

Analysis of Motivations Behind Corruption Among Senior Executives in State-Owned Enterprises

Zhoupei Yang *, Yulu Han

Chengdu University Chengdu 610106, China2Huaqiao University, Xiamen 361000, China

Abstract: Frequent corruption cases involving senior executives in state-owned enterprises (SOEs) are showing a new trend shifting from individual corruption to group corruption, causing significant losses to the national economy. Taking the 2022 corruption case of Kunming Steel Holding Co., Ltd., reported by the Central Commission for Discipline Inspection and the National Supervisory Commission, as an example, this paper analyzes the motivations behind SOE senior executives' corruption from an institutional perspective. The analysis finds that the motivations for corruption among SOE executives are inherent in natural institutional flaws. The interaction between incentive failures and lack of constraints caused by these institutional defects ultimately leads to executives having motives to engage in corrupt behavior. Therefore, establishing a transparent internal information disclosure system is an effective measure to improve internal supervision mechanisms; strengthening legal constraints, rigorous government oversight, and comprehensive media supervision are important steps to enhance external supervision; actively promoting market-oriented reforms and building a professional manager market are necessary to reduce corruption motivations among SOE executives; breaking the culture of centralized corporate control is crucial for preventing corruption.

Keywords: SOE senior executives; Corruption; Corporate governance.

1. Introduction

State-owned enterprises (SOEs) are the backbone of the national economy, playing a vital role in key industries such as petroleum, chemicals, machinery, electronics, metallurgy, and building materials. However, the corporate governance system of SOEs remains imperfect, and corruption among senior executives is an extreme manifestation of governance failure. In the highly publicized 2021-2022 corruption case involving Kunming Steel Holding Co., Ltd., the corruption network of senior executives extended across various stages, including procurement, distribution, advertising, and even restructuring. Following investigations and evidence collection, over thirty corrupt individuals from top to lower levels led by the former chairman Du Lujun were all apprehended.

The motivation behind corruption by SOE senior executives fundamentally arises from the combined effects of incentive failure and lack of supervision. Restrictions on SOE executives' salaries have caused their relative compensation to fail as an effective incentive. The unique dual agency mechanism and highly centralized organizational structure in SOEs grant executives both decision-making control and management authority. Excessive power coupled with insufficient incentives ultimately heightens the motivation for corruption among SOE senior executives.

2. Theoretical Background

Corruption among senior management takes diverse forms, including but not limited to bribery, kickbacks, unauthorized transfer of company assets, embezzlement of funds, misappropriation, extravagant spending, securing excessive compensation, and building personal business empires. Scholars both domestically and internationally have adopted various classification methods to study this issue. Chinese scholar Huang Qunhui (2005) [1] categorizes executive

corruption into transactional and non-transactional types. Transactional corruption involves executives abusing control rights through actions such as related-party transactions, bribery, and soliciting kickbacks. Non-transactional corruption refers to direct acts such as embezzlement, misappropriation, and occupational theft. Furthermore, executive corruption can be divided into latent and overt types. Latent corruption involves executives engaging in rent-seeking through covert but legal means, such as lavish consumption, building business empires, and obtaining high salaries. Overt corruption includes acts that violate regulations or laws, such as embezzlement, bribery, and related-party transactions. Executive corruption essentially represents rent-seeking behavior where executives exploit their control rights to breach fiduciary duties for personal gain. While granting executives control can improve decision-making efficiency, it also increases the risk of rent-seeking. Empirical research by domestic and foreign scholars has found that greater executive power correlates with a higher probability of corruption. With the deepening of government decentralization policies, SOEs face increased risks of executive rent-seeking. Xu Xixiong and Liu Xing (2013) [2] found that the greater a CEO's power, the higher the likelihood of corruption, and that state-controlled listed companies experience more frequent executive corruption than private firms. Hu Mingxia and Gan Shengdao (2015) [3] empirically analyzed the relationships among management power, internal controls, and executive corruption, similarly concluding that stronger management power increases corruption risk, whereas high-quality internal controls help suppress it. Since the 1980s, decentralization policies have significantly strengthened executives' power, creating more opportunities and space for corruption. As these policies have progressed, corruption has become more widespread and severe, especially in SOEs. Therefore, identifying the root causes of executive corruption is of critical practical significance for effectively preventing and punishing such

behavior.

