



Fraud and white-collar crime: a Chinese perspective

Fraud and
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crime

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Abstract

Purpose – This paper sets out to discuss white-collar crime and fraud in China and to draw implications for Western businesses wishing to enter the Chinese market.

Design/methodology/approach – The paper provides examples of recent frauds committed in China and also provides a brief review of the literature. It traces the development of China's economy, describing China's modern-day economy, and also looks at cultural issues and differences between Western and Chinese attitudes.

Findings – Western businesses planning to enter the Chinese market need to do their due diligence before committing resources. What works in Western society may not work in another culture, like China's. However, gaining an understanding of the culture and general way of life will go a long way towards laying the groundwork for success.

Research limitations/implications – Additional focus should be placed on examining how cultural differences affect judgments and behaviors.

Originality/value – From a practical standpoint, the paper provides insights into possible areas of disagreement between employees from different cultures that can result from their divergent opinions about individuals' responsibility for fraudulent acts.

Keywords Fraud, Corruption, China

Paper type General review

Introduction

One of the most influential criminologists in the twentieth century was sociologist Edwin Sutherland. In his 1949 monograph, *White-Collar Crime*, Dr Sutherland defined white-collar crime "approximately as a crime committed by a person of respectability and high social status in the course of his occupation" (p. 9). While many of the high profile white-collar crimes in the USA (e.g. Enron, WorldCom, Adelphia) were committed by individuals that fit this definition, others were perpetrated by average citizens (e.g. clerks, petty criminals, bookkeepers). For example, crimes like identity theft, check fraud and embezzlement are often committed by those trying to make a living or others trying to climb the social ladder.

The situation in China, while similar in some ways, is different in many others. Although China has been moving from a state-controlled economic system to a market-oriented economy since late 1979, the business world in China is not independent of political and governmental control. The Communist Party and government still wield a great deal of power in the business world, and it is this power that often creates an opportunity for party and/or government officials to engage in behavior that benefits them or their families (Zhang, 2001). Thus, more common forms of white-collar crime in China involve bribery and corruption.

Zhou and Cong (2001) define occupational fraud as part of white-collar crime that "refers to an act whereby the individual illegally uses his or her position for personal



benefit” (p. 59). These types of crimes “did not become a national disease until the economic reform and open door policy were implemented in the early 1980s” (Zhang, 2001, p. 26). As stated by Rojek (2001, p. 101), “Corruption and the acquisition of wealth are rife at all levels of the Chinese government. It is ironic that China had been the paragon of a society that was nearly crime-free and highly interdependent, but is rapidly becoming wracked with materialism and crime”.

Zhang (2001) provides examples of bribery and corruption on both an individual basis and organizational level. He argues that Chinese officials believe that the chance of getting caught is quite remote and that this is true because:

- the political culture leaves a great deal of room for the abuse of power;
- even if caught, any penalty or punishment would influence the “face” of the government and damage official authority; and
- bribery and corruption are seen to be common practice and that punishment of a corrupt official simply implies that the individual has “bad luck”.

Beyond this, it is thought that there is social privilege attached to having official social standing. Thus, as the transformation to a market economy has taken place, individual interests are starting to replace the collectivist tradition that previously existed. Zhang states (p. 30) that “the interesting phenomenon is that the nation is lifting old social constraints, the economic transition is producing opportunities, and the motivation (getting rich) is strongly socialized for committing corruption”.

The development of China’s economy

To fully understand the climate in which white-collar crime takes place, it is necessary to have a general understanding of China’s history. In 1949, the People’s Republic of China (PRC) was established by Mao Zedong and the Chinese Communist Party (CCP) in Beijing. The Communist Party took control at a low point in China’s history; the country had been plagued by war and social conflict for many years. The economy was struggling and, as a result, inflation was high. The governing party’s solution was a version of the Soviet Union’s political and economic order. Throughout the 1950s, the Chinese government worked diligently to improve the country’s economic and social status. The CCP, under the direction of Mao, gained popularity when inflation improved and the economy was restored. Something critical to the current business makeup of China occurred during this time. The authority of the CCP grew and expanded into many aspects of Chinese life, including business.

