED], who was seconded to Singapore, was [REDACTED].

²¹ [REDACTED], is listed as the company's director, see [REDACTED] and other matters v Public Prosecutor (2013) SGHC 69 <https://tinyurl.com/public-prosecutor-2013> (28 May 2015).

²² See [REDACTED] and other matters v Public Prosecutor (2013) SGHC 6, , <https://tinyurl.com/public-prosecutor-2014> and <https://tinyurl.com/public-prosecutor-2013-2> (28 May 2015). Note that, technically, the indictment does not concern corruption, but rather "falsification of documents" and "transfer of unlawful dividends". The Singaporean Prevention of Corruption Act does not apply extraterritorially, and therefore cannot be invoked against foreign nationals.

²³ See <http://www.singaporelawwatch.sg/slw/headlinesnews.html> (15 November 2014, *Today*), see also *Public Prosecutor v An Wei* (2014) SGDC 182.

²⁴ The Corrupt Practices Investigation Bureau in Singapore has asked the Chinese embassy in Singapore for information on the whereabouts of [REDACTED] and was recently advised by the embassy to send a formal request for mutual legal assistance to the Chinese authorities. Such processes can take a very long time, and it is uncertain when the criminal prosecution of [REDACTED] can be completed.

2.4 Zambia

In 2011, the Zambian government awarded ZTE a contract for the delivery and installation of surveillance cameras. Contrary to national laws, ZTE's representatives and the Zambian government concluded the contract without a public tender. The contract value was USD 210 million.²⁵

In response to subsequent allegations of corruption in connection with the contract, the Zambian government terminated the contract in September 2013.²⁶ The Zambian Anti-Corruption Commission (ACC) then investigated the allegations, and in July 2014 concluded that the corruption allegations had been substantiated. The ACC's Public Relations Manager stated that, *"The allegations of corruption were proved true by ACC in this matter but the commission has not prosecuted anyone due to legal technicalities. However, recommendations have been made to the Ministry of Home Affairs for administrative action."*²⁷

2.5 The Philippines

The most wide-ranging corruption allegation in which ZTE has been involved concerns a contract for the construction of the National Broadband Network (NBN) in the Philippines in 2007. The case has been investigated by the Office of the Ombudsmen of the Republic of the Philippines. A large amount of public information is available on the corruption allegations related to this contract, including a large number of witness statements given to the Senate of the Philippines and interviews conducted by the Office of the Ombudsmen in connection with its investigation of the matter.²⁸ The witness interviews reveal that several ZTE executives and former political leaders in the Philippines were involved. Criminal prosecutions have been brought against individuals in the Philippines, although none of these are ZTE employees.

Under the NBN contract, ZTE was to develop and install a broadband network in the Philippines. ZTE's final bid was approved by the National Economic and Development Authority Board (NEDA) in 2007. The contract had a total value of USD 333 million. The core allegation is that ZTE's bid was supported by members of the Philippines political elite, who lobbied for the company and ensured that the bid was approved without a public tender, contrary to national laws.

In response to allegations against ZTE concerning overpricing under the contract and the payment of bribes to public officials, including [REDACTED] and [REDACTED], a Senate hearing was launched at the beginning of September 2007.²⁹ On 11 September 2007, the Supreme

²⁵ See *Trace Compendium*, ZTE Corporation, <https://www.traceinternational2.org/compendium/view.asp?id=250> (28 May 2015).

²⁶ See for example *All Africa*, 11 September 2013, <http://allafrica.com/stories/201309120058.html>, *PC Advisor*, 16 July 2014, <http://www.pcadvisor.co.uk/news/enterprise/3531111/zambia-finds-corruption-in-award-of-cctv-contract-to-zte/>, *Trace Compendium*, ZTE Corporation, <https://www.traceinternational2.org/compendium/view.asp?id=250> (28 May 2015).

²⁷ See *PC Advisor*, 16 July 2014, <http://www.pcadvisor.co.uk/news/enterprise/3531111/zambia-finds-corruption-in-award-of-cctv-contract-to-zte/> (28 May 2015).

²⁸ For examples of public news articles, see *Caijin Magazine*, 19 September 2007, and *China Daily*, 20 October 2007.

²⁹ See *Senate Official Transcripts for September 2007*.