Executive corruption occurs when management, in the absence of effective supervision, exploits their control rights to engage in rent-seeking for personal gain. Therefore, analyzing the causes of executive corruption should start from its essence: the excessive concentration of executive power primarily results from incomplete checks and balances within the agency system. The agency system is widely applied in corporate governance, and under conditions of information asymmetry and inefficient regulation, conflicts between agents and principals intensify, creating opportunities for executives to engage in rent-seeking. Scholars generally agree that executive corruption stems from weaknesses in corporate governance mechanisms. When there is a misalignment between incentives provided by compensation contracts and executives' actual performance contributions, corruption tends to become more severe. This issue is particularly pronounced in state-owned enterprises (SOEs), where long-term salary controls restrict executives' compensation and become a major motivation for corruption. Empirical studies by Chen Xinyuan and Chen Donghua (2009) [4], as well as Xu Xixiong and Liu Xing (2013) [2], confirm that salary controls indeed worsen corruption among SOE executives. Additionally, during the market economy transition, SOE executives often shoulder multiple policy-driven tasks, causing enterprises to face diversified objectives. This multiplicity blurs the causal relationship between business performance and management, creating conditions and space for executives to shirk responsibilities after engaging in rent-seeking (Chen Donghua et al., 2005) [5]. Furthermore, government intervention provides SOEs with a safety net when they encounter operational difficulties, and government budgets offer excuses for executives to evade accountability following corruption.

3. Research Design and Case Overview

(1) Method Selection

This study adopts a single case study approach, selecting the highly publicized Kunming Steel (Kunsteel) corruption case from 2021-2022 as the research subject. The case involves numerous individuals and has a significant impact, making it highly representative.

(2) Case Overview

The development of any entity and the emergence of its problems are rooted in specific environments and contexts. This section provides a detailed description of the Kunming Steel Group's development, followed by an in-depth explanation of the Kunsteel corruption case.

Kunming Iron and Steel Holding Co., Ltd. was established in February 1939, headquartered in Anning City, located in the southwestern suburbs of Kunming, known as the "Spring City." After the founding of the People's Republic of China, the dawn of hope illuminated the land. Despite the turmoil of war and chaos, Kunming Steel (Kunsteel) began its journey toward growth and expansion. At that time, the nation was poised for widespread development. Kunsteel actively launched vigorous patriotic labor competitions, resulting in unprecedented production momentum. With strong support from the central government and local provincial and municipal authorities, Kunsteel successively completed the construction of its No. 2 and No. 3 blast furnaces with a capacity of 210 cubic meters, and the No. 4 blast furnace of 255 cubic meters. A series of steelmaking and rolling production lines were put into operation. In the following

years, Kunsteel gradually phased out outdoor operations and manual material feeding, ending the era of using coal coke and raw ore for ironmaking. A steel plant with a production capacity of 500,000 tons initially took shape. Beginning in 1978, China's reform and opening-up policy gathered momentum, nourishing the country's development. In 1999, Kunsteel restructured into Kunming Iron and Steel Group Co., Ltd., making substantive progress in establishing a modern enterprise system. In 2002, Kunsteel was listed among China's top 500 enterprises for the first time. By 2004, it became Yunnan Province's first state-owned enterprise to achieve annual sales exceeding 10 billion yuan. Driven by a spirit of struggle, Kunsteel has continually surpassed its past to pioneer the future. Keeping pace with the times, it bases itself on pragmatism, pursues innovation as the source of development, and strives for excellence. Rooted in Yunnan, Kunsteel responds to the market with high-quality products and services. It has addressed excess capacity, vigorously developed emerging industries, and evolved into a large-scale state-owned enterprise group integrating traditional industries such as steel and cement with modern logistics, energy conservation and environmental protection, new materials, advanced equipment manufacturing, and modern services. Kunsteel is one of China's super-large industrial enterprises and a member of the Top 500 Chinese Enterprises, as well as the largest integrated steel production base in Yunnan Province.