In 1958, Mao announced a new economic plan called the “Great Leap Forward”. The purpose of the plan was to rapidly raise industrial and agricultural production through giant communes and “backyard factories”. However, Mao’s plan proved disastrous, and the economy and people of China were devastated. From the time of the “Great Leap Forward” to the time of Mao’s death in 1976, the CCP faced frequent opposition and cries for reform. Mao’s death presented new opportunities for China. The leadership that followed him made many changes that continue to impact China’s current place in the global market. In 1978, the government leaders instituted new economic reform policies, specifically aimed at expanding rural income and incentives, encouraging widespread experiments in enterprise autonomy, reducing central planning and attracting foreign investment into the Chinese economy. Although the late 1980s saw high inflation, the 1990s were a time of great emphasis on success in

business. During this time, China began working to create a socialist market economy that attempted to maintain the political system but integrate reform of the economic system.

Although China has made many changes since Mao passed away in 1976, it is still a Communist country, which means the government and the CCP are still heavily involved in many aspects of Chinese life. Pei (2006) reports that for 2003, the state directly accounted for 38 percent of the country's GDP and employed 85 million people (about one third of the urban workforce). He also references a report from the financial UBS indicating that China's private sector accounts for no more than 30 percent of the economy. Pei believes that these numbers do not show the full extent to which the government is actually involved in Chinese business and that the state is a monopolist or a dominant player in the most important sectors of the Chinese economy. He states that only 40 private firms exist among the 1,520 Chinese companies listed on domestic and foreign exchanges and that 81 percent of the chief executives of state-owned enterprises are appointed directly by the Communist Party and 56 percent of all senior corporate executives are appointed by the Communist Party in China. Thus, even though the 1990s were a time for restructuring the business landscape in China, the government still maintains a great deal of control and it appears that the control of the Communist Party in China's business sector will continue for some time.

The modern day Chinese economy

China's economy has been a hot topic for many years now. Much of the excitement surrounding the economy is due to the fact that it is one of the largest economies in the world and has grown at a rate of over 8 percent for three years in a row (Robertson *et al.*, 2008). China has a massive manufacturing workforce of over 100 million people and, as a result, labor is cheap, especially when compared to the average compensation of production workers in the USA and of many developed countries of the world (Banister, 2005). The availability of cheap labor excites many businesspeople who want to take advantage of the situation in China.

In addition, established infrastructures, preferential policies and a gigantic potential market in terms of land area, population and gross domestic product (GDP), also entice foreign investment to enter the Chinese market. These factors, along with CCP's constant commitment to the open-door economic reform policy, constitute the positive perception through which foreign companies believe that they can distribute large quantities of goods while benefiting from significant economies of scale. It is also why many of the world's largest companies have determined that China is and will continue to be a major part of their long-term global plans and strategies.

However, it is easy to get lost in the advantages of doing business in China and overlook the complications. In his book, *Doing Business in China: How to Profit in the World's Fastest Growing Market*, Plafker (2007) warns that "just like the kick of the fiery grain liquor offered at any Chinese banquet", the realities of doing business in China "can sneak up on you and knock you for a loop, leaving you with nothing but a nasty headache, a fuzzy collection of bad memories, and some gut-wrenching questions about where all your money went" (p. 5). As such, it is necessary to understand the philosophical underpinnings of Chinese society and the differences between China and its Western counterparts.

Cultural issues

It is quite challenging to directly compare Western and Chinese societies and philosophies. Yet, in general, the ethical system in China can basically help mirror the noticeable dissimilarities between these two civilizations. China is not a country that is devoid of morals. Their beliefs and approaches are *different*, and that has driven many Western businesspeople to assume that they are “wrong”. This isn’t necessarily the case. Although their system of ethics seems to be opposite of the ethics in America, they in fact do have a set of ethics worth exploring. To understand Chinese ethical principles, one must have a basic understanding of the ideas behind Confucianism.

Confucianism is a scholarly tradition and lifestyle based on the teachings of Confucius, a Chinese sage and philosopher who lived during the sixth and fifth centuries BC. Although his ideals were never organized into a religion, they have been followed by the Chinese for over two millennia. Despite the mushrooming introduction of Western management ideas, products, and technologies in today’s China, which is emerging as one of the most important economies in this globe, the inception of Western influence has been re-morphed by the deeply rooted socio-cultural context that is still bounded by the Confucian belief. Given that Confucian thought emphasizes that man is inner-directed, searching for *jen* (humanity), there is little need for formal, external law when Confucianism is followed (Rojek, 2001).