Court of the Philippines handed down an interim ruling suspending the contract, a decision set aside by [REDACTED] 11 days later. She nevertheless annulled the contract in 2008.³⁰

During an interview in 2008, [REDACTED], a ZTE engineer and the person with primary responsibility for the drafting of the contract bid, stated that half the contract sum – i.e. more than USD 150 million – was used to pay kickbacks. The money was split between the Philippine consultants who negotiated the agreement on behalf of the authorities and ZTE employees. Further, an adviser to the Philippine government, [REDACTED], stated in an interview on 8 February 2008 that a total of USD 130 million were received in bribes. Of this total, [REDACTED] and [REDACTED] were to receive approximately USD 50 million.³¹

In 2009, the corruption allegations were investigated by the Office of the Ombudsmen, which in April of that year withdrew the indictment against the [REDACTED] and [REDACTED] based on, respectively, immunity and a lack of evidence. However, a new investigation into the matter was launched in 2011, and in December of that year, [REDACTED] og [REDACTED] were indicted for corruption in connection with the ZTE contract.³² As recently as 7 February 2014, it was reported in the press that the case against [REDACTED] and [REDACTED] among others, was ongoing.³³

2.6 Other corruption allegations

Between 1998 and 2014, ZTE has been investigated for corruption in five additional countries. Since these allegations are not documented as well as those above, the Council on Ethics has given less weight to them in its assessment. Some of the allegations are nevertheless described briefly below in order to illustrate systematic use of corruption by the company.

Malaysia

In 2014, the Malaysia Anti-Corruption Commission (“MACC”) confirmed that it was investigating ZTE Malaysia and the company’s [REDACTED] for corruption.³⁴ ZTE’s [REDACTED] is alleged to have offered cash to a manager from a Malaysian telecommunications company during a business dinner. The aim was to influence the Malaysian telecommunications company’s choice of supplier of telecommunications equipment.³⁵ The incident was reported to MACC, which launched an investigation. Shortly afterwards, ZTE’s [REDACTED] left Malaysia. ZTE Malaysia has not commented on the matter.

³⁰ See for example *World Socialist Website*, 7 March 2008, <http://www.wsws.org/en/articles/2008/03/phil-m07.html> (28 May 2015).

³¹ See *Senate Official Transcripts January-February 2008*. In an interview on 18 September 2008, Jose De Venecia III stated that, in his capacity as head of Amsterdam Holdings Inc, he had submitted a bid for the NBN contract, but that he had been asked to withdraw. He stated that [REDACTED] had offered him USD 10 million in bribes to withdraw his bid, so that ZTE would remain as the sole bidder; see *Senate Official Transcripts from March 2008-September 2009*.

³² See *The Guardian*, 13 March 2012, <https://tinyurl.com/corruption-and-arrested> (28 May 2015).

³³ See <http://opinion.inquirer.net/71214/unfinished-business-3> (28 May 2015).

³⁴ See *The Malay Online*, 2 June 2014, <http://www.themalaymailonline.com/malaysia/article/macc-probes-china-company-over-cash-in-chocolate-box-gift> (28 May 2015).

³⁵ See <http://www.themalaymailonline.com/malaysia/article/macc-probes-china-company-over-cash-in-chocolate-box-gift> (28 May 2015). In 2014, the average NOK-MYR (Malaysian ringgit) exchange rate was 1.9; see <http://www.norges-bank.no/Statistikk/Valutakurser/valuta/MYR/> (28 May 2015).

Myanmar

ZTE is involved in two corruption allegations in Myanmar. The first allegation was formally investigated in 2005, and the second in 2013.

The 2005 case concerned a contract between ZTE and Myanmar's former [REDACTED]. An investigation was launched because it was suspected that ZTE had paid large kickbacks to public officials, including [REDACTED], in connection with the contract. The contract was allegedly overpriced ten times compared to the actual market price.³⁶ The Council on Ethics is not familiar with the outcome of this investigation.

In 2013, more than 60 public officials at the Myanmar Ministry of Posts and Telecommunications were investigated for corruption in connection with the award of public telecoms contracts. ZTE is believed to be one of the companies involved in this investigation.³⁷ The Council has no information on when this investigation will be completed.

Nigeria

In the period 2003–2011, a number of allegations were made in the press to the effect that ZTE was paying bribes in Nigeria. In 2003, a contract between ZTE and Nigerian Telecommunications Limited (NITEL) was annulled based on suspicions of corruption.³⁸ In 2011, the Supreme Court of Nigeria ordered the Economic and Financial Crimes Commission (EFCC) to investigate the award to ZTE of a contract for the delivery of surveillance cameras which was valued at USD 470 million.³⁹ At around the same time, it was announced that the House of Representatives would also investigate the contract.⁴⁰ The Council on Ethics has no information on the outcome of these investigations.