In April 2021, a total of 31 individuals, ranging from the former chairman Du Lujun to workshop employees in subsidiary companies of Kunming Steel, were investigated. Public records show that Du Lujun was born in December 1970 in Xuanhan, Sichuan Province, and holds a postgraduate degree. He began working at Kunsteel's Qiaogang Plant in 1993, serving successively as a finance department staff member, deputy head of the labor and wage department, and head of the finance department. From 2004 onward, Du held several positions at Kunsteel, including Chief Financial Officer and General Manager of Kunsteel Group. In April 2019, he was appointed Party Secretary and Chairman of Kunsteel Group. The disciplinary notice of his "double dismissal" (removal from party and public office) highlighted that Du lost his ideals and beliefs, showed no party principles or sense of reverence, and experienced a collapse of his "three views" (worldview, outlook on life, and values). His desires grew unchecked, and he broke moral boundaries by using public power as a tool for personal gain and treating state-owned assets as a "toy" to manipulate at will. His lifestyle was extravagant, involving close relations and improper dealings with private business owners, willingly becoming "hunted." After the 18th National Congress of the Communist Party of China, he did not restrain himself, and especially after the 19th Congress, he continued to engage in power-for-money transactions without remorse. The expressions about the collapse of the "three views" and treating state assets as toys are notably rare. The notice also pointed out that Du falsified financial data and exhibited a lax work attitude, resulting in Kunsteel's heavy debt burden and operational difficulties. Kunming Steel Holding Co., Ltd.'s liabilities have steadily increased in recent years, rising from 39.7 billion yuan in 2017 to 41.271 billion yuan in 2018, reaching 45.586 billion yuan in 2019, and 46.153 billion yuan by the end of the third quarter of 2020.

(3) Data Collection

As a publicly listed company, Kunsteel Group's annual

reports and other documents provide the author with relatively complete secondary data. The case data in this study primarily come from the following sources: First, websites such as Luobo Research, Kunsteel's official website, and government portals; Second, Kunsteel's annual reports; Third, academic journal articles and related literature; Fourth, data compiled and organized by the author based on collected materials.

4. Case Analysis and Findings

(1) Failure of Compensation Incentives

Improper executive compensation design can partly contribute to corruption among senior managers in state-owned enterprises (SOEs). Classic studies provide insights into the relationship between pay structure and executive behavior. Jensen and Murphy (1990) [6] pointed out that compensation design significantly influences executive incentives and actions. When incentive mechanisms are ineffective, executives may resort to illegal means to gain extra income, triggering corruption. Bebchuk and Fried (2003) [7] emphasized the agency problem in executive pay, where executives may pursue personal interests at the expense of the company. If compensation is non-transparent, unfair, or disconnected from company performance, executives might abuse power or embezzle funds for personal gain. Frydman and Saks (2010) [8] offered a long-term perspective, showing that flawed pay structures can distort short-term behavior and weaken long-term competitiveness, increasing executives' vulnerability to corruption temptations.

Synthesizing these findings, unreasonable compensation structures in SOEs like Kunsteel may encourage corrupt behavior. Therefore, establishing a transparent, fair, and performance-linked compensation mechanism can reduce the risk of executive corruption and improve corporate governance.

(2) Failure of Political Promotion Incentives

For SOE executives, given the relatively low monetary pay and equity incentives, political promotion serves as the most effective motivation. Yan Changle proposed that for SOE managers, company performance relates not only to compensation but also to their political capital. The motivation for political promotion among SOE executives differs significantly from that of private entrepreneurs seeking political titles like People's Congress representatives or CPPCC members to build political connections and gain economic benefits for their companies. While SOE executives also value company performance, it primarily serves as a criterion for their political advancement. Compared with private entrepreneurs, political promotion is a stronger incentive for SOE executives.

In SOEs, company performance acts as a "catalyst": when performance is good, executives can achieve political promotion despite inadequate monetary incentives; however, when the company struggles and executives fail to deliver strong results—especially near retirement—political promotion opportunities diminish. Without the prospect of political advancement, executives may become disillusioned, which fosters motives for corruption such as embezzlement and bribery.

5. Conclusion

In the Kunsteel corruption case, political factors had a profound impact on corporate decision-making. Political interference and the bureaucratic system made executives more inclined to appease their political superiors, leading to resource allocation and contract signing being influenced by political connections. This created opportunities for corrupt behavior, especially when political considerations took precedence over corporate performance. Furthermore, state-owned enterprises often operate in monopolistic industries with little market competition. This lack of competitive pressure may reduce executives' focus on performance and efficiency, weakening the sense of urgency and responsibility in management, thereby creating conditions conducive to corruption. Issues with the personnel appointment system also contribute to the lack of executive accountability. Senior leadership appointments are often closely tied to political relationships rather than professional qualifications or performance. This can result in incompetent or irresponsible individuals occupying leadership positions, increasing the risk of corruption. Additionally, the absence of effective supervision mechanisms and transparency provides fertile ground for corruption. Although SOEs are supervised by government or party committees, institutional deficiencies may exist within these regulators. A lack of transparency in financial reporting and operations makes it easier for corrupt activities to be concealed. Finally, the absence of proper incentive mechanisms causes executives to lack motivation for performance. Without sufficient incentives and clear penalties, executives may not feel a pressing responsibility for corporate performance, further raising the risk of corruption.

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