While US and Western societies are built on Plato’s philosophy, which stresses individualism, equity, and democracy, China, a historically collectivist society, is built on Confucius’s five Cardinal Relationships, emphasizing hierarchical social order and authoritarianism. This stark cultural contract reveals that Chinese people are socially oriented and situation-centered and that they more likely tend to follow orders or doctrine from their leaders. Notwithstanding the riot of Cultural Revolution, the social and moral structures of Confucianism still have retained and guided Chinese people to conform to the dominance of the CCP. Notwithstanding the exceptional economic development, spiritual erosion by Western insights and beliefs, which are considered exotic and nontraditional, is yet to be tolerated in China.

Even though Chinese society has undergone enormous change over the past three decades, traditional socio-cultural values have continued to influence the Chinese people’s societal behavior. The long history of collectivism has continuously shaped Chinese people in such a way that they tend to prioritize the needs of the group (i.e. family, work associates, or friends) over the individual. As such, when compared with Westerners, Chinese members of the group are more concerned about the welfare of the group than the needs of outsiders. Unlike Western societies, such as the USA, which value self-expression and trust, Chinese societies value trust inside the family and deem that self-expression in front of others confronts entrenched behaviors and beliefs and causes societal tension and conflict.

The ethical ideas taught by Confucius have had a major impact on China’s moral fabric and these ideas are still seen today in Chinese business. For example, Confucianism focuses not only on the advancement and wellbeing of the individual, but also on the harmony of the state and society. Western beliefs stress that human beings have individual rights to seek truth and personal privacy and property, whereas Chinese beliefs tend to emphasize social harmony and balance and are comparatively relationship-oriented for virtue. Therefore, a Chinese manager will likely judge what an employee does based on whether or not his motivations were appropriate and what his

intent was in relation to Confucius's moral principles. As Hu Jintao, the current Chinese President, calls for the establishment of social harmony and synchronization, Chinese people, when compared with Westerners, tend not to alter their external environment and instead focus on adapting to their current surroundings because they believe that all things are interdependent and exist for peace.

Confucianism advocates ethical normality, which means that men and women should practice moral excellence correctly within the confines of an ethical code. In China, this ethical code is defined in the interpersonal relationship environment referred to as *guanxi* (Leung, 2004). Chinese society is built upon the so-called Chinese term *guanxi* (interpersonal connections and networks) and Chinese people prefer to utilize *guanxi* to seek business possibilities in their social hierarchy. *Guanxi*, regarded as the lifeblood of personal relationships and business conduct in Chinese society, may be one of the most important words a businessperson can learn before entering China. However, it is difficult, if not impossible, to simply translate *guanxi* into an English word.

Burton and Stewart (2008) explain that *guanxi* is "a complex cultural system of personal relationships – and moral obligations – which most Chinese see not only as a natural way of doing business but also as pragmatically necessary" (para. 2). It ranks relationships higher than other ethical considerations, not excluding things like a company's code of conduct and the law. This concept scares many Western businesspeople because who are used to a different set of ethical standards. Westerners are taught and trained to rank obeying the law and following a company's code of conduct above relationships. Therefore, if ethics in China were compared to driving a car, Westerners would believe that the Chinese are driving on the "wrong" side of the road.

Since *guanxi* stems from the traditional Confucian belief of close bonding with one's family and group, a Chinese person's existence is defined by a bilateral relationship with another person, and Chinese people operate collectively, having close relationships with their immediate groups, and those out of this network are considered as strangers unless they are referred by someone trusted in the group (Lee and Dawes, 2005). Based on their social networks, Chinese users normally tend to seek suggestions or opinions from their social groups instead of acting individually and they prefer to use indirect and implicit communications with others. When learning about *guanxi*, many Western businesspeople automatically consider it a form of corruption and take the position that it will not be tolerated in their company.

Although it is easy to think the solution is to simply forbid Chinese employees from honoring *guanxi*, this is not always practical. Western businesses must remember that *guanxi* is deeply rooted in Chinese business culture, and business ethics in China are founded upon it. It is also important to note that *guanxi* does not give an individual permission to steal. Moderation must be observed because when moderate amounts are exceeded, the acts are seen as illegal and unethical; in fact, there are even limits to the obligations as a result of relationships.

Western companies with operations in China must accept that there will be some ideals and norms that are uncommon to them that they will be subject to. Burton and Stewart (2008) believe that while China is "utterly different", this does not mean that it is corrupt. The Chinese see Western ethics as strange, just as we see theirs as strange. They suggest that businesses acknowledge *guanxi* as part of the culture and that they

set boundaries in which it can be practiced. Although *guanxi* is deeply rooted in China, business there is starting to reflect Western and foreign norms. But Western companies should not expect China to abandon their values. It will take the participation of both Chinese and Western businesses to understand and control *guanxi*.