Liberia

In 2006, ZTE was charged in Liberia with offering bribes to employees of the state-owned Liberian Telecoms Corporation (LTC, now LIBTELCO). The bribes were allegedly paid to secure a contract awarded by the National Transitional Government (NTG) in 2004.⁴¹ Several former LTC executives were charged with corruption in connection with the case. According to the indictment, ZTE offered bribes to public officials in Liberia to secure the award of the contract.⁴²

In 2006, when Ellen Johnson-Sirleaf became president, all contracts awarded by the NTG, including the contract with ZTE, were investigated. However, the investigation did not result

³⁶ See *BurmaNet*, 22 February 2005, <http://www.burmanet.org/news/2005/02/22/south-china-morning-post-deposed-pms-allies-face-sentencing-more-than-300-myanmar-officers-set-to-receive-jail-terms-this-week-as-disquiet-grows-in-the-military-larry-jagan/> (available until December 2014).

³⁷ See http://www.atimes.com/atimes/Southeast_Asia/SEA-01-050413.html (28 May 2015).

³⁸ According to a confidential report sent by the US Embassy in Abuja, the contract with ZTE was annulled by the Nigerian government. Stephen Oronsaye, former head of the Civil Service of the Federation (2009–2010), apparently acknowledged to the US ambassador that, “*NITEL and Communications Ministry officials had brokered side-deals favouring certain telecom companies*”.

³⁹ See *Trace Compendium*, ZTE, <https://www.traceinternational2.org/compendium/view.asp?id=250> (28 May 2015).

⁴⁰ See <http://allafrica.com/stories/201112020588.html> (no longer available).

⁴¹ See the article in *All Africa* of 17 February 2006, <http://allafrica.com/stories/200602170655.html>, which also refers to an article in the *Liberian Observer* of the same date (28 May 2015).

⁴² Item b) in the indictment stated that, “*ZTE Corporation offered bribes to the Inviter of the bid by offering to give LTC Free equipments in an efforts to kick out UTE, thereby interfering with UTE legitimate contract...*”, see also <http://allafrica.com/stories/200602170655.html> (28 May 2015).

in the annulment of the contract. According to public officials involved in the investigation, the reason was that ZTE had already invested in equipment and infrastructure, and thus already partly fulfilled the contract.

3 Anti-corruption standards

Some general principles to guide a company's efforts to establish and implement an effective anti-corruption programme can be derived from international standards for corporate anti-corruption work. Internal anti-corruption procedures are relevant in the assessment of company's ability to avoid involvement in corruption.

The UN anti-corruption portal TRACK (*Tools and Resources for Anti-Corruption Knowledge*), Global Compact: *A guide for anti-corruption risk-assessment* (2013), and the OECD's *Good Practice Guidance on Internal Controls, Ethics and Compliance* (2010), provide useful guidance in these matters. In *Business Principles for Countering Bribery*, Transparency International (TI) has listed a number of general recommendations for building robust compliance systems.

In the context of the present case, the most relevant elements in international standards for corporate anti-corruption systems are focused corruption-risk identification and assessment and the application of a zero tolerance corruption policy.

A prerequisite for the establishment and implementation of robust anti-corruption systems is thorough survey and evaluation of a company's corruption risk. Important risk factors that have to be assessed include the company's size, local and regional conditions, and the sector in which the company operates. As a minimum, the company must have strong preventive mechanisms in place in the areas presenting the greatest risks to the company. Large companies should undertake regular risk identification and assessment, and particularly exposed areas should be monitored continuously. Risk identification should also cover the design of the company's internal procedures, training programmes for employees, and third-party due diligence. A clear procedure for reporting breaches of company guidelines must be established, and it must be communicated clearly how individuals breaking internal guidelines are sanctioned.