White-collar crimes in China

With all the advantages of doing business in China, it is important to remember that there can be many downfalls. China has its own unique business environment, and understanding the complexities of the social, legal, and political environment is crucial for any business looking to succeed there. One major concern in China's business community is the enormous number of various white-collar crimes. Part of the white-collar crime problem stems from the government itself, both the corruption of the Communist Party and actual government officials' personal involvement in individual crimes. The government is also responsible for inconsistencies in the level of punishment for crimes. One indication of the severity of white-collar crime in China is the increasing amounts of money involved in these crimes.

Before looking at some examples of white-collar crimes committed by individuals in China, the strategy used to deal with these crimes will be discussed. Control at the first level (political) takes place in the CCP. The Central Committee of Supervision and Discipline was created in 1979 and is in charge of investigating and disciplining officials' criminal behavior. This committee also determines if an individual is to be turned over to the criminal justice system for further investigation. If this does occur, the second level of control (legal) takes over and the government agency in charge is the Prosecution Department of China, which also has corresponding local departments and agencies. The third level of control is more recent and basically relates to administrative measures (e.g. reduce the size of the central government).

While it is not possible to review all of the recent cases of white-collar crime in China, it will be beneficial to provide a summary of some more recent cases, and the punishments given to the perpetrators of these economic crimes. Cha (2007) notes that as China moves from a planned economy to a free-market system, cracking down on fraud, embezzlement and other financial crimes has become a major priority for the government. Among the cases taken most seriously are the ones that harmed common people. Some examples that have been reported in the media:

- Two former employees of China Construction Bank, Zhou Limin and Liu Yibing, were executed for defrauding bank customers out of approximately \$50 million by offering bogus accounts they said would earn high interest rates (*Sawf-News*, 2006).
- A leading Chinese oil executive, Li Rongxing, was given the death sentence for embezzling more than \$4 million and taking \$620,000 in bribes (Cha, 2007).
- The former chief of the State Food and Drug Administration, Zheng Xiaoyu, was sentenced to death for accepting bribes of nearly \$850,000 to approve faulty medicines that killed at least six patients (Cody, 2007).
- A small business owner, Wang Zhendong, sold overpriced ant farms to the public as part of a giant scam (\$387 million) and was given the death penalty for his crimes (Reuters, 2007).

Each of the above cases resulted in a death sentence for the perpetrator. The government defended the use of the death penalty for financial crimes, which have risen as unscrupulous people attempt to take advantage of the booming economy. Supreme People's Court President Xiao Yang told the audience at a death penalty criminal law conference: "It is necessary to use the death penalty in China to punish criminals who commit extremely serious crimes in order to safeguard state security, public interests and smooth operation of economic construction" (Cha, 2007, para. 11).

All fraud cases do not result in a death sentence but it is becoming clear, at least from these cases, that the government is making an attempt to protect the public's interest. Other cases have also meted out harsh penalties for the perpetrators while stopping short of a death sentence. For example:

- A corrupt banker, Yu Zhendong, was sentenced to 12 years in prison for embezzlement and money laundering. Yu had fled to the USA after committing his crimes and returned to China based on the promise that he would not be executed for his offenses. Yu was the first corrupt Chinese official to be repatriated since China ratified the United Nations Convention Against Corruption (Xinhua, 2006).
- One of China's wealthiest businessmen, Zhang Rongkun, was sentenced to 19 years in prison for his involvement in a social security fund scandal. Zhang received over \$25 million that was embezzled from Shanghai's social security fund. He was also convicted of bribing government officials with over \$4 million (*China Daily*, 2008).

To put things in perspective, Bernie Ebbers (former CEO of WorldCom) and Jeff Skilling (former CEO of Enron) were given the harshest sentences ever for a white-collar crime in the USA (25 and 24 years, respectively). These are significant changes in the US sentencing of white-collar criminals as former perpetrators like Michael Milken served short sentences (Milken served less than two years) and often walked out of prison as wealthy individuals (Milken was said to have a fortune of approximately \$500 million when he was released from prison).