It is crucial that anti-corruption procedures are implemented in the business, that these are monitored, developed further and constantly improved and made more effective. Anti-corruption procedures should be monitored by an independent body, and be evaluated and improved regularly based on, for example, internal experience and external factors like new laws and regulations.⁴³

⁴³ The UN anti-corruption portal TRACK (*Tools and Resources for Anti-Corruption Knowledge*) is available at <http://www.track.unodc.org/Pages/home.aspx>, Global Compact: *A guide for anti-corruption risk-assessment* (2013) is available at <https://www.unglobalcompact.org/resources/411>, and the OECD's *Good Practice Guidance on Internal Controls, Ethics and Compliance* (2010) is available at <http://www.oecd.org/investment/anti-bribery/anti-briberyconvention/44884389.pdf>. TI's recommendations were first launched in 2003, and then revised in 2009 and, most recently, 2013. The recommendations are available at http://www.transparency.org/whatwedo/publication/business_principles_for_countering_bribery. General anti-corruption principles are also found in *The OECD Guidelines for Multinational Enterprises*, <http://www.oecd.org/daf/inv/mne/48004323.pdf>. The UK Bribery Act and the Foreign Corrupt Practices Act (FCPA) have also influenced international standards for corporate anti-corruption efforts. In 2011, the UK Ministry of Justice published guidelines on what arrangements companies should make to avoid criminal liability under the UK Bribery Act. The guidelines are available at <http://www.justice.gov.uk/downloads/legislation/bribery-act-2010-guidance.pdf>. In 2012, the US Department

ZTE is listed in China. In recent years, Chinese authorities have intensified their anti-corruption efforts. An offensive anti-corruption campaign has been launched to combat corruption, primarily in state bodies, and it is pledged that the campaign will target both “tigers and flies”. The prohibition against corruption is enshrined in several laws. The most important provisions are found in the PRC Criminal Law – for example Article 393 on corporate penalties – the PRC Company Law and the Rules Governing the Listing of Stocks on the Shanghai and Shenzhen Stock Exchange – which are intended to clarify various anti-corruption regulations in the PRC Company Law – and the PRC Bidding Law.⁴⁴

According to the information gathered by the Council on Ethics on Chinese anti-corruption standards, companies are expected to have an explicit zero tolerance attitude towards corruption, to give their staff compliance and anti-corruption training and to have whistleblowing systems for the reporting of potential breaches of internal laws and regulations. Many companies have established an advisory council or group of experts to advise on the operational implementation of anti-corruption procedures.

4 Information from ZTE

4.1 The Council’s contact with ZTE

In May 2014, the Council sent a letter to ZTE asking the company to comment on corruption allegations which had come to the Council’s attention. The company was also asked to describe its internal anti-corruption and compliance systems, and to provide a detailed account of its anti-corruption systems in the countries in which corruption investigations have been launched against it.

In September, the Council had a telephone meeting with an employee from ZTE’s Security & Investor Relations Department and an employee from the company’s legal department. The company also subsequently replied to an email containing follow-up questions. In its replies,

of Justice (DoJ) and the US Securities and Exchange Commission (SEC) published guidelines on what arrangements companies should make to avoid criminal liability under the FCPA. These are called *A Resource Guide to the U.S. Foreign Corrupt Practices Act*, and are available at <http://www.justice.gov/criminal/fraud/fcpa/guide.pdf>. The guidelines also refer to other relevant guidelines, such as *Business Ethics: A Manual for Managing a Responsible Business Enterprise in Emerging Market Economies*, published by the Department of Commerce, International Trade Administration, and available at http://ita.doc.gov/goodgovernance/business_ethics/manual.asp. Other relevant sources for international anti-corruption standards include the United Nations Global Compact (*Ten Principles*), the Asia-Pacific Economic Council (*Anti-Corruption Code of Conduct for Business*), the International Chamber of Commerce (*ICC Rules on Combating Corruption*), the World Bank (*Integrity Compliance Guidelines*), and the World Economic Forum (*Partnering Against Corruption-Principles for Countering Bribery*).

⁴⁴ Key guidelines can be found in the document *Interpretations issued by the Supreme People’s Court, the Supreme People’s Procuratorate, or the State Administration for Industry and Commerce*. According to the Rules Governing the Listing of Stocks on the Shanghai and Shenzhen Stock Exchange, listed companies must publish, within a reasonable period of time, all legal breaches committed by directors, advisers and senior employees. The PRC Bidding Law states that all major public contracts must be awarded following a preceding competitive tender, and that the payment of bribes in return for the award of contracts is prohibited; see Article 32. Breaches that qualify as criminal offences must be prosecuted in accordance with the penal code; see Article 53. On 25 December 2013, the General Office of the CPC Central Committee put forward its Plan for Establishing and Improving the Work of Punishing and Preventing Corruption (2013–2017) (“2013–2017 Work Plan”) to strengthen party organisations at all levels, to establish internal anti-corruption systems and to strengthen compliance.

the company did not comment on any of the specific corruption allegations, discussing only its internal compliance and anti-corruption systems.

On 9 February 2015, ZTE was sent a draft of the recommendation for comment. In response to a further enquiry by the Council, ZTE replied by email on 2 March, stating that it wished to submit its comments before the recommendation was sent to Norges Bank. In an email of 10 March, ZTE asked for the submission deadline to be extended until 13 March. On 20 March, not having received a reply, the Council sent the company an email asking it to submit its comments by 28 March 2015. The same date, ZTE replied in an email that it believed it would be able to reply within two weeks. The Council has not received the company's comments.

4.2 ZTE's anti-corruption procedures

The information which has been available on ZTE's internal anti-corruption procedures is largely based on the information provided to the Council during the telephone meeting in September 2014 and in the subsequent email. The Council has also obtained some information from ZTE's website and its CSR reports for 2013 and 2014.

ZTE has an internal compliance programme. The compliance programme covers not only corruption, but also many other topics related to laws and regulations relevant to the company. Until 2013, ZTE had a separate anti-corruption programme, but in that year all corporate compliance issues were amalgamated into the compliance programme.⁴⁵

According to the company's ethical guidelines, which are summed up in its Code of Conduct, no-one may pay or accept bribes in China or abroad. This applies throughout the ZTE group, and to both private and public contracts.⁴⁶ The company has procedures for reporting and approving gifts, as well as due diligence procedures for the use of third parties.⁴⁷ Staff are also given oral training in compliance.⁴⁸ In 2013, an online training programme was launched.⁴⁹

In its email to the Council, ZTE also explained that the company has whistleblowing systems in place, such as an internal hotline and an email address to which all staff can report breaches. The compliance team also carries out regular inspections to uncover breaches of the rules. The Council has been informed that, in the past two years, reports have been received on matters such as breach of the Data Protection Act and "*non-compliance of the internal compliance regulation*".⁵⁰

⁴⁵ Pages 45–46 of the company's CSR report for 2013 suggests that the company established an entirely new anti-corruption system in 2013. During the telephone meeting on 18 September 2014, however, it was explained to the Council on Ethics that this was incorrect, and that the entire compliance system had been restructured and streamlined in 2013. The 2013 CSR report is available at http://www.zte.com.cn/en/about/corporate_citizenship/report/201407/P020140715391031798502.pdf (28 May 2015).

⁴⁶ Email to the Council on Ethics from ZTE dated 11 October 2014.

⁴⁷ Email to the Council on Ethics from ZTE dated 11 October 2014. The Council has not had access to the *Global Anti-corruption and Anti-bribery Policy and Compliance Guidance*, nor to any of the other routines and procedures.

⁴⁸ This is apparent from the attachments to ZTE's email to the Council dated 11 October 2014.

⁴⁹ Email to the Council on Ethics from ZTE dated 11 October 2014. The Council has not seen the compliance commitment letter or examples of country-specific guidelines.

⁵⁰ Email to the Council on Ethics from ZTE dated 11 October 2014. According to the email, ZTE currently has 19 Compliance Directors and 306 Compliance Managers working on compliance issues part-time, in addition to 15 full-time Compliance Specialists. The Compliance Specialists have overall responsibility for promoting, advising on, implementing and monitoring compliance procedures. The Compliance Managers are responsible

5 The Council on Ethics' assessment

Based on the available documentation, the Council on Ethics has assessed whether ZTE should be excluded on the basis of the corruption criterion in the ethical guidelines for the GPFPG.

Firstly, the Council assesses whether there was an unacceptable risk of the company being involved in practices which constitute gross corruption under the guidelines, including whether the corruption has been carried out in an extensively and/or systematic way.

Given that corruption allegations have been made against ZTE in 18 countries since 1998, of which 10 cases have been investigated and one has resulted in conviction and exclusion from public competitive tenders, it appears that ZTE may be responsible for practices that must be deemed to constitute gross corruption. In all of the cases investigated by the Council, ZTE appears to have paid bribes to public officials – either directly or via its representatives – with the aim of securing public contracts. In several cases, ZTE appears to have orchestrated the corruption by overpricing contract and then using the difference between the agreed and actual contract values to fund the bribes.

In addition to the large number of corruption cases in which ZTE appears to have been involved, the Council has emphasised that corruption allegations have been made in numerous different countries. Moreover, the allegations cover a period of many years, stretching from just after ZTE's formation in the late 1990s to 2014. Further, in the cases on which the Council has information, the size of the amounts involved indicates that ZTE executives must, or should have, known about the corrupt practices.

Secondly, the Council has assessed whether there is an unacceptable risk that the company may again become involved in similar practices.

In recent years, the Chinese authorities have intensified their anti-corruption efforts. An offensive anti-corruption campaign has been launched to combat corruption, primarily in state bodies. A prohibition on the payment of bribes abroad has also been enshrined in law. Viewed in isolation, these measures may lead to a reduction in the risk of extensive and/or systematic corruption in companies like ZTE. However, the ongoing anti-corruption campaign is focused primarily on Chinese state bodies. ZTE is a private enterprise, and the practices of which it is accused relate to corruption in its foreign operations. The conclusion in this recommendation that there is an unacceptable risk that ZTE may again become involved in similar practices is due to the Council's decision to give greater weight to the corruption risk in the company's industry, to how the company has responded to discovered instances of corruption in the company and to the steps the company has taken to reduce corruption risk.

ZTE operates in many countries associated with a high corruption risk. Even though the risk of corruption in the sector may be reduced due to the measures implemented by the authorities, the company operates in many other countries presenting a considerable risk of corruption. The telecommunications industry, in which large public contracts are commonplace, also exposes the company to corruption risk. In the Council's view, this places a particular requirement on the company to adopt robust systems and measures to prevent corruption. The significant number of corruption allegations against the company strengthens this requirement further.

for reporting breaches of compliance rules to the Compliance Directors, and for training their departments. Responsibility for internal controls and auditing lies with the Legal & Compliance Management Department and the Internal Control & Audit Department.

ZTE provides little information on its anti-corruption efforts. In its communication with the Council, the company failed to provide satisfactory answers on how it seeks to prevent corruption. It is unclear what risk identification and assessment the company has carried out when establishing its systems. It is also unclear what risk assessments the company performs with regard to partners, sales consultants and third parties, among others. Such risk identification and assessment is an essential prerequisite for the introduction of robust, targeted measures. It lays the foundation for, and facilitates continual adjustment and improvement of, the entire company's anti-corruption systems. The specific corruption allegations against ZTE indicate that extensive risk identification and assessment are absolutely vital if the company is to run its business so as to avoid future involvement in similar incidents.

It is also unclear what consequences employees face if they breach laws and internal guidelines. For example, a company representative posted bail for ZTE's [REDACTED] for Papua New Guinea when a formal investigation into his activities was launched in Singapore. As far the Council is aware, the company has not commented publicly either on this incident or on any of the other corruption allegations. When company executives clearly signal that corruption is unacceptable, this is an important preventive measure. Strategies and guidelines are in themselves insufficient to communicate this. Anti-corruption efforts will only be effective if executives communicate clearly that corruption is unacceptable, both by helping to clear up instances of corruption and by showing that corruption has consequences for company representatives.

It is also unclear how the company ensures the independence of its compliance staff, and how anti-corruption procedures are monitored and improved.

Accordingly, the Council cannot see that ZTE's anti-corruption systems include the elements that can reasonably be expected. Nor do they appear to be adequately implemented.

In its replies to the Council, as well as on its website, ZTE has stated that it has implemented new measures to prevent corruption as recently as in 2013. However, it is unclear which measures are new and how effective they will be in preventing new incidents. The corruption allegations currently under investigation in Malaysia apparently took place in 2014, and the contract in Kenya which may have involved corruption was concluded the same year as the new measures were apparently implemented. The latest corruption allegations, and the fact that ZTE is so reticent about providing the Council with information, do not induce confidence that the company will address its challenges in a manner that reduces the risk of reoccurrence.

Based on available information, the Council on Ethics considers that there is an unacceptable risk that ZTE has been involved in gross corruption and that the company may again become involved in similar practices.

6 Recommendation

The Council on Ethics recommends the exclusion of ZTE Corporation from the Government Pension Fund Global due to an unacceptable risk that the company is responsible for gross corruption.

Johan H. Andresen
Chair

(Signature)

Hans Chr. Bugge

(Signature)

Cecilie Hellestveit

(Signature)

Arthur Sletteberg

(Signature)

Guro Slettemark

(Signature)