The current state of white-collar crime in China

Wu Heping, a spokesman for China's Public Service Bureau, says economic crimes rose more than 4 percent last year to more than 84,000 cases. He says that economic crimes have reached a new peak. In recent years with China's fast economic development, economic crimes have been climbing higher every day (Schearf, 2008). It should be noted, however, that due to the illicit nature of corrupt activities, it is all but impossible to determine the "true" figures for economic crimes.

This growth in corruption is not breaking news to the people in China. China's Prime Minister, Wen Jiabao, may have put it best in February 2006 when he said: "Bribery has poisoned the ethos of administrative, industrial, and social practices and has become a plague" (Plafker, 2007, p. 239). Surveys among government officials and everyday citizens point to corruption as one of their top concerns. From 1999 to 2004, officials studying at the CCP's Central Party School have continuously listed corruption as the most serious or the second most serious social problem.

Transparency International, a Berlin-based non-governmental organization, releases an annual Corruption Perception Index, which orders the nations of the

world according to the degree of corruption among government officials; China consistently ranks among the most corrupt nations in the world. From 1996 to 2005, annual audits performed by China's National Audit Agency "uncovered 1.29 trillion yuan (\$170 billion) in misappropriated and misspent public funds (illegal practices include overstating the number of staff, setting up slush funds, misappropriating special funds, and collecting illegal fees)" (Pei, 2007, para. 5).

In an interview with Tommy Seah, a professor of economics, chartered banker, certified fraud examiner and expert on fraud in the Chinese economy, a question was raised dealing with the overall rate of fraud in China relative to the USA. Mr Seah's response was: "I believe the rate of fraud in China is greater. You have an oppressed people who are suddenly given some autonomy over economic decision making. The burgeoning economy in China means more opportunities to commit fraud" (p. 36). Mr Seah went on to say that although most businesses in China operate honestly, dishonest executives can "cook the books" just like their US counterparts.

Conclusion

As China plays a more important role in the development and integration of today's global economy, it is engaged in exploring a unique means of combining socialism and capitalism in order to seek an alternative approach to prosperity. The world, which is composed of a plethora of different cultures, will be further enriched if the presence of a rapidly growing Chinese economy continues contributing to the globalized economy and the Chinese culture can co-exist with other nations whose citizens may have different philosophical and ethical perceptions and understandings. Simply neglecting or rejecting the uniqueness or dissimilarities of other cultures with regard to how social opinions are governed and disseminated is likely to result in erroneous perceptions and/or misunderstandings. This, in turn, may hinder organizations and/or nations from effectively and efficiently communicating and cooperating with their foreign business partners.

Understanding why white-collar crime is so rampant in China can be difficult for people in Western societies like the USA because the cultures and histories are so different and often misunderstood. In China, many of these crimes are often regarded as a socially acceptable way for employees to prepare for retirement or to keep up with the spending of their peers. This type of logic is so foreign to people who don't understand at least some of the culture that drives ethics in China. Thus, it is inappropriate to simply to translate or impose Western ethical standards on Chinese individuals; in fact, it is a methodical mistake to do so because China has a different set of ethical beliefs.

Bhasin (2007) recently pointed out that appropriate adjustments need to be made before any foreign company enters the Chinese market because of the differences in culture, language, religion, and jurisdiction, etc. It is also apparent that the white-collar-crime-related sentences handed down are completely different. Wang Zhendong and others were sentenced to die for their crimes. In the USA, it is unimaginable that someone would receive the death penalty for committing a white-collar crime. Despite the threat of being sentenced to death, crimes continue. Professor Tommy Seah (p. 36) suggests that "Although the penalty for white-collar crime is more severe in China than America, the Chinese see fraud as an opportunity to break out of the chain of poverty. Lots of Chinese people have now traveled

internationally; they see the good life capitalism brings, and may be impatient to get rich quickly. Some see no shame in committing fraud because they believe they are just getting back what was theirs in the first place”.

In an effort to examine white-collar crime in a rapidly growing economy like China, and make comparisons to Western societies from the perspective of philosophical and ethical dissimilarities, this article has implications for both practice and research. From a practical standpoint, it provides insights into possible areas of disagreement between employees from different cultures than can result from their divergent opinions about individuals' responsibility for fraudulent acts. With respect to research implications, additional focus should be placed on examining how cultural differences affect judgments and behaviors.

One thing is abundantly clear: Western businesses planning to enter the Chinese market need to do their due diligence before committing resources. What works in Western society may not work in another culture, like China's. However, gaining an understanding of the culture and general way of life will go a long way towards laying the groundwork for success.